IMPORTANT NOTICE

You must read the following disclaimer before continuing

THIS DOCUMENT MAY NOT BE FORWARDED OR DISTRIBUTED TO ANY OTHER PERSON AND MAY NOT BE REPRODUCED IN ANY MANNER WHATSOEVER, AND IN PARTICULAR, MAY NOT BE TRANSMITTED INTO OR DISTRIBUTED WITHIN THE UNITED STATES.

The following disclaimer applies to the Prospectus attached following this notice and you are therefore required to read this disclaimer page carefully before reading, accessing or making any other use of the Prospectus. In accessing the Prospectus, you agree to be bound by the following terms and conditions, including any modifications to them from time to time, each time you receive any information from us as a result of such access.

NOTHING IN THIS ELECTRONIC TRANSMISSION CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN ANY JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE BONDS HAVE NOT BEEN, AND WILL NOT BE, REGISTERED UNDER THE SECURITIES ACT, OR THE SECURITIES LAWS OF ANY STATE OF THE U.S. OR ANY OTHER JURISDICTION AND THE BONDS MAY NOT BE OFFERED OR SOLD WITHIN THE U.S. OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS (AS DEFINED IN REGULATION S UNDER THE SECURITIES ACT), EXCEPT PURSUANT TO AN EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND APPLICABLE STATE OR LOCAL SECURITIES LAWS.

The Prospectus has been sent to you in electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of transmission and consequently the Manager (or any person who controls it or any director, officer, employee or agent of it, or affiliate of any such person) accepts no any liability or responsibility whatsoever in respect of any difference between the document distributed to you in electronic format and the hard copy version available to you on request from us.

You are reminded that the Prospectus has been delivered to you on the basis that you are a person into whose possession the Prospectus may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located and you may not nor are you authorised to deliver the Prospectus to any other person.

By accessing the Prospectus, you shall be deemed to have confirmed and represented to us that (a) you have understood and agree to the terms set out herein, (b) you consent to delivery of the Prospectus by electronic transmission, (c) you are not a U.S. person (within the meaning of Regulation S under the Securities Act) or acting for the account or benefit of a U.S. person and the electronic mail address that you have given to us and to which this e-mail has been delivered is not located in the United States, its territories and possessions (including Puerto Rico, the U.S. Virgin Islands, Guam, American Samoa, Wake Island and the Northern Mariana Islands) or the District of Columbia and (d) if you are a person in the United Kingdom, then you are a person who (i) has professional experience in matters relating to investments or (ii) is a high net worth entity falling within Article 49(2)(a) to (d) of the Financial Services and Markets Act (Financial Promotion) Order 2005.

Prospectus dated 23 February 2017

Uliving@Essex Issuerco PLC

(incorporated with limited liability in England under company number 10546935)

£98,200,000 0.100 per cent. Index-Linked Guaranteed Secured Bonds due 31 August 2058 pursuant to financial guarantees issued by

ASSURED GUARANTY®

ASSURED GUARANTY (EUROPE) LTD.

(incorporated with limited liability in England and Wales under company number 02510099)

and

ASSURED GUARANTY MUNICIPAL CORP.

(a stock insurance company organised under the laws of the State of New York, United States of America)

Issue Price: 100 per cent.

TradeRisks Limited

The £98,200,000 0.100 per cent. index-linked guaranteed secured bonds due 31 August 2058 (the "**Bonds**" or "**Bonds**")) of Uliving@Essex Issuerco PLC (the "**Issuer**") will be issued pursuant to a bond trust deed to be dated 24 February 2017 (as amended or supplemented from time to time, the "**Bond Trust Deed**") among the Issuer, Assured Guaranty (Europe) Ltd. ("**AGE**"), Assured Guaranty Municipal Corp. ("**AGM**" and together with AGE, the "**Financial Guarantors**") and BNY Mellon Corporate Trustee Services Limited as bond trustee (the "**Bond Trustee**", which expression includes the trustee or trustees for the time being under the Bond Trust Deed). The issue price will be 100 per cent. The Bonds (excluding those held by or on behalf of any Obligor or any Affiliate of an Obligor or Shareholder of an Obligor) will be unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest (adjusted for indexation in accordance with the terms and conditions of the Bonds (the "**Conditions**")) in respect of the Bonds (excluding in each case any amounts due in respect of the Bonds (i) attributable to any increase in interest margin, penalty or other sum payable by the Issuer for whatever reason; (ii) attributable to any present or future taxes, duties, withholding, deduction, assessment or other charge (including interest and penalties in respect of such taxes, duties, withholding, deduction, assessment or other charge) of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state (including the United Kingdom), or any political subdivision or governmental or taxing authority therein or thereof; (iii) attributable to any default interest; (iv) attributable to any amount relating to prepayment, early redemption, broken-funding indemnities, penalties, premium, spens, any make-whole amount or similar types of payments payable in respect of the Bonds; or (v) in respect of which AGM or AGE has made an Accelerated Payment (as defined in the relevant Financial Guarantee) on or prior to a Scheduled Payment Date) in accordance with a financial guarantee to be issued by AGE (the "**AGE Financial Guarantee**") and as set out in the section entitled *Form of AGE Financial Guarantee* below and a financial guarantee to be issued by AGM (the "**AGM Financial Guarantee**", and together with the AGE Financial Guarantee, the "**Financial Guarantees**" and each a "**Financial Guarantee**") and as set out in the section entitled *Form of AGM Financial Guarantee* below.

Interest on the Bonds (adjusted for indexation) will be payable semi-annually (the "**Scheduled Interest**") in arrear on 28 February (or 29 February in each leap year) and 31 August in each year (each a "**Scheduled Payment Date**").

Unless previously redeemed or purchased and cancelled, the Bonds will mature on 31 August 2058 and will be subject to redemption in part from, and including, 28 February 2017, in accordance with the amortisation schedule set out in the section entitled *Terms and Conditions of the Bonds - Payments and Exchange of Talons - Scheduled Payments*. The Bonds are also subject to redemption in whole but not in part, at the Early Redemption Amount (as defined below), at the option of the Issuer (as provided in Condition 6 (see the section entitled *Terms and Conditions of the Bonds - Redemption and Purchase - Redemption at the option of the Issuer* below) or at the Indexed Par Amount (as defined below), in the event of certain changes affecting the Index (as defined in Condition 7 (*Indexation*)) (see the section entitled *Terms and Conditions of the Bonds - Redemption and Purchase - Redemption for Index Reasons*) below).

The Issuer is a special purpose vehicle whose principal purposes are, inter alia, to issue the Bonds, and to on-lend the proceeds to Uliving@Essex Limited ("**ProjectCo**"), pursuant to an issuer on-loan agreement (see the section entitled "*Refinancing of the Project"*). ProjectCo is a special purpose vehicle that was established for the principal purpose of (i) designing, building and maintaining new student accommodation for the University in the Meadows area of the University of Essex (the "**Meadows Premises**", (ii) acquiring the existing University accommodation known as the Quays (the "**Quays Premises**", together with the Meadows Premises, the "**Accommodation**" and (iii) providing associated facilities and amenities at the Accommodation. Uliving@Essex HoldCo Limited ("**HoldCo**" and together with the Issuer, and ProjectCo, the "**Obligors**") is a special purpose vehicle established for the principal purposes of acting as the holding company of the Issuer and ProjectCo.

Equitix Education 2 Limited ("**Equitix Education**") is the legal and beneficial owner of 85% of the issued shares of HoldCo. Centro Place Investments Limited ("**Centro**") is the legal and beneficial owner of 15% of the issued shares of HoldCo and together with Equitix Education, the "**Shareholders**" and each a "**Shareholder**"). Derwent Housing Association Limited ("**Derwent**") is the legal and beneficial owner of 100% of the issued shares of Centro. There is no recourse to the Shareholders except to the extent described in this Prospectus.

The obligations of the Issuer under the Bonds will be secured in favour of BNY Mellon Corporate Trustee Services Limited as security trustee (the "**Security Trustee**") as described in the section entitled *Refinancing of the Project - The Security Arrangements* below. The Bonds are expected to be rated upon issue AA by Standard & Poor's Credit Market Services France S.A.S. ("**S&P**"). A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by S&P. A suspension, reduction or withdrawal of the rating assigned to the Bonds may adversely affect the market price of the Bonds.

The rating will be based solely upon the financial strength rating of AGE and AGM. Standard and Poor's Global Ratings Services ("**S&PGRS**") has assigned to AGE financial strength and financial enhancement ratings of AA (stable outlook) and Moody's Investors Service, Inc., ("**Moody's**") has assigned to AGE an insurance financial strength rating of A2 (stable outlook). S&PGRS has assigned to AGM financial strength and financial enhancement ratings of AA (stable outlook), Kroll Bond Rating Agency ("**KBRA**") has assigned to AGM an insurance financial strength rating of AA+ (stable outlook) and Moody's has assigned to AGM an insurance financial strength rating of A2 (stable).

S&P is established in the EU and registered under Regulation (EC) No 1060/2009, as amended (the "**CRA Regulation**"). None of S&PGRS, KBRA or Moody's is established in the European Community and none of them are registered in accordance with Regulation (EC) No 1060/2009 (as amended). Credit ratings issued by S&PGRS have been endorsed by S&P, credit ratings issued by Moody's have been endorsed by Moody's Investors Service Ltd and KBRA has been certified under the CRA Regulation.

The Prospectus has been approved by the Central Bank of Ireland (the "**Central Bank**"), as competent authority under Directive 2003/71/EC, as amended (the "**Prospectus Directive**"). The Central Bank only approves this Prospectus as meeting the requirements imposed under Irish and EU law pursuant to the Prospectus Directive. Application has been made to the Irish Stock Exchange for the Bonds to be admitted to the official list (the "**Official List**") and trading on its regulated market (the "**Main Securities Market**"). The Main Securities Market is a regulated market for the purposes of Directive 2004/39/EC (the "**Markets in Financial Instruments Directive**"). Such approval relates only to the Bonds which are to be admitted to trading on a regulated market for the purposes of Directive 2004/39/EC and/or which are to be offered to the public in any Member State of the European Economic Area.

The Bonds will be in bearer form and in the denominations of £100,000 and integral multiples of £1,000 in excess thereof. For so long as the Bonds are represented by a Global Bond (as defined below) and the relevant clearing system(s) so permit, the Bonds will be tradable in such denominations, subject always to a minimum denomination and trading amount of £100,000. There can be no assurance, however, that the relevant clearing system(s) will enforce such minimum trading amount. The Bonds will initially be in the form of a temporary global bond (the "**Temporary Global Bond**"), without receipts, coupons or talons attached, which will be deposited on or around 24 February 2017 (the "**Issue Date**") with a common safekeeper for Euroclear S.A./N.V. as operator of the Euroclear System ("**Euroclear**") and Clearstream Banking, Société Anonyme, Luxembourg ("**Clearstream, Luxembourg**"). The Temporary Global Bond will be exchangeable, in whole or in part, not earlier than 40 calendar days from (but not including) the Issue Date upon certification of non-U.S. beneficial ownership, for interests in a permanent global bond (the "**Permanent Global Bond**", together with the Temporary Global Bond, the "**Global Bonds**" and each a "**Global Bond**"), without receipts, coupons or talons attached. Interest payments in respect of the Bonds cannot be collected without such certification of non-U.S. beneficial ownership. The Permanent Global Bond will be exchangeable in whole, but not in part, for Bonds in definitive form (the "**Definitive Bonds**") in the denominations of £100,000 and integral multiples of £1,000 in excess thereof, with receipts for principal and coupons for interest and talons for further receipts or coupons attached, only in the limited circumstances described in the section *Summary of Provisions relating to the Bonds while in Global Form* below. If Definitive Bonds are required to be issued, such Definitive Bonds (a) will only be issued to Bondholders (as defined below) holding Bonds having a nominal amount equal to or in excess of £100,000 and (b) will only be printed in denominations equal to or in excess of £100,000 and to the extent in excess of £100,000 in integral multiples of £1,000.

An investment in the Bonds involves certain risks. Prospective investors should have regard to the factors described in the section entitled Risk Factors below.

IMPORTANT NOTICE

This Prospectus (which includes the appendices) comprises a prospectus with regard to the Issuer and the Bonds for the purposes of Article 5.3 of the Prospectus Directive and has been approved by the Central Bank acting in its capacity as competent authority.

The Issuer accepts responsibility for the information contained in this Prospectus. To the best of the knowledge of the Issuer (which has taken all reasonable care to ensure that such is the case), such information is in accordance with the facts and does not omit anything likely to affect the import of such information. The Issuer has accurately reproduced the ProjectCo Information, the Equitix Education Information, the Centro Information, the AGE Information and the AGM Information (each as defined below) and as far as the Issuer is aware and is able to ascertain from information published by ProjectCo, each Shareholder, AGE and AGM no facts have been omitted which would render the reproduced information inaccurate or misleading.

HoldCo accepts responsibility for the information in this Prospectus (i) under the heading *HoldCo* in the section entitled "*Description of the Issuer, HoldCo and ProjectCo* and paragraphs 5 and 10 of the section entitled *General Information*, and (ii) Appendix 7 (the "**HoldCo Information**"). To the best of the knowledge of HoldCo (which has taken all reasonable care to ensure that such is the case), such information is in accordance with the facts and does not omit anything likely to affect the import of such information.

ProjectCo accepts responsibility for the information in this Prospectus under (i) the heading *ProjectCo* in the section entitled *Description of the Issuer, HoldCo and ProjectCo* and in paragraphs 6 and 11 of the section entitled *General Information* and (ii) Appendix 6 (the "**ProjectCo Information**"). To the best of the knowledge of ProjectCo (which has taken all reasonable care to ensure that such is the case), such information is in accordance with the facts and does not omit anything likely to affect the import of such information.

Equitix Education accepts responsibility for the information in this Prospectus under the heading *Equitix Education 2 Limited* in the section entitled *Description of the Shareholders* (the "**Equitix**" "**Education Information**"). To the best of the knowledge of Equitix Education (which has taken all reasonable care to ensure that such is the case), such information is in accordance with the facts and does not omit anything likely to affect the import of such information.

Centro accepts responsibility for the information in this Prospectus under the heading *Centro Place Investments Limited* in the section entitled *Description of the Shareholders* (the "**Centro Information**"). To the best of the knowledge of Centro (which has taken all reasonable care to ensure that such is the case), such information is in accordance with the facts and does not omit anything likely to affect the import of such information.

C&W accepts responsibility for the information in this Prospectus under the heading Demand Report in Appendix 9 to this Prospectus. To the best of its knowledge (which it has taken all reasonable care to ensure that such is the case), such information is in accordance with the facts and does not omit anything likely to affect the import of such information. C&W has consented to the inclusion of its report in this Prospectus but investors should be aware that they do not accept any duty of care to any recipient of this Prospectus.

The information relating in this Prospectus to the Office for National Statistics and the United Kingdom Retail Price Index has been accurately reproduced from information published by that office. So far as the Issuer is aware and is able to ascertain from information published by the Office for National Statistics, no facts have been omitted which would render the reproduced information misleading.

The Demand Report by Cushman & Wakefield ("**C&W**") has been accurately reproduced in Appendix 8 to this Prospectus. So far as the Issuer is aware and is able to ascertain from information published by C&W, no facts have been omitted which would render the reproduced information misleading. C&W has consented to the inclusion of its report in this Prospectus but investors should be aware that they do not accept any duty of care to any recipient of this Prospectus.

AGE accepts responsibility for the information contained in this Prospectus (i) in the sections entitled "*Risk Factors – Risks Relating to the Financial Guarantors*", "*Description of the Financial Guarantors - Assured Guaranty (Europe) Ltd*" and "*Form of AGE Financial Guarantee*" and (ii) in Appendix 1 and Appendix 2 to this Prospectus (together, the "**AGE Information**"). To the best of the knowledge and belief of AGE (which has taken all reasonable care to ensure that such is the case), the AGE Information is in accordance with the facts and does not omit anything likely to affect the import of such information. AGE accepts no responsibility for any other information contained in this Prospectus. Save for the AGE Information, AGE has not separately verified the information contained herein. No representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by AGE as to the accuracy or completeness of any information contained in this Prospectus (other than the AGE Information) or any other information supplied in connection with the Bonds or their distribution. Each person receiving this Prospectus acknowledges that such person has not relied on AGE nor on any person affiliated with it in connection with its investigation of the accuracy of any information contained in this Prospectus (other than the AGE Information) or in making its investment decision.

AGM accepts responsibility for the information contained in this Prospectus (i) in the sections entitled "*Risk Factors – Risks Relating to the Financial Guarantors*", "*Description of the Financial Guarantors - Assured Guaranty Municipal Corp.* " and "*Form of AGM Financial Guarantee*" and (ii) in Appendix 3, Appendix 4 and Appendix 5 to this Prospectus (together, the "**AGM Information**"). To the best of the knowledge and belief of AGM (which has taken all reasonable care to ensure that such is the case), the AGM Information is in accordance with the facts and does not omit anything likely to affect the import of such information. AGM accepts no responsibility for any other information contained in this Prospectus. Save for the AGM Information, AGM has not separately verified the information contained herein. No representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by AGM as to the accuracy or completeness of any information contained in this Prospectus (other than the AGM Information) or any other information supplied in connection with the Bonds or their distribution. Each person receiving this Prospectus acknowledges that such person has not relied on AGM nor on any person affiliated with it in connection with its investigation of the accuracy of any information contained in this Prospectus (other than the AGM Information) or in making its investment decision.

The Issuer and ProjectCo have each confirmed to TradeRisks Limited (the "**Manager**") that this Prospectus contains all information regarding the Issuer, ProjectCo, the Project, the Finance Documents, the Project Documents and the Bonds which is material in the context of the issue of the Bonds; such information is true and accurate in all material respects and is not misleading in any material respect; any opinions or intentions expressed in this Prospectus are honestly held and are based on reasonable assumptions, this Prospectus does not omit to state any fact which would make any statement misleading in any material respect; and all reasonable enquiries have been made to ascertain and to verify the foregoing.

The Financial Guarantees will be issued on the Issue Date subject to certain conditions precedent being satisfied.

The Financial Guarantees have not been and will not be executed as at the date of this Prospectus.

No person has been authorised to give any information or to make representations other than the information or the representations contained in this Prospectus in connection with the Obligors, the University, the Financial Guarantors, or the issue or sale of the Bonds and, if given or made, such information or representations must not be relied upon as having been authorised by the Obligors or the Financial Guarantors, the Manager, the Bond Trustee, the Principal Paying Agent or the Security Trustee. Neither the delivery of this Prospectus nor the offering, sale or delivery of any Bond shall in any circumstances, create any implication that there has been no adverse change, nor any event reasonably likely to involve any adverse change, in the condition (financial or otherwise) of the Obligors or the Financial Guarantors since the date hereof. Unless otherwise indicated herein, all information in this Prospectus is given as of the date of this Prospectus.

The Manager, the Principal Paying Agent, the Bond Trustee and the Security Trustee have not separately verified the information contained in this Prospectus. Accordingly, no representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by

the Manager, the Principal Paying Agent, the Bond Trustee or the Security Trustee as to the accuracy or completeness of the information contained in this Prospectus or any other information supplied in connection with the Bonds or their distribution. The statements made in this paragraph are without prejudice to the respective responsibilities of the Obligors and the Financial Guarantors. Each person receiving this Prospectus acknowledges that such person has not relied on the Manager, the Principal Paying Agent, the Bond Trustee or the Security Trustee or on any person affiliated with any of them in connection with its investigation of the accuracy of such information or its investment decision.

None of the Obligors, the Manager, the Financial Guarantors, the Bond Trustee, the Security Trustee, the Principal Paying Agent or any other party named in this Prospectus accepts responsibility to investors for the regulatory treatment of their investment in the Bonds in any jurisdiction or by any regulatory authority. If the regulatory treatment of an investment in the Bonds is relevant to an investor's decision whether or not to invest, the investor should make its own determination as to such treatment and for this purpose seek professional advice and consult its regulator. Prospective investors are referred to the section entitled "*Risk Factors - Changes to the risk weighted asset framework*" of this Prospectus.

This Prospectus does not constitute, and may not be used for the purposes of, an offer or solicitation by any person to subscribe or purchase any Bonds. Neither this Prospectus nor any other financial statements are intended to provide the basis of any credit or other evaluation and should not be considered as a recommendation by any of the Obligors, the Financial Guarantors or the Manager that any recipient of this Prospectus or any other financial statements should purchase the Bonds. Each person contemplating making an investment in the Bonds must make its own investigation and analysis of the creditworthiness of the Obligors and the Financial Guarantors and its own determination of the suitability of any such investment, with particular reference to its own investment objectives and experience and any other factors which may be relevant to it in connection with such investment. A prospective investor who is in any doubt whatsoever as to the risks involved in investing in the Bonds should consult independent professional advisers. The Manager does not undertake to review the financial conditions or affairs of the Obligors or the Financial Guarantors during the life of the arrangements contemplated by this Prospectus, or to advise any investor or potential investor in the Bonds of any information coming to the attention of the Manager.

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (i) the Bonds are legal investments for it, (ii) the Bonds can be used as collateral for various types of borrowing and (iii) other restrictions apply to its purchase or pledge of the Bonds. Financial institutions should consult their legal advisors or the appropriate regulators to determine the appropriate treatment of the Bonds under any applicable risk-based capital or similar rules.

The distribution of this Prospectus and the offering, sale and delivery of the Bonds in certain jurisdictions may be restricted by law. The Issuer does not represent that the Bonds may at any time lawfully be sold in compliance with any applicable registration or other requirements in any jurisdiction, or pursuant to any exemption available thereunder, and does not assume any responsibility for facilitating such sale. Persons into whose possession this Prospectus comes are required by the Obligors, the Financial Guarantors and the Manager to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers and sales of the Bonds and on the distribution of this Prospectus, see the section entitled "*Subscription and Sale*" below. In particular, the Bonds, the Obligor Guarantees (as defined below) and the Financial Guarantees have not been and will not be registered under the United States Securities Act of 1933 (as amended) (the "**Securities Act**") and the Bonds will be in bearer form and so are subject to U.S. tax law requirements. Subject to certain exceptions, the Bonds, the Obligor Guarantees and the Financial Guarantees may not be offered, sold or delivered within the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act and in the U.S. Internal Revenue Code of 1986, as amended, and regulations thereunder). The Bonds are being offered outside the United States in accordance with Regulation S under the Securities Act. See the section entitled *Subscription and Sale* below.

All references herein to "**pounds**", "**sterling**", "**Sterling**" or "**£**" are to the lawful currency of the United Kingdom, all references to "**$**", "**U.S.$** ", "**U.S. dollars**" and "**dollars**" are to the lawful currency of the United States of America, and all references to "**€**", "**EUR**" or "**Euro**" are to the single currency

introduced at the start of the third stage of the European Economic and Monetary Union pursuant to the Treaty establishing the European Community, as amended.

SUPPLEMENTARY PROSPECTUS

If at any time the Issuer shall be required to prepare a supplementary prospectus pursuant to Article 16 of the Prospectus Directive, the Issuer will prepare and make available an appropriate amendment or supplement to this Prospectus or a further Prospectus which, in respect of any subsequent issue of Bonds to be listed on the Official List and admitted to trading on the Main Securities Market of the Irish Stock Exchange, shall constitute a supplementary prospectus as required by the Central Bank and Article 16 of the Prospectus Directive.

The Obligors have given an undertaking to the Manager that if at any time during the term of the Bonds there is a significant new factor, material mistake or inaccuracy relating to information contained in this Prospectus which is capable of affecting the assessment of any Bonds and whose inclusion in this Prospectus or removal is necessary, for the purpose of allowing an investor to make an informed assessment of the assets and liabilities, financial position, profits and losses and prospects of the Obligors, the Financial Guarantors and the rights attaching to the Bonds, the Issuer shall prepare an amendment or supplement to this Prospectus or publish a replacement Prospectus for use in connection with any subsequent offering of bonds and shall supply to the Manager such number of copies of such supplement hereto as the Manager may reasonably request. Each supplementary prospectus that is published will incorporate by reference any supplementary prospectus previously filed with the Central Bank.

TABLE OF CONTENTS

OVERVIEW OF THE BOND ISSUE

Terms defined in "Terms and Conditions of the Bonds" have the same meaning in this section.

Introduction:	The Issuer (as defined below) is a special purpose vehicle whose principal purposes are to issue the Bonds (as defined below), and on-lend the proceeds to Uliving@Essex Limited ("**ProjectCo**). ProjectCo is a special purpose vehicle whose principal purposes are to finance and operate elements of the accommodation for, and to provide certain services to, the University of Essex (the "**University**"). ProjectCo will use the proceeds of the loan from the Issuer in order to (i) fund the management, refinancing and operating costs and other expenditure (including fees, any refinancing gain, and incidental costs and expenses) in relation to the Project and (ii) to pay commission and expenses incurred in relation to the issue of the Bonds. Uliving@Essex HoldCo Limited ("**HoldCo**") is a special purpose vehicle established for the principal purpose of acting as the holding company of the Issuer and ProjectCo (and, together with the Issuer and ProjectCo, the **Obligors**"). Equitix Education 2 Limited ("**Equitix Education**") is the legal and beneficial owner of 85% of the issued shares of HoldCo. Centro Place Investments Limited ("**Centro**") is the legal and beneficial owner of 15% if the issued shares of HoldCo and together with Equitix Education, the "**Shareholders**" and each a "**Shareholder**"). Derwent Housing Association Limited ("**Derwent**") is the legal and beneficial owner of 100% of the issued shares of Centro. There is no recourse to any shareholders of HoldCo except to the extent described in this Prospectus. Pursuant to the terms of the Collateral Deed, the Obligors will grant a joint and several guarantee in respect of each other's obligations to the Senior Creditors (as defined below) under the Senior Finance Documents. The obligations of the Issuer under the Bonds will be secured in favour of BNY Mellon Corporate Trustee Services Limited as security trustee (the "**Security Trustee**") (each as described in the section entitled "*Refinancing of the Project — The Security Arrangements*"). Each of AGE and AGM has agreed to provide a separate Financial Guarantee in relation to the Bonds. The Financial Guarantees will unconditionally and irrevocably guarantee the payment of scheduled principal and interest (in each case adjusted for indexation) (except for Bonds held by or on behalf of any Obligor or any Affiliate of an Obligor or Shareholder of an Obligor). See "*Terms and Conditions of the Bonds*". The coverage provided by the Financial Guarantees is the payment of scheduled payments of principal and interest only and does not cover any amounts due in respect of the Bonds:

(i) attributable to any increase in interest margin, penalty or other sum payable by the Issuer for whatever reason;

(ii) attributable to any present or future taxes, duties, withholding, deduction, assessment or other charge (including interest and penalties in respect of such taxes, duties, withholding, deduction, assessment or other charge) of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state (including the United Kingdom), or any political subdivision or governmental or taxing authority therein or thereof;

(iii) attributable to any default interest;

(iv) attributable to any amount relating to prepayment, early redemption, broken-funding indemnities, penalties, premium, "spens", any make-whole amount or similar types of payments payable in respect of the Bonds; or

(v) in respect of which AGM or AGE has made an Accelerated Payment (as defined in the relevant Financial Guarantee) on or prior to a Scheduled Payment Date.

See "*Form of AGE Financial Guarantee*" and "*Form of AGM Financial Guarantee*".

Issuer:	Uliving@Essex Issuerco PLC
Issue:	£98,200,000 0.100 per cent. index-linked guaranteed secured bonds due 31 August 2058 (the "**Bonds**").
Issue Price:	100 per cent.
Manager:	TradeRisks Limited
Final Maturity:	31 August 2058
Financial Guarantors:	Assured Guaranty (Europe) Ltd. and Assured Guaranty Municipal Corp.
Interest and Redemption:	Payments of interest and principal will be due on the Bonds as set out in "*Terms and Conditions of the Bonds — Payments and Exchange of Talons*".
Indexation:	All payments of principal and interest in relation to the Bonds will be indexed using the RPI(0,6) Index Ratio (as defined in Condition 7 (*Indexation*)).
Financial Guarantees:	The Bonds (excluding those held by or on behalf of any Obligor or any Affiliate of an Obligor or Shareholder of an Obligor) will have the benefit of the Financial Guarantees under which (i) AGE has unconditionally and irrevocably agreed to pay to the Bond Trustee 8 per cent. of all sums due and payable but unpaid by the Issuer in respect of scheduled principal and interest on the Bonds and (ii) AGM has unconditionally and irrevocably agreed

	to pay to the Bond Trustee (x) the remaining 92 per cent. of the aforementioned sums, and (y) any sums due and payable but unpaid by AGE, all as more particularly described in the Financial Guarantees.
Reimbursement and Indemnity Deed:	The Obligors will be obliged to reimburse the Financial Guarantors, in respect of payments made under the relevant Financial Guarantee pursuant to the Reimbursement and Indemnity Deed. In addition, the Financial Guarantors will be subrogated to the rights of the Bondholders and the Bond Trustee (as described below) in respect of any payments made by it under the relevant Financial Guarantee.
Status of Bonds:	The Bonds will constitute direct and secured obligations of the Issuer which will rank *pari passu* and rateably without any preference or priority among themselves and will rank in priority to all unsecured obligations of the Issuer, save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.
Status of Financial Guarantees:	The AGE Financial Guarantee will constitute a direct and unsecured obligation of AGE which will rank at least *pari passu* with all other unsecured obligations of AGE save for such obligations as may be preferred by provisions of law that are both mandatory and of general application. The AGM Financial Guarantee will constitute a direct and unsecured obligation of AGM which will rank at least *pari passu* with all other unsecured obligations of AGM save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.
Financial Guarantor Downgrade Event:	A "**Financial Guarantor Downgrade Event**" means if at any time while the Bonds remain outstanding, both: (i) AGM's insurer financial strength rating by Moody's ceases to be at least "Baa3" and (ii) AGM's insurer financial strength rating by Standard & Poor's Global Ratings Services ("**S&PGRS**") ceases to be at least "BBB-"; provided, that during such time as AGM's insurer financial strength is not rated by either Moody's or S&PGRS, then a "Financial Guarantor Downgrade Event" means at any time while the Bonds remain outstanding, that AGM's insurer financial strength rating is not rated at least "BBB-" or the equivalent by at least one other credit rating agency which is registered with the United States Securities and Exchange Commission as a nationally recognized statistical rating organization (such rating agency during such time, an "**Alternative Rating Agency**"). If a Financial Guarantor Downgrade Event has occurred and is continuing, then the Issuer shall notify the Bondholders and the Bond Trustee that a Financial Guarantor Downgrade Event has occurred and of their rights pursuant to and in accordance with the Bond Trust Deed and the Conditions. If directed by Bondholders acting by way of an Extraordinary Resolution, the Bond

Trustee shall, subject to being prefunded and/or indemnified and/or secured to its satisfaction by the Bondholders, issue a notice (the "**Financial Guarantor Removal Notice**") to the Financial Guarantors specifying that, unless the Financial Guarantor Downgrade Event has been remedied or waived by the date that is three calendar months after the date of delivery of the Financial Guarantor Removal Notice (the "**Financial Guarantor Removal Date**"), each of the Financial Guarantees shall be unconditionally and irrevocably terminated and cancelled in whole (and not in part) effective on and from the Financial Guarantor Removal Date, and no further claim may be made on the Financial Guarantees on and from the Financial Guarantor Removal Date and any such further claim shall be null and void and of no force or effect.

Where a Financial Guarantor Downgrade Event has occurred, the Financial Guarantors may remedy such Financial Guarantor Downgrade Event and the related Financial Guarantor Removal Notice by transferring the AGM Financial Guarantee to an affiliate of AGM that is rated at least "Baa3" by Moody's or "BBB-" by S&PGRS at any time prior to the Financial Guarantor Removal Date in which case the Financial Guarantor Downgrade Event shall be deemed to have been remedied.

The Issuer will immediately notify the Bondholders upon (i) any remedy or waiver of a Financial Guarantor Downgrade Event (including by way of transfer of the AGM Financial Guarantee) or (ii) termination of the Financial Guarantees pursuant to Condition 2(b) (*Financial Guarantees*).

If a continuing Financial Guarantor Downgrade Event has not been remedied or waived prior to the Financial Guarantor Removal Date, on the Financial Guarantor Removal Date:

- the Issuer shall pay to the Financial Guarantors an amount equal to (i) all amounts paid by such Financial Guarantors under the Financial Guarantees, (ii) all other amounts due and payable in accordance with the Reimbursement and Indemnity Deed including without limitation, indemnifications, gross up, taxes, reimbursements, interest, charges, fees, costs and expenses, (iii) any and all financial guarantee fees due and payable in accordance with the Financial Guarantee Fee Letters and (iv) any other amounts of any nature whatsoever due and payable to the Financial Guarantors pursuant to the Senior Finance Documents (such amounts collectively the "**Financial Guarantor Removal Payments**", as set forth in a notice in writing delivered to the Issuer and the Bond Trustee by the Financial Guarantors)

- the Financial Guarantees shall be unconditionally

and irrevocably terminated and cancelled in whole (and not in part) and shall cease to have any further force or effect and the term of the Financial Guarantees shall be deemed to have expired

- all Senior Finance Documents (including without limitation the Reimbursement and Indemnity Deed and the Financial Guarantee Fee Letters) other than the Financial Guarantees shall continue in full force and effect

- the financial guarantee fees shall cease to be paid to the Financial Guarantors, and Bondholders may by Extraordinary Resolution sanction to use the amounts no longer required to be paid as such financial guarantee fees in accordance with Condition 2(b) (*Financial Guarantees*)

If and to the extent that the Financial Guarantor Removal Payments have not been finally and irrevocably paid in full on the Financial Guarantor Removal Date by the Issuer, the Financial Guarantors shall be entitled to charge and receive from the Issuer interest on all Financial Guarantor Removal Payments (on and from the Financial Guarantor Removal Date until the date on which the Financial Guarantors (acting reasonably) have notified the Issuer and the Bond Trustee in writing that the Financial Guarantor Removal Payments have been finally and irrevocably paid in full (the "**Financial Guarantor Removal Effective Date**")) at the rate and in the amount specified in the Reimbursement and Indemnity Deed with respect to interest charged and payable on unpaid amounts. The Financial Guarantors' rights to be paid the Financial Guarantor Removal Payments shall survive the termination of the Financial Guarantees and continue in full force and effect until the Financial Guarantor Removal Effective Date shall have occurred.

For the purposes of paragraph (a)(i) of the definition of Controlling Creditor, no termination shall occur until the Financial Guarantor Removal Effective Date (and not on the occurrence of the Financial Guarantor Removal Date).

Aggregate Rating Downgrade: If both (i) the rating of the Bonds and AGM's insurer financial strength rating by S&P is less than "BBB-" or is withdrawn and (ii) each of AGM's insurer financial strength rating and the rating of the Bonds from an Alternative Rating Agency is less than "BBB-" (or such equivalent rating) or is withdrawn, and AGM has an insurer financial strength rating of at least "Baa3" by Moody's on the date that such downgrades or withdrawals occur, then the Financial Guarantors shall request the Issuer obtains and the Issuer shall use reasonable endeavours to obtain within 2 months of such date (A) a rating for the Bonds from Moody's, at the cost of AGE and (B) that the rating of the Bonds by S&P is withdrawn. The Financial Guarantors may also request that the Issuer obtains (at AGE's expense) and the Issuer shall use

	reasonable endeavours to obtain a rating of the Bonds from Moody's.
Listing and admission to trading:	Application has been made for the Bonds to be admitted to the Official List and to trading on the Main Securities Market of the Irish Stock Exchange.
Ratings:	The Bonds are expected to be rated, upon issue, AA by S&P, based on the financial strength rating of the Financial Guarantors. A rating is not a recommendation to buy, sell or hold securities, and will depend, amongst other things, on the business and financial condition of the Financial Guarantors from time to time.
Settlement/Clearance:	Euroclear and Clearstream, Luxembourg and any additional or substitute clearing system from time to time (nominated in accordance with the Bond Trust Deed).
Security Trustee:	BNY Mellon Corporate Trustee Services Limited
Bond Trustee:	BNY Mellon Corporate Trustee Services Limited
Principal Paying Agent:	The Bank of New York Mellon, London Branch
Form and Denomination:	The Bonds will be in bearer form in the denominations of £100,000 and integral multiples of £1,000 in excess thereof. The Bonds will initially be represented by the Temporary Global Bond, without receipts, coupons or talons attached, deposited with a common safekeeper for Euroclear and Clearstream, Luxembourg. The Temporary Global Bond will be exchangeable, in whole or in part, not earlier than 40 calendar days from (but not including) the Issue Date and upon certification of non-U.S. beneficial ownership, for interests in the Permanent Global Bond, without receipts, coupons or talons attached, which will also be deposited with such common safekeeper for Euroclear and Clearstream, Luxembourg. Interest payments in respect of the Bonds cannot be collected without such certification of non-U.S. beneficial ownership. The Permanent Global Bond will be exchangeable in whole, but not in part, for Bonds in definitive form in the denominations of £100,000 and integral multiples of £1,000 in excess thereof, with receipts for principal and coupons for interest and talons for further receipts or coupons attached in the limited circumstances described in the section entitled "*Summary of Provisions relating to the Bonds while in Global Form*" below. If Definitive Bonds are required to be issued, such Definitive Bonds (a) will only be issued to Bondholders (as defined below) holding Bonds having a nominal amount equal to or in excess of £100,000 and (b) will only be printed in denominations equal to or in excess of £100,000.
Security:	The payment obligations of the Issuer under the Bonds shall have the benefit of security interests granted by (i) the Issuer over all or substantially all of its undertaking

and assets both present and future, (ii) HoldCo over all or substantially all of its undertaking and assets both present and future and (iii) ProjectCo over all or substantially all of its undertaking and assets both present and future. See "*Refinancing of the Project — The Security Arrangements*".

Any exercise by the Security Trustee of its rights in respect of such security is subject to certain restrictions set out in the security trust and intercreditor deed dated on or about the Issue Date between the Obligors, the Financial Guarantors, the Bond Trustee, the Principal Paying Agent, the Account Bank, the Shareholders and the Security Trustee (the "**Security Trust and Intercreditor Deed**").

Covenants etc.: The representations, warranties, covenants (positive, negative and financial) and events of default which will apply to, *inter alia*, the Bonds will be set out in the Collateral Deed (see "*Refinancing of the Project — Collateral Deed*").

Bondholder Report: The Issuer has covenanted in the Collateral Deed that it will publish either through an electronic website or through the Principal Paying Agent via the bond clearing system (x) if and for so long as the Bond Trustee is not the Controlling Creditor annually on or before the date which is 20 business days prior to the Scheduled Payment occurring on 28 February (or 29 February in each leap year) in each year after Financial Close and (y) if and for so long as the Bond Trustee is the Controlling Creditor, semi-annually on or before the date, which is 20 business days prior to each Scheduled Payment Date, a report (the "**Bondholder Report**") in the form set out in the Collateral Deed containing, amongst other things, the following information to the extent applicable:

- Details of compliance with the financial ratios
- Key performance indicators
    - Summary financial results
    - Number of Rooms (as defined in the section entitled *"Summary of the Project Documents – Rent Setting"* below) nominated by the University. If this is less than 100% of Rooms, occupancy / voids / rental rates
- Penalties & deductions
- Costs incurred to date on extraordinary maintenance / lifecycle and relevant changes to maintenance schedule
- Changes to service providers
- Material new contracts
- Material insurance claims

- Material variations effected
- Details of each Applicable Test pursuant to clause 13.4 (Restrictive Covenant) of the Project Agreement
- Any other material topics as relevant to the Project
- Any Regulatory News Service (RNS) or other market announcements made during the reporting period.

Taxes:	All payments of principal and interest in respect of the Bonds by the Issuer will be made free and clear of, and without withholding or deduction for, taxes, unless required by law. If such taxes are imposed, the Issuer will pay principal and interest after such withholding or deduction has been made. The Issuer will not be obliged to make any additional payments to Bondholders, Receiptholders or Couponholders (as defined below in the section entitled "*Terms and Conditions of the Bonds*"). Similarly if any withholding or deduction for taxes is required in relation to any payments by AGE or AGM under the relevant Financial Guarantees, such payments will be made by AGE or AGM, as the case may be, subject to such withholding or deduction and neither AGE or AGM, as the case may be, will be obliged to make any additional payments to Bondholders, Receiptholders or Couponholders in respect of such withholding or deduction.
Governing Law:	The Bonds and each Financial Guarantee will be governed by English law.
Currency:	The Bonds will be denominated in Pounds Sterling.

RISK FACTORS

This section summarises certain factors involved in the Project which may materially affect the ability of the Issuer to make payments of interest and principal on the Bonds. In the case of certain risks this may lead to, among other things:

(i) *an Event of Default under the Collateral Deed (see the section entitled "Refinancing of the Project — Collateral Deed" below) and hence, at the option of the Controlling Creditor, acceleration of the Bonds (see the section entitled "Terms and Conditions of the Bonds"; or*

(ii) *non-payment of those amounts due on the Bonds and not guaranteed under the Financial Guarantees (see the section entitled "Overview of the Bond Issue" above), and if additionally AGE and/or AGM were to default on its obligations under the relevant Financial Guarantee, non-payment of amounts due on the Bonds that are guaranteed under such Financial Guarantee.*

Any prospective Bondholders should take their own legal, financial, accounting, tax and other relevant advice as to the structure and viability of their investment.

Risks relating to the Issuer and ProjectCo

The Issuer is a special purpose vehicle whose principal purposes are to issue the Bonds and on-lend the proceeds to ProjectCo. ProjectCo has been incorporated for the purpose of entering into the Project Agreement and running the Project. The ability of ProjectCo to repay amounts it has borrowed from the Issuer thus enabling the Issuer to perform its obligations under the Bonds is conditional upon the success of the Project. The risks relating to the Project set out below are therefore relevant to each of the Issuer and ProjectCo.

Risks relating to the Project

Introduction

The contractual arrangements for the Project are generally structured to minimise the retention by ProjectCo of risks inherent in the Project. Risks under the Project Agreement are generally borne by ProjectCo, unless assumed by the University. To the extent borne by ProjectCo under the Project Agreement, most risks are passed on to the FM Service Contractor or managed through insurance or reserved for with any residual risk being retained by ProjectCo. However, to the extent that indemnity obligations have not been imposed on sub-contractors, or where sub-contractors, their respective guarantors, the University or insurers fail to meet their obligations in respect of risks under the Project Documents which have been passed on to them by ProjectCo, or claims by ProjectCo exceed agreed limits on liability, ProjectCo will continue to bear such risks to the extent defined in the Project Agreement.

Amongst the risks which ProjectCo retains and which are not passed to its insurers or sub-contractors are demand risk, ProjectCo’s own operation costs (including certain insurance costs) certain change in law costs, latent defect risk in respect to the Quays premises and after the 12 year period during which risk is borne by Bouygues (U.K.) Limited (the "**Building Contractor**"), latent defect risk in respect to the Meadows Premises. The Building Contractor’s 12 year latent defect period will expire on the twelfth anniversary of practical completion of the development (i.e. the Meadows Premises), being 18 September 2013. A number of costs may under the Project Agreement be passed on to student rents, however, in addition to constraints under the rent setting mechanism in the Project Agreement, market conditions may limit ProjectCo's ability to pass the costs on through the student rents.

Compulsory Change Events, Force Majeure Events and Relief Events

Compulsory Change Events are specified events that are either caused by the University's default or for which the University takes the risk. Compulsory Change Events include Force Majeure Events which are a narrow category of specified events that are outside both the University’s and ProjectCo’s control. If these occur, ProjectCo will have to secure Suitable Alternative Equivalent Accommodation (as defined in the section entitled *“Summary of the Project Documents – Damage to the Accommodation”*

below), but does not take the risk on payment in the way it would if the delay were due to its own fault. The University will compensate ProjectCo for carrying out any works or changes to the Services (as defined in the section entitled *"Summary of the Project Documents – Services"* below) necessary to give effect to the Compulsory Change Event.

Relief Events are a list of specified events that are outside both the University's and ProjectCo's control. No default, Default Event and Service Warning Notice (as defined in the section entitled *"Summary of the Project Documents – Service Warning Notice"* below) shall arise from a Relief Event. ProjectCo shall not be entitled to any compensation.

See also the section entitled "*Summary of the Project Documents – The Project Agreement – Supervening Events*" below.

Site matters

ProjectCo bears substantially all the risks relating to the site, ground conditions and environmental matters (see also the section entitled "*Summary of the Project Documents – The Project Agreement – The Site*" below).

Operational risks (see also the sections entitled "*Summary of the Project Documents – The Project Agreement – Services*" and "*Summary of the Project Documents – The Project Agreement –Payment*" below).

Demand Risk

The University has the right, on an annual basis, to nominate up to 100 per cent. of the rooms. When they do so they become responsible for paying the rent for these rooms, including taking the void risk for which they retain 4 per cent. of the rent. The University is also responsible for the marketing and allocation of rooms to students.

Should the University elect to nominate less than 100 per cent. of the Accommodation, it is required to continue to market the rooms to its student body on substantially the same basis as it markets its own accommodation. In respect of any rooms which are subsequently taken up by University of Essex students, the University will become responsible for paying the rent for that room.

Where the University does not nominate 100 per cent. of the rooms, ProjectCo is entitled to conduct its own marketing to any full-time student in higher education. This allows for marketing to all University of Essex students as well as other higher education institutions.

The total university full-time student population at the University of Essex in 2014/15 was approximately 12,185. Approximately 88 per cent. of this number is studying at the University of Essex Colchester campus. According to the demand study, after allowing for all current university and privately operated halls, plus those known to be in the pipeline, the current ratio of students within the town to bed spaces is 1.8:1.

Demand from students for accommodation could be affected by a number of factors. One such factor is the possibility that the number of students choosing to study at the University could decline. This could be caused by the following possible influences:

Tuition fees and Policy Changes

Tuition fees for current students at the University of Essex are £9,000, in line with the majority of institutions. The Higher Education and Research Bill will seek to allow higher education institutions to increase fees in line with inflation. It is not yet clear how strong an impact tuition fee increases at undergraduate level will affect demand from UK students for postgraduate education.

In 2015 HEFCE Student Number Controls were further extended, allowing successful universities to recruit more students within an overall expansion of places in the higher education system. However, strong universities stand to benefit more and there may be greater fluctuations in recruitment due to competitive factors each year. Other fee considerations may affect student numbers such as

competition from overseas universities, particularly those situated in EU member states, requiring lower tuition fees.

International Student Arrangements in the United Kingdom

Non-EU students have been subject to restrictions since 2012, when they were no longer able to work for 20 hours a week whilst studying (they have no rights to work) or to remain in the UK for 2 years on graduation as they used to under the previous rules. Students have to obtain a visa in order to remain in the UK to work now, which has to be sponsored by an employer. The change to work experience rules may deter some international students, such as many Indian students, from studying in the UK (who valued the opportunity to work following their degree).

Brexit

The impact of Brexit may be wide ranging in effect on recruitment of non-UK students from all domiciles. It is too early to say how this impact will affect demand for high quality universities in the long term. Short term the impacts can be seen in a number of events, such as the perception that the UK is unwelcoming to foreign nationals, mitigated by the weakening of the pound against major currencies. Some visa trials to allow students to remain in the UK to work after graduation are currently underway, which again may pilot opportunities to widen the appeal of UK higher education in future if they are widened out.

The University of Essex remains comfortable with its competitive position and with its outlook with regard to non-UK student recruitment. The quality of the students at the University is high and the University is reacting positively to change across the sector in its strategies. The University continues to attract a large number and proportion of students from non-EU domiciles.

University-operated accommodation

The majority of the University's accommodation is located on the main Colchester campus. In 2016/17, the University offers 4,117 rooms (including the 1,429 rooms that ProjectCo is obliged to provide pursuant to the Project Agreement).

The University has an accommodation project in the immediate pipeline for development of an additional 643 rooms for occupation in the 2018/19 academic year, as part of a masterplan for maximum total potential development of in the region of 2,000 bed spaces.

Private sector operated, purpose built accommodation

The number of private rooms is limited in Colchester, totalling 1,256 rooms. The newest scheme is The Maltings, which opened in 2014, adding 780 rooms to the market.

ProjectCo is exposed to the risk that the University will default in making payments under the Project Agreement and/or sub-leases

The rents payable by students under the student leases are collected by the University as landlord directly from students and are then paid to ProjectCo as rent (see section entitled *Summary of the Project Documents – The Project Agreement – Payment*). ProjectCo's ability to meet payments under the Bonds, as well as meet all of its other financial commitments under sub-contracts and to meet it other operating expenses, is dependent on the University collecting in those rents and paying them on the relevant payment dates to ProjectCo. Although such non-payment could give rise to an entitlement for ProjectCo to terminate the Project Agreement against the University, there is no guarantee that compensation on termination payments would be paid at the time and in the manner contemplated by the Project Agreement.

Increases in overall operating expenditure will impact on ProjectCo's financial performance, if it is unable to pass those costs through to rents

The principal operating expenditure is facilities management fees payable to the FM Service Contractor, insurances, utilities (see risk factor below entitled "*ProjectCo may not be able to pass on*

an increase in utilities costs to rental income") and employment costs. The FM Service Contractor is entitled to annual increases in its contract price, linked to RPI.

In an environment where high levels of inflation exist, there is a risk that all or part of the effects of inflation could not be passed through to student rents. This is because there is a cap on the amount by which a proportion of the rent can increase due to inflation in any year. In addition the market may be unable to sustain such an increase without adversely affecting demand for the accommodation (see further "*Summary of the Project Documents - Project Agreement - Rent Setting*" below).

Accordingly, if overall operating expenditure increases and those increases cannot be passed through to rents, this may adversely affect ProjectCo's financial performance.

ProjectCo may not be able to pass on an increase in utilities costs to rental income.

There are mechanisms within the Project Agreement to enable the pass-through of increases in utility consumption against an assumed consumption level and tariff to rents on an annual basis. Utilities costs, including energy (both volume and price), are, to the extent not recovered from students or occupiers, borne by ProjectCo. Rents charged to students are inclusive of utility costs, including heating and electricity charges

There is a risk that the total increase in utility costs cannot be fully passed through to rent for the next rental period, amongst other reasons the market is unable to sustain the proposed increase directly attributable to the increase in utility costs (combined with any other increases) without impacting on demand for the accommodation.

Unavailability

In the event of any unavailability of a room, ProjectCo bears the risk of procuring Suitable Alternative Equivalent Accommodation and/or any associated loss of revenue. This risk has been assumed by the FM Service Contractor, subject to annual cap of 100 per cent. of its annual service fee. This cap is subject to the exclusion of certain liabilities.

Lifecycle

During the term of the Project Agreement, ProjectCo will need to undertake certain lifecycle work in order to satisfy its obligations under the Project Agreement. The timing and expenditure in relation to lifecycle has been judged by ProjectCo as being appropriate for the Project.

There are a variety of factors which could lead to higher than projected costs, such as shorter than anticipated asset lifespan or higher inflation than predicted affecting lifecycle costs. Under the financing arrangements, an account (the "**Lifecycle Account**") has been opened and will be maintained by ProjectCo with the Account Bank in order to reserve designated cash by reference to the projected future lifecycle expenditure over a defined period.

The FM Service Contractor has assumed the risk that the cost of performing the lifecycle works may exceed the amount projected in any Contract Year and over the Term.

Termination and Replacement of the FM Service Contractor

In the event of FM Service Contractor termination, ProjectCo will need to replace the FM Service Contractor (or procure alternative provision of the part of the Services to be sub-contracted) to ensure continued provision of the Services to the University.

The University is entitled to require ProjectCo to terminate the FM Service Contract in the case of certain specified situations where Service Warning Notices have been issued by the University. A Service Warning Notice can be issued if a specified number of service default points are reached. Service default points are de-merit points awarded to ProjectCo for poor performance under the agreed service level agreement. The thresholds associated with service default points set in the FM Service Contract are lower than required to terminate the Project Agreement in order to give ProjectCo a "buffer" to manage the risk of a non-performing FM Service Contractor. The Project Agreement allows ProjectCo to pass on the increased cost of procuring a replacement FM Service Contractor for the

remainder of the Term (as defined below) through the rent setting mechanism where the FM Service Contract has been terminated at the request of the University (see further "*Summary of the Project Documents – the Project Agreement – Termination of the FM Service Contract at the University's Request*" below).

In any other FM Service Contract termination scenario, ProjectCo bears the risk of any increased cost of procuring a replacement FM Service Contractor for the remainder of the Term (as defined below) although the outgoing FM Service Contractor will be liable for ProjectCo's losses (including the increased costs of any replacement FM Service Contractor) where the termination is due to the FM Service Contractor's default. This is subject to the FM Service Contractor's agreed liability termination cap of 200 per cent. of its annual service fee. This cap is subject to the exclusion of certain liabilities.

Project term risks (see also the section entitled "*Summary of the Project Documents – The Project Agreement – Supervening Events*" below)

Physical Damage

ProjectCo bears the risk of physical damage to the Accommodation and other property of ProjectCo. The University has certain obligations to pursue students for recovery where this damage is caused by students. Where the University has not recovered costs from students, ProjectCo will seek to recover from insurances. The University will reimburse ProjectCo for any insurance deductible and/or any repair costs not recovered by ProjectCo from insurances.

Changes in Legislation

ProjectCo must, generally, comply with all legislation throughout the Term. A change in legislation is where legislation or a court judgment creating a binding precedent comes into effect after 7 August 2012 (the "**Original Financial Close Date**") (a "**Change in Legislation**").

A change in Legislation affecting the FM Service Contractor's obligations under the FM Service Contract is a Compulsory Change Event under the terms of the FM Service Contract.

ProjectCo may adjust the student rents to take into account a number of changes in legislation ("**Relevant Changes in Legislation**"). This is further described in the section entitled "*Summary of the Project Documents – The Project Agreement – Rent Setting*" below. In this way, ProjectCo anticipates that the costs of Changes in Legislation for which it remains responsible will be passed on to the occupiers of the rooms by way of increasing the student rents. The financial impact of high value changes in legislation may need to be passed down to rents over a period of time.

Cost and Unavailability of Insurance

ProjectCo's strategies for the management and mitigation of a number of risks depend on its ability to insure. Subject as noted in the three following paragraphs, ProjectCo bears the risk that, over time, the cost of its insurance programme may increase or that insurances may not be available at all, on the same terms or at sustainable cost.

Where the actual cost of placing the insurances required by the Project Agreement is more than the cost for them (as estimated at the Original Financial Close Date), then ProjectCo will generally have to pay that increased insurance cost. ProjectCo will not have to bear the increased cost, however, if it is so large that it makes a risk uninsurable ("**Uninsurable**"). A risk becomes Uninsurable in these circumstances if the cost or terms are at such a level that the risk is not generally being insured against in the European insurance market with reputable insurers of good standing. Where a risk is Uninsurable and the parties cannot agree as to how to manage that risk, ProjectCo is generally protected through either the University being able to terminate the Project Agreement (in the event of third party liability insurance being Uninsurable) and a termination amount becoming payable by the University or the Project Agreement continuing until the occurrence of an Uninsurable risk at which point the University can either elect to pay the equivalent of the insurance proceeds that would have been payable had the insurance been available and thereafter continue with the Project Agreement or to terminate the Project Agreement and pay the applicable termination amount. Apart from these large cost changes, ProjectCo substantially bears the risk of increased insurance costs. This risk may, to some extent, be mitigated by

the rent setting provisions (see the section entitled "*Risk Factors – Risks Relating to the Project - Demand Risk*" above). These may allow the rents charged to the students and other occupiers to be increased as a result of the increased insurance costs.

Particular terms or conditions of insurance policies (as opposed to insurance against risks themselves) required by the Project Agreement may not be available to ProjectCo (at all or at sustainable cost) ("**Unavailable Insurance**"). ProjectCo will then have to secure an appropriate alternative or replacement term or condition, if available. If it is agreed or determined that such alternative is not available, ProjectCo is relieved from taking out this Unavailable Insurance. The underlying risk, however, remains with ProjectCo.

Termination of the Project Agreement

The Project Agreement incorporates termination rights for both the University and ProjectCo. The Project Agreement provides where the University must pay compensation to ProjectCo on termination. The amount of compensation will vary depending on the reason for termination and other circumstances.

The Project Agreement could be terminated for the following reasons:

(a) ProjectCo Default;

(b) default by the University;

(c) a Compulsory Change Event occurring;

(d) a Prohibited Act being committed;

(e) if ProjectCo deals with its financing agreements in a manner which may have a material adverse effect;

(f) an Uninsurable Risk (as defined in the section entitled "*Cost and Unavailability of Insurance*" above) occurring; or

(g) on termination of the Agreement for Lease (as defined in the section entitled "*Summary of the Project Documents – Agreement for Lease*" below).

This is further described in the section entitled "*Summary of the Project Documents – The Project Agreement – Compensation on Termination*" below).

Litigation risks

From time to time, ProjectCo may become involved in litigation as part of the ordinary course of its business. There is a risk that it may be unsuccessful in defending or pursuing any such actions, for example in relation to public and employee health and safety or claims for loss or damage, although project insurances may provide financial mitigation depending on the precise circumstances.

VAT

The University issued at practical completion certificates of relevant residential purpose to ProjectCo in respect of both the Meadows and the Quays sites. Such certificates will only be valid if the use of each site is 95 per cent residential accommodation for students (although under current HMRC practice non term time use by the University may be ignored). If either certificate were incorrect, ProjectCo could be compelled to repay VAT recovered on construction costs if they were found to be acting recklessly in accepting the certificate. Uliving's indemnity in favour of the University in the underleases could extend to any VAT suffered by the University as a result of a 'change of use' charge if the actual use of the relevant property is less than 95 per cent for student accommodation. Ongoing rental payments by the University in relation to the underleases of the Accommodation are exempt for VAT purposes.

Input Tax on ProjectCo operating and maintenance costs is irrecoverable as it is deemed to relate to the making of future exempt rental supplies under the underleases.

Any VAT charged on Facilities maintenance and lifecycle services provided by Derwent is also irrecoverable as the lifecycle works and FM services are attributable to exempt supplies of property by ProjectCo. Staff who undertake the lifecycle works and other facilities management works are employed under joint contracts of employment which identify both ProjectCo and Derwent (that is, the joint employers). Sums paid by ProjectCo to Derwent for the reimbursement of ProjectCo's share of the employment costs incurred by Derwent are intended not to be subject to VAT on the basis that they do not represent a supply for VAT purposes as a consequence of the joint employment.

The Project has been structured in a way designed to minimise irrecoverable VAT on construction and operating costs. A significant increase in the amount of VAT which was irrecoverable by ProjectCo or for which ProjectCo had to indemnify the University would have a major impact on the project economics.

Risks Relating to the Financial Guarantors

Reliance on the Financial Guarantors

Pursuant to the Financial Guarantees, the Financial Guarantors guarantee scheduled payments of principal and interest under the Bonds. The payment of the guaranteed amounts (as defined in the Financial Guarantees) ("**Guaranteed Amounts**") will depend upon each of the Financial Guarantors performing its obligations under its respective Financial Guarantee. The likelihood of payment of the Guaranteed Amounts will depend upon the creditworthiness of each of the Financial Guarantors. Consequently, investors are relying not only on the creditworthiness of the Issuer, but also on the creditworthiness of each of the Financial Guarantors to perform its obligations under the relevant Financial Guarantee. The insolvency of either of the Financial Guarantors or a default by it under its respective Financial Guarantee may adversely affect the likelihood of investors receiving scheduled payments of principal and interest and could result in a withdrawal or downgrade of the ratings of the Bonds.

The Financial Guarantees only guarantee scheduled principal and scheduled interest payments by the Issuer on the date(s) when such amounts are initially scheduled to become due and payable (subject to and in accordance with each Financial Guarantee), and do not guarantee the market price, or liquidity of any securities, nor do they guarantee that the ratings on such securities will not be revised or withdrawn.

Reliance by AGE on AGM

The financial strength ratings of AGE are based primarily on the ratings of and the capital support and reinsurance provided by AGM to AGE pursuant to certain intercompany support agreements (the "**Support Agreements**"). Any downgrade of the ratings of AGM would very likely result in a downgrade of the ratings of AGE. The Support Agreements are not, and should not be regarded as, conferring any recourse against AGM or any other person under the Support Agreements. See "*Description of the Financial Guarantors*" below for further details on the Support Agreements.

Ratings of Bonds affected by the Financial Guarantors

The ratings of the Bonds are based primarily on the Financial Guarantees issued by the Financial Guarantors with respect to the Bonds. The financial strength ratings assigned by S&PGRS, Moody's and KBRA, as applicable, to the Financial Guarantors represent the rating agencies' opinions of each Financial Guarantor's financial strength and ability to meet ongoing obligations to policyholders and cedants in accordance with the terms of the financial guarantees each has issued or the reinsurance agreements each has executed. The ratings also reflect qualitative factors, such as the rating agencies' opinion of the Financial Guarantor's business strategy and franchise value, the anticipated future demand for its product, the composition of its insured portfolio, and its capital adequacy, profitability and financial flexibility. Issuers, investors, underwriters, ceding companies and others consider the Financial Guarantors' financial strength or financial enhancement ratings an important factor when deciding whether or not to utilize a financial guarantee or purchase reinsurance from one of the Financial Guarantors. A downgrade by a rating agency of the financial strength or financial enhancement ratings of a Financial Guarantor could impair that Financial Guarantor's financial

condition, results of operation, liquidity, business prospects or other aspects of that Financial Guarantor's business.

The ratings assigned by the rating agencies that publish financial strength or financial enhancement ratings on the Financial Guarantors are subject to frequent review and may be lowered by a rating agency as a result of a number of factors, including, but not limited to, the rating agency's revised stress loss estimates for a Financial Guarantor's insured portfolio, adverse developments in a Financial Guarantor's financial condition or results of operations due to underwriting or investment losses or other factors, changes in the rating agency's outlook for the financial guarantee industry or in the markets in which a Financial Guarantor operates, or a revision in the rating agency's capital model or ratings methodology. Their reviews can occur at any time and without notice to the Financial Guarantors and could result in a decision to downgrade, revise or withdraw the financial strength or financial enhancement ratings of the Financial Guarantors. For example, while all of the rating agencies that rate AGM have indicated that their evaluations of AGM already take into account stress scenarios related to developments in the Commonwealth of Puerto Rico ("**Puerto Rico**"), actual developments in Puerto Rico beyond what a rating agency considered could cause that rating agency to review its ratings of AGM.

Since 2008, each of S&PGRS and Moody's has reviewed and downgraded the financial strength ratings of AGM and AGE. In addition, S&PGRS and Moody's have from time to time changed the ratings outlook for AGM and AGE to "negative" from "stable" or have placed such ratings on watch for possible downgrade. The Financial Guarantors periodically assess the value of each rating assigned to them, and may as a result of such assessment may request that a rating agency add or drop a rating. For example, the KBRA ratings were first assigned to AGM in 2014.

The Financial Guarantors believe that the uncertainty introduced by S&PGRS' and Moody's various actions and proposals have reduced the Financial Guarantors' new business opportunities and have also affected the value of the Financial Guarantors' product to issuers and investors. Their financial strength ratings are an important competitive factor in the financial guaranty insurance and reinsurance markets. If the financial strength or financial enhancement ratings of one or more of the Financial Guarantors were reduced below current levels, the Financial Guarantors expect that would reduce the number of transactions that would benefit from the Financial Guarantors' insurance; consequently, a downgrade by rating agencies could harm the Financial Guarantors' new business production, results of operations and financial condition.

The rating agencies from time to time have evaluated the Financial Guarantors' capital adequacy under a variety of scenarios and assumptions. The rating agencies do not always supply clear guidance on their approach to assessing the Financial Guarantors' capital adequacy and the Financial Guarantors may disagree with the rating agencies' approach and assumptions. For example, S&PGRS assesses each individual credit (including potential new credits) insured by the Financial Guarantors based on a variety of factors, including the nature of the credit, the nature of the support or credit enhancement for the credit, its tenor, and its expected and actual performance. This assessment determines the amount of capital a Financial Guarantor is required to maintain against that credit to maintain its financial strength ratings under S&PGRS' capital adequacy model. Sometimes the rating agencies consider the amount of additional capital that could be required for certain risks or sectors under certain stress scenarios based on their views of developments in the market, as each have done recently with respect to AGM's exposures to Puerto Rico. Factors influencing the rating agencies are beyond management's control and not always known to the Financial Guarantors. In the event of an actual or perceived deterioration in creditworthiness, or a change in a rating agency's capital model or rating methodology, that rating agency may require the Financial Guarantors to increase the amount of capital allocated to support the affected credits, regardless of whether losses actually occur, or against potential new business. Significant reductions in the rating agencies' assessments of credits in the Financial Guarantors' insured portfolio can produce significant increases in the amount of capital required for the Financial Guarantors to maintain their financial strength ratings under the rating agencies' capital adequacy models, which may require the Financial Guarantors to seek additional capital. The amount of such capital required may be substantial, and may not be available to the Financial Guarantors on favourable terms and conditions or at all. Accordingly, the Financial Guarantors cannot ensure that they will seek to, or be able to, raise additional capital. The failure to raise additional required capital could result in

a downgrade of the Financial Guarantors' ratings and thus have an adverse impact on its business, results of operations and financial condition.

Since 2009, Moody's and S&PGRS have downgraded a number of structured finance securities and public finance bonds, including obligations that the Financial Guarantors insure. Additional obligations in the Financial Guarantors' insured portfolio may be reviewed and downgraded in the future. Downgrades of a Financial Guarantor’s insured credits will result in higher capital requirements for that Financial Guarantor under the relevant rating agency capital adequacy model. If the additional amount of capital required to support such exposures is significant, a Financial Guarantor may need to undertake certain actions in order to maintain its ratings, including, but not limited to, raising additional capital (which, if available, may not be available on terms and conditions that are favourable to the Financial Guarantor); curtailing new business; or paying to transfer a portion of its in-force business to generate rating agency capital. If a Financial Guarantors is unable to complete any of these capital initiatives, it could suffer ratings downgrades. These capital actions or ratings downgrades could adversely affect such Financial Guarantor’s results of operations, financial condition, ability to write new business or competitive positioning.

Impact of the Financial, Credit and Financial Guaranty Markets on the Financial Guarantors

The financial guarantees issued by the Financial Guarantors insure the credit performance of the guaranteed obligations over an extended period of time, in some cases over 30 years, and in most circumstances, the Financial Guarantors have no right to cancel such financial guarantees. As a result, each Financial Guarantor's estimate of ultimate losses on a financial guarantee is subject to significant uncertainty over the life of the guaranteed transaction. Credit performance can be adversely affected by economic, fiscal and financial market variability over the long duration of most contracts. If a Financial Guarantor's actual losses exceed its current estimate, this may result in adverse effects on the relevant Financial Guarantor's financial condition, results of operations, liquidity, business prospects, financial strength ratings and ability to raise additional capital.

In addition, if the Financial Guarantors are required to make claim payments, even if they are reimbursed in full over time and do not experience ultimate loss on a particular policy, such claim payments would reduce the Financial Guarantors' invested assets and result in reduced liquidity and net investment income. If the amount of claim payments is significant, the Financial Guarantors' ability to make other claim payments and their financial condition, financial strength ratings and business prospects could be adversely affected.

The determination of expected loss 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. The Financial Guarantors do not use traditional actuarial approaches to determine their estimates of expected losses. Actual losses will ultimately depend on future events or transaction performance. As a result, the Financial Guarantors' current estimates of probable and estimable losses may not reflect the Financial Guarantors' future ultimate claims paid.

Certain sectors and large risks within the Financial Guarantors' insured portfolio have experienced credit deterioration in excess of the Financial Guarantors’ initial expectations, which has led or may lead to losses in excess of the Financial Guarantors’ initial expectations. The Financial Guarantors' expected loss models take into account current and expected future trends, which contemplate the impact of current and probable developments in the performance of the credit. These factors, which are integral elements of the Financial Guarantors' reserve estimation methodology, are updated on a quarterly basis based on current information. Because such information changes, sometimes materially, from quarter to quarter, the Financial Guarantors’ projection of losses may also change materially. Since the financial crisis, much of the development in AGM’s loss projections has been with respect to insured U.S. residential mortgage-backed securities ("RMBS"). While AGM’s net par outstanding of U.S. RMBS rated below investment grade ("**BIG**") under AGM’s rating methodology as of September 30, 2016 was still $2.2 billion and may still be a source of loss development, AGM believes the performance of this portfolio has stabilised. More recently, there has been credit deterioration with respect to certain insured credits of Puerto Rico and various obligations of its related authorities and public corporations.

AGM has insured exposure to general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations aggregating $2.0 billion net par as of September 30, 2016, $1.9 billion of which is rated BIG under its methodology. Puerto Rico has experienced significant general fund budget deficits in recent years. In addition to high debt levels, Puerto Rico faces a challenging economic environment; the economy has declined nearly every year since 2007, while the population has shrunk every year since 2006 as residents have emigrated. On June 28, 2015, Governor García Padilla of Puerto Rico publicly stated that Puerto Rico's public debt, considering the current level of economic activity, was unpayable and that a comprehensive debt restructuring might be necessary. On November 30, 2015 and December 8, 2015, Governor García Padilla issued executive orders directing the Puerto Rico Department of Treasury and the Puerto Rico Tourism Company to retain or transfer certain taxes pledged to secure the payment of bonds issued by the Puerto Rico Highways and Transportation Authority, Puerto Rico Infrastructure Financing Authority ("**PRIFA**"), and Puerto Rico Convention Center District Authority. On January 1, 2016, PRIFA defaulted on payment of a portion of the interest due on its bonds on that date, resulting in a claim on AGM for those PRIFA bonds AGM insures. There have been additional payment defaults on this and other Puerto Rico credits since then, including, on July 1, 2016, a default on the payment of Puerto Rico's general obligation bonds. AGM has now paid claims on several Puerto Rico credits. On June 30, 2016, the Puerto Rico Oversight, Management, and Economic Stability Act ("**PROMESA**") was signed into law by the President of the United States. PROMESA establishes a seven-member federal financial oversight board ("**Oversight Board**") with authority to require that balanced budgets and fiscal plans be adopted and implemented by Puerto Rico. PROMESA provides a legal framework under which the debt of Puerto Rico and its related authorities and public corporations may be voluntarily restructured, and grants the Oversight Board the sole authority to file restructuring petitions in a federal court to restructure the debt of Puerto Rico and its related authorities and public corporations if voluntary negotiations fail, provided that any such restructuring must be in accordance with an Oversight Board approved fiscal plan that respects the liens and priorities provided under Puerto Rico law. The Oversight Board has begun meeting. Additional information about AGM's exposure to Puerto Rico may be found in Appendix 3 and 5. The final shape, timing and validity of responses to Puerto Rico's distress eventually enacted or implemented under the auspices of PROMESA and the Oversight Board or otherwise, and the impact of any such responses on obligations insured by AGM, is uncertain.

The Financial Guarantors' loss reserves, profitability, financial position, insured portfolio, investment portfolio, cash flow and statutory capital could be materially affected by the U.S. and global financial markets. Upheavals in the financial markets affect economic activity and employment and therefore can affect the Financial Guarantors' business. The global economic outlook remains uncertain, including the overall growth rate of the U.S. economy, the fragile economic recovery in Europe and the impact of the gradual tightening of global monetary conditions on emerging markets. These and other risks could materially and negatively affect the Financial Guarantors' ability to access the capital markets, the cost of the Financial Guarantors' debt, the demand for its products, the amount of losses incurred on transactions it guarantees, the value of its investment portfolio, its financial ratings and the price of its common shares.

Some of the state and local governments that issue the obligations AGM insures have experienced significant budget deficits and pension funding and revenue collection shortfalls that required them to significantly raise taxes and/or cut spending in order to satisfy their obligations. While the U.S. government has provided some financial support and although overall state revenues have increased in recent years, significant budgetary pressures remain, especially at the local government level and in relation to retirement obligations. Certain local governments, including ones that have issued obligations insured by AGM, have sought protection from creditors under chapter 9 of the U.S. Bankruptcy Code as a means of restructuring their outstanding debt. In some recent instances where local governments were seeking to restructure their outstanding debt, and partially in response to concerns that materially reducing pension payments would lead to employee flight and, therefore, an inadequate level of local government services, pension and other obligations owed to workers were treated more favourably than senior bond debt owed to the capital markets. If the issuers of the obligations in AGM's public finance portfolio do not have sufficient funds to cover their expenses and are unable or unwilling to raise taxes, decrease spending or receive federal assistance, AGM may experience increased levels of losses or impairments on its public finance obligations, which could materially and adversely affect its business, financial condition and results of operations. If such issuers succeed in restructuring pension and other obligations owed to workers so that they are treated more

favourably than obligations insured by AGM, such losses or impairments could be greater than AGM otherwise anticipated when the insurance was written.

AGM's risk of loss on and capital charges for municipal credits could also be exacerbated by rating agency downgrades of municipal credit ratings. A downgraded municipal issuer may be unable to refinance maturing obligations or issue new debt, which could reduce the municipality's ability to service its debt. Downgrades could also affect the interest rate that the municipality must pay on its variable rate debt or for new debt issuance. Municipal credit downgrades, as with other downgrades, result in an increase in the capital charges the rating agencies assess when evaluating the AGM's capital adequacy in their rating models. Significant municipal downgrades could result in higher capital requirements for AGM in order to maintain its financial strength ratings.

In addition, obligations supported by specified revenue streams, such as revenue bonds issued by toll road authorities, municipal utilities or airport authorities, may be adversely affected by revenue declines resulting from reduced demand, changing demographics or other factors associated with an economy in which unemployment remains high, housing prices have not yet stabilized and growth is slow. These obligations, which may not necessarily benefit from financial support from other tax revenues or governmental authorities, may also experience increased losses if the revenue streams are insufficient to pay scheduled interest and principal payments.

Demand for financial guaranty insurance generally fluctuates with changes in market credit spreads. Credit spreads, which are based on the difference between interest rates on high-quality or "risk free" securities versus those on lower-rated or uninsured securities, fluctuate due to a number of factors and are sensitive to the absolute level of interest rates, current credit experience and investors' risk appetite. Over the last several years, interest rates generally have been lower than historical norms. In 2015, average daily AAA benchmark 30-year municipal interest rates as reflected by the MMD Index were approximately 35 basis points lower that their levels in 2014, a year in which rates were already low by historical standards. When interest rates are low, or when the market is relatively less risk averse, the credit spread between high-quality or insured obligations versus lower- rated or uninsured obligations typically narrows. As a result, financial guaranty insurance typically provides lower interest cost savings to issuers than it would during periods of relatively wider credit spreads. When issuers are less likely to use financial guaranties on their new issues when credit spreads are narrow, this results in decreased demand or premiums obtainable for financial guaranty insurance, and a resulting reduction in the Financial Guarantors' results of operations. The continued persistence of low interest rate levels and credit spreads could continue to dampen demand for financial guaranty insurance.

Conversely, in a deteriorating credit environment, credit spreads increase and become "wide", which increases the interest cost savings that financial guaranty insurance may provide and can result in increased demand for financial guaranties by issuers. However, if the weakening credit environment is associated with economic deterioration, the Financial Guarantors' insured portfolio could generate claims and loss payments in excess of normal or historical expectations. In addition, increases in market interest rate levels could reduce new capital markets issuances and, correspondingly, a decreased volume of insured transactions.

The Financial Guarantors can face competition, either in the form of current or new providers of credit enhancement or in terms of alternative structures, including uninsured offerings, or pricing competition. Increased competition could have an adverse effect on the Financial Guarantors' insurance business.

AGM's reporting currency is the U.S. dollar and AGE's reporting currency is the British pound sterling. The Financial Guarantors maintain both assets and liabilities in currencies different than their reporting currencies, which expose them to changes in currency exchange rates. The principal currencies impacting the Financial Guarantors are the U.S. dollar, the British pound sterling and the European Union euro. The Financial Guarantors cannot accurately predict the nature or extent of future exchange rate variability among these currencies. Currency exchange rates are sensitive to factors beyond the Financial Guarantors' control. The Financial Guarantors do not engage in active management, or hedging, of their currency exchange rate risk. Therefore, fluctuation in exchange rates among these currencies could adversely impact the Financial Guarantors' financial position, results of operations and cash flows.

The Financial Guarantors pursue new business opportunities in international markets. The underwriting of obligations of an issuer in a foreign country involves the same process as that for a domestic issuer, but additional risks must be addressed, such as the evaluation of foreign currency exchange rates, foreign business and legal issues, and the economic and political environment of the foreign country or countries in which an issuer does business. Changes in such factors could impede the Financial Guarantors' ability to insure, or increase the risk of loss from insuring, obligations in the countries in which it currently does business and limit its ability to pursue business opportunities in other countries.

The Financial Guarantors' operating results are affected, in part, by the performance of their respective investment portfolios which consist primarily of fixed-income securities and short-term investments. Credit losses and changes in interest rates could have an adverse effect on their respective shareholders' equity and net income. Credit losses result in realized losses on the Financial Guarantors' investment portfolio, which reduce net income and shareholders' equity. Changes in interest rates can affect both shareholders' equity and investment income. For example, if interest rates decline, funds reinvested will earn less than expected, reducing the Financial Guarantors' future investment income compared to the amount they would earn if interest rates had not declined. However, the value of the Financial Guarantors' fixed-rate investments would generally increase if market interest rates decreased. Conversely, if interest rates increase, the value of the investment portfolio will be reduced.

Interest rates are highly sensitive to many factors, including monetary policies, domestic and international economic and political conditions and other factors beyond the Financial Guarantors' control. The Financial Guarantors do not engage in active management, or hedging, of interest rate risk, and may not be able to mitigate interest rate sensitivity effectively.

The market value of the investment portfolio also may be adversely affected by general developments in the capital markets, including decreased market liquidity for investment assets, market perception of increased credit risk with respect to the types of securities held in the portfolio, downgrades of credit ratings of issuers of investment assets and/or foreign exchange movements which impact investment assets. In addition, the Financial Guarantors invest in securities insured by other financial guarantors, the market value of which may be affected by the rating instability of the relevant financial guarantor.

Capital and Liquidity Requirements of the Financial Guarantors

The Financial Guarantors' capital requirements depend on many factors, primarily related to their in-force book of business and rating agency capital requirements. Both Financial Guarantors need liquid assets to make claim payments on their insured portfolio and to write new business. Failure to raise additional capital as needed may result in the Financial Guarantors being unable to write new business and may result in the ratings of the Financial Guarantors being downgraded by one or more ratings agency. The Financial Guarantors' access to external sources of financing, as well as the cost of such financing, is dependent on various factors, including the market supply of such financing, the long-term debt ratings of their holding companies and the Financial Guarantors' insurance financial strength ratings and the perceptions of the financial strength of their holding companies and their financial strength. The holding companies' debt ratings are in turn influenced by numerous factors, such as financial leverage, balance sheet strength, capital structure and earnings trends. If the Financial Guarantors' need for capital arises because of significant losses, the occurrence of these losses may make it more difficult for the Financial Guarantors to raise the necessary capital.

Financial guaranty insurers and reinsurers typically rely on providers of lines of credit, credit swap facilities and similar capital support mechanisms (often referred to as "soft capital") to supplement their existing capital base, or "hard capital". The ratings of soft capital providers directly affect the level of capital credit which the rating agencies give the Financial Guarantors when evaluating their financial strength. AGM currently maintains soft capital facilities with providers having ratings adequate to provide AGM's desired capital credit. For example, effective January 1, 2016, AGM and certain affiliates entered into a $360 million aggregate excess of loss reinsurance facility with a number of reinsurers that covers certain U.S. public finance credits insured or reinsured by those companies. However, no assurance can be given that AGM will be able to renew any existing soft capital facilities or that one or more of the rating agencies will not downgrade or withdraw the applicable ratings of such providers in the future. In addition, AGM may not be able to replace a downgraded soft capital provider with an acceptable replacement provider for a variety of reasons, including if an acceptable replacement provider is willing to provide AGM with soft capital commitments or if any adequately-

rated institutions are actively providing soft capital facilities. Furthermore, the rating agencies may in the future change their methodology and no longer give credit for soft capital, which may necessitate AGM having to raise additional capital in order to maintain its ratings.

Insurance regulatory authorities impose capital requirements on the Financial Guarantors. These capital requirements, which include leverage ratios and surplus requirements, may limit the amount of insurance that they may write. The Financial Guarantors have several alternatives available to control their leverage ratios, including obtaining capital contributions from their affiliates, purchasing reinsurance or entering into other loss mitigation agreements, or reducing the amount of new business written. However, a material reduction in the statutory capital and surplus of a Financial Guarantor, whether resulting from underwriting or investment losses, a change in regulatory capital requirements or otherwise, or a disproportionate increase in the amount of risk in force, could increase such Financial Guarantor's leverage ratio. This in turn could require a Financial Guarantor to obtain reinsurance for existing business (which may not be available, or may only be available on terms that such Financial Guarantor considers unfavourable), or add to its capital base to maintain its financial strength ratings. Failure to maintain regulatory capital levels could limit a Financial Guarantor's ability to write new business.

Business of the Financial Guarantors

The Financial Guarantors are exposed to the risk that issuers of debt that they insure or other counterparties may default in their financial obligations, whether as a result of insolvency, lack of liquidity, operational failure or other reasons. Similarly, the Financial Guarantors could be exposed to corporate credit risk if a corporation's securities are contained in a portfolio of collateralized debt obligations ("**CDOs**") they insure, or if the corporation or financial institution is the originator or servicer of loans, mortgages or other assets backing structured securities that the Financial Guarantor has insured.

In addition, because AGM insures municipal bonds, it can have significant exposures to single municipal risks (e.g., the Commonwealth of Puerto Rico). While AGM's risk of a complete loss, where it would have to pay the entire principal amount of an issue of bonds and interest thereon with no recovery, is generally lower for municipal bonds than for corporate bonds as most municipal bonds are backed by tax or other revenues, there can be no assurance that a single default by a municipality would not have a material adverse effect on its results of operations or financial condition.

The Financial Guarantors' ultimate exposure to a single name may exceed their underwriting guidelines, and an event with respect to a single name may cause a significant loss. The Financial Guarantors seek to reduce this risk by managing exposure to large single risks, as well as concentrations of correlated risks, through tracking its aggregate exposure to single names in their various lines of business, establishing underwriting criteria to manage risk aggregations. They have also in the past obtained third party reinsurance for such exposure. AGM may insure and has insured individual public finance and asset-backed risks well in excess of $1 billion. Should the Financial Guarantors' risk assessments prove inaccurate and should the applicable limits prove inadequate, the Financial Guarantors could be exposed to larger than anticipated losses, and could be required by the rating agencies to hold additional capital against insured exposures whether or not downgraded by the rating agencies.

The Financial Guarantors are exposed to correlation risk across the various assets they insure. During periods of strong macroeconomic performance, stress in an individual transaction generally occurs in a single asset class or for idiosyncratic reasons. During a broad economic downturn, a wider range of the Financial Guarantors' insured portfolio could be exposed to stress at the same time. This stress may manifest itself in ratings downgrades, which may require more capital, or in actual losses. In addition, while the Financial Guarantors have experienced catastrophic events in the past without material loss, unexpected catastrophic events may have a material adverse effect upon the Financial Guarantors' insured portfolio and/or their investment portfolios.

As of September 30, 2016 5% of AGM’s financial guaranty direct net exposures were executed as credit derivatives. Traditional financial guaranty insurance provides an unconditional and irrevocable guaranty that protects the holder of a municipal finance or structured finance obligation against non-payment of principal and interest, while credit derivatives provide protection from the occurrence of

specified credit events, including non-payment of principal and interest. In general, AGM structures credit derivative transactions such that circumstances giving rise to its obligation to make payments are similar to that for financial guaranty policies and generally occur when issuers fail to make payments on the underlying reference obligations. The tenor of credit derivatives exposures, like exposure under financial guaranty insurance policies, is also generally for as long as the reference obligation remains outstanding.

Nonetheless, credit derivative transactions are governed by International Swaps and Derivatives Association, Inc. ("**ISDA**") documentation and operate differently from financial guaranty insurance policies. For example, AGM's control rights with respect to a reference obligation under a credit derivative may be more limited than when it issues a financial guaranty insurance policy on a direct primary basis. In addition, a credit derivative may be terminated for a breach of the ISDA documentation or other specific events, unlike financial guaranty insurance policies.

Further downgrades of one or more of the Financial Guarantors' reinsurers could reduce the Financial Guarantors' capital adequacy and return on equity. The impairment of other financial institutions also could adversely affect the Financial Guarantors.

At September 30, 2016, AGM had ceded approximately 6% of its principal amount of insurance outstanding to third party reinsurers. In evaluating the credits insured by AGM, securities rating agencies allow capital charge "credit" for reinsurance based on the reinsurers' ratings. In recent years, a number of AGM’s third-party reinsurers were downgraded by one or more rating agencies, resulting in decreases in the credit allowed for reinsurance and in the financial benefits of using reinsurance under existing rating agency capital adequacy models. Many of AGM's reinsurers have already been downgraded to single-A or below by one or more rating agencies. AGM could be required to raise additional capital to replace the lost reinsurance credit in order to satisfy rating agency and regulatory capital adequacy and single risk requirements. In addition, downgraded reinsurers may default on amounts due to AGM and such reinsurer obligations may not be adequately collateralised, resulting in additional losses to AGM and a reduction in its shareholders' equity and net income.

The Financial Guarantors also have exposure to counterparties in various industries, including banks, hedge funds and other investment vehicles in its insured transactions. Many of these transactions expose the Financial Guarantors to credit risk in the event its counterparty fails to perform its obligations.

The Financial Guarantors' success substantially depends upon their ability to attract and retain qualified employees and upon the ability of its senior management and other key employees to implement its business strategy. The Financial Guarantors believe there are only a limited number of available qualified executives in the business lines in which the Financial Guarantors compete. AGM relies substantially upon the services of Dominic J. Frederico, President and Chief Executive Officer, and other executives. Although the Financial Guarantors have designed their executive compensation with the goal of retaining and creating incentives for its executive officers, the Financial Guarantors may not be successful in retaining their services. The loss of the services of any of these individuals or other key members of the Financial Guarantors' management team could adversely affect the implementation of their business strategies.

The Financial Guarantors rely upon information technology and systems, including technology and systems provided by or interfacing with those of third parties, to support a variety of their business processes and activities. In addition, the Financial Guarantors may have collected and stored confidential information including, in connection with certain loss mitigation and due diligence activities related to their structured finance business, personally identifiable information. While the Financial Guarantors do not believe that the financial guaranty industry is as inherently prone to cyber-attacks as industries relating to, for example, payment card processing, banking, critical infrastructure or defense contracting, the Financial Guarantors’ data systems and those of third parties on which they rely are still vulnerable to security breaches due to cyber-attacks, viruses, malware, hackers and other external hazards, as well as inadvertent errors, equipment and system failures, and employee misconduct. Problems in or security breaches of these systems could, for example, result in lost business, reputational harm, the disclosure or misuse of confidential or proprietary information, incorrect reporting, inaccurate loss projections, legal costs and regulatory penalties.

The Financial Guarantors' business operations rely on the continuous availability of their computer systems as well as those of certain third parties. In addition to disruptions caused by cyber-attacks or other data breaches, such systems may be adversely affected by natural and man-made catastrophes. The Financial Guarantors' failure to maintain business continuity in the wake of such events, particularly if there were an interruption for an extended period, could prevent the timely completion of critical processes across its operations, including, for example, claims processing, treasury and investment operations and payroll. These failures could result in additional costs, loss of business, fines and litigation.

Impact of GAAP and Applicable Law on the Financial Guarantors

AGM is required to mark-to-market certain derivatives that it insures, including CDS that are considered derivatives under U.S. GAAP. Although there is no cash flow effect from this "marking-to-market", net changes in the fair value of the derivative are reported in AGM's consolidated statements of operations and therefore affect its reported earnings. As a result of such treatment, and given the large principal balance of AGM's CDS portfolio, small changes in the market pricing for insurance of CDS will generally result in AGM recognizing material gains or losses, with material market price increases generally resulting in large reported losses under U.S. GAAP. Accordingly, AGM's U.S. GAAP earnings will be more volatile than would be suggested by the actual performance of its business operations and insured portfolio.

The fair value of a credit derivative will be affected by any event causing changes in the credit spread (i.e., the difference in interest rates between comparable securities having different credit risk) on an underlying security referenced in the credit derivative. Common events that may cause credit spreads on an underlying municipal or corporate security referenced in a credit derivative to fluctuate include changes in the state of national or regional economic conditions, industry cyclicality, changes to a company's competitive position within an industry, management changes, changes in the ratings of the underlying security, movements in interest rates, default or failure to pay interest, or any other factor leading investors to revise expectations about the issuer's ability to pay principal and interest on its debt obligations. Similarly, common events that may cause credit spreads on an underlying structured security referenced in a credit derivative to fluctuate may include the occurrence and severity of collateral defaults, changes in demographic trends and their impact on the levels of credit enhancement, rating changes, changes in interest rates or prepayment speeds, or any other factor leading investors to revise expectations about the risk of the collateral or the ability of the servicer to collect payments on the underlying assets sufficient to pay principal and interest. The fair value of credit derivative contracts also reflects the change in AGM's own credit cost, based on the price to purchase credit protection on AGM.

If a credit derivative is held to maturity and no credit loss is incurred, any unrealised gains or losses previously reported would be offset as the transactions reach maturity. Due to the complexity of fair value accounting and the application of U.S. GAAP requirements, future amendments or interpretations of relevant accounting standards may cause AGM to modify its accounting methodology in a manner which may have an adverse impact on its financial results.

Changes in or the issuance of new accounting standards, as well as any changes in the interpretation of current accounting guidance, may have an adverse effect on the Financial Guarantor's reported financial results, including future revenues, and may influence the types and/or volume of business that management may choose to pursue.

AGE is authorised by the UK Prudential Regulation Authority (the "PRA") to carry out and effect "credit", "suretyship" and miscellaneous financial loss insurance business in the United Kingdom and, pursuant to the EC third non-life insurance directive (No. 92/49/EEC), various European countries (such authorisation being the "**Insurance Business Authorisation**") and is regulated by the PRA and the UK Financial Conduct Authority.

The Insurance Business Authorisation may be revoked, withdrawn or restrictively modified by the PRA. Such revocation, withdrawal or restrictive modification could have a material adverse impact on AGE, including its ability to generate new business or increased costs of regulatory compliance.

AGM is licensed to write financial guaranty insurance and reinsurance (which is classified in some states as surety or another line of insurance) in the 50 states of the United States of America, the District of Columbia and Puerto Rico. The New York State Department of Financial Services ("**NYSDFS**") is the regulatory authority of the State of New York, U.S.A., which is AGM's state of organisation and domicile.

U.S. state insurance authorities have broad regulatory powers with respect to various aspects of the business of U.S. insurance companies, including licensing these companies to transact business, accreditation of reinsurers, admittance of assets to statutory surplus, regulating unfair trade and claims practices, establishing reserve requirements and solvency standards, regulating investments and dividends and, in certain instances, approving policy forms and related materials and approving premium rates. If AGM fails to comply with applicable insurance laws and regulations it could be exposed to fines, the loss of insurance licenses, limitations on its right to originate new business and restrictions on its ability to pay dividends, all of which could have an adverse impact on its business results and prospects. If AGM's surplus declines below minimum required levels, the insurance regulator could impose additional restrictions on AGM or initiate insolvency proceedings.

On June 23, 2016, a referendum was held in the U.K. in which a majority voted to exit the European Union, known as "**Brexit**". Negotiations will determine the future terms of the U.K's relationship with the EU, including the terms of trade between the U.K. and the EU. Any resulting political, social and economic uncertainty and changes arising from Brexit may have a negative impact on the economies of the U.K. as well as non-U.K. EU and EEA countries, which may increase the probability of losses on obligations insured by the Financial Guarantors that are exposed to risks in the U.K. and non-U.K. EU and EEA countries. In addition, central banks, including the United States Federal Reserve, may lower interest rates, or extend the period of lower interest rates, to mitigate the economic impacts of Brexit. Low interest rates may adversely affect the Financial Guarantors as described above.

Brexit could lead to legal uncertainty and politically divergent national laws and regulations as the U.K. determines which EU laws to replace or replicate. Depending on the terms of Brexit, AGE may lose the ability to insure new transactions from London in non-U.K., EU and EEA countries without obtaining additional licenses, which may require a presence in another EU country. Brexit-related changes in laws and regulations may also adversely affect AGE's surveillance and loss mitigation activities with respect to existing insured transactions in non-U.K., EU and EEA countries, especially to the extent Brexit inhibits the issuance of new guarantees in distressed situations. Brexit may also impact laws, rules and regulations applicable to U.K. entities with obligations insured by the Financial Guarantors and could adversely impact the ability of non-U.K., EU or EEA citizens to continue to be employed at AGE in London.

From time to time, U.S. legislators have called for changes to the U.S. Internal Revenue Code in order to limit or eliminate the Federal income tax exclusion for municipal bond interest. Such a change would increase the cost of borrowing for state and local governments, and as a result, could cause a decrease in infrastructure spending by states and municipalities. Municipalities may issue a lower volume of bonds, and in particular may be less likely to refund existing debt, in which case, the amount of bonds that can benefit from AGM's insurance might also be reduced.

Control by the Financial Guarantors

While the Financial Guarantees mitigate the credit risks to which potential investors in the Bonds would otherwise be exposed, the involvement of the Financial Guarantors has certain consequences. For example, for so long as they are the Controlling Creditor, the Financial Guarantors will have the right to exercise many of the discretions which would otherwise rest in the Bond Trustee and the Security Trustee (including the discretion as to whether to declare events of default or enforcement events or to accelerate payments of principal and interest, and in respect of which the Bond Trustee might otherwise have sought the directions of the Bondholders). In addition, in the event that the Financial Guarantors are required to make a payment under the Financial Guarantees, the Issuer will be required to reimburse the Financial Guarantors and to pay various fees, costs and expenses to the Financial Guarantors.

Acceleration of Bonds

The terms of each Financial Guarantee provide that amounts of principal on any Bonds which have become immediately due and payable (whether by virtue of acceleration, prepayment or otherwise) will not be treated as Guaranteed Amounts which are due for payment unless the relevant Financial Guarantor in its sole discretion elects so to do by notice in writing to the Bond Trustee. If no such election is made, that Financial Guarantor will continue to be liable to make payments of Guaranteed Amounts in respect of the Bonds pursuant to the relevant Financial Guarantee on the dates on which such payments would have been required to be made if such amounts had not become immediately due and payable (see further the sections entitled "Form of AGE Financial Guarantee" and "Form of AGM Financial Guarantee" below).

Withholding Tax

If any withholding tax is imposed on payments under the Bonds or the Financial Guarantees, the Financial Guarantors are not required to "gross up" payments to the holders of the Bonds. In such circumstances, holders of the Bonds will receive payments from the Financial Guarantors net of such withholding tax (see further the sections entitled "Form of AGE Financial Guarantee" and "Form of AGM Financial Guarantee" below).

Risks relating to the Bonds and the Market

Indexation in respect of Bonds

The calculation of principal and interest will be affected by changes in the Index (as defined in Condition 7 (*Indexation*)). Potential investors should be aware that:

(a) the market price of such Bonds may be volatile;

(b) the Index may be subject to significant fluctuations that may not correlate with changes in other indices; and

(c) the timing of changes in the Index may affect the actual yield to investors, even if the average level is consistent with their expectations. In general, the earlier the change in the Index, the greater the effect on yield.

In addition, there is a risk that there will be a mismatch between indexed amounts payable under the Project Agreement and indexed amounts payable under the Bonds, as the Bonds are subject to indexation twice a year on each Scheduled Payment Date and amounts payable under the Project Agreement are subject to indexation once a year in September using RPI from the December 21 months before.

Interest Rate Risks

Since the Bonds bear interest at fixed rate (which is subject to indexation), investment in the Bonds involves the risk that subsequent changes in market interest rates may adversely affect the value of the Bonds.

Modification, Waivers and Substitution

The Conditions contain provisions for calling meetings of Bondholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Bondholders including Bondholders who did not attend and vote at the relevant meeting and Bondholders who voted in a manner contrary to the majority.

If it is then the Controlling Creditor, subject to clause 5 (*Consent of Controlling Creditor and Entrenched Rights and Reserved Matters of Senior* Creditors) of the Security Trust and Intercreditor Deed, the Bond Trustee may, without the consent of the Bondholders, Receiptholders or Couponholders concur with the Issuer, the Financial Guarantors or any other relevant parties in making:

(a) any modification to the Conditions, the Bond Trust Deed, the Financial Guarantees, the Security Documents, the Collateral Deed and the Finance Documents which is in the opinion of the Bond Trustee of a formal, minor or technical nature or is made to correct a manifest error; and

(b) any other modification of any such document which is in the opinion of the Bond Trustee not materially prejudicial to the interests of Bondholders.

For the avoidance of doubt, and notwithstanding the foregoing, the Bond Trustee shall have the unfettered right to seek the consent of Bondholders to the making of any such modification and provided further that no such direction or an Extraordinary Resolution shall affect any authorisation or waiver previously given.

If the Bond Trustee is then the Controlling Creditor, subject to clause 5 (*Consent of Controlling Creditor and Entrenched Rights and Reserved Matters of Senior Creditors*) of the Security Trust and Intercreditor Deed, the Bond Trustee may also, without the consent of any of the Bondholders, Receiptholders or Couponholders, waive or authorise any Event of Default, any Potential Event of Default, any Financial Guarantor Default or any Financial Guarantor Downgrade Event or any other breach or proposed breach of the Bond Trust Deed, the Bonds, the Financial Guarantees, the Security Trust and Intercreditor Deed or any other Relevant Document to which it is a party, or determine that any Financial Guarantor Default or any Financial Guarantor Downgrade or any Event of Default or any Potential Event of Default shall not, or shall not subject to specified conditions, be treated as such or, in the case of a Financial Guarantor Default or Financial Guarantor Downgrade Event, has been cured to its satisfaction, if the Bond Trustee is of the opinion that so to do will not be materially prejudicial to the interests of the Bondholders.

For the avoidance of doubt, the Bond Trustee, if it is then the Controlling Creditor, shall have the unfettered right to seek the consent of Bondholders to any such authorisation or waiver and provided further that no such direction or an Extraordinary Resolution shall affect any authorisation or waiver previously given.

The secondary market generally

The Bonds may have no established trading market when issued and one may never develop. If a market does develop, it may not be very liquid. Therefore, investors may not be able to sell the Bonds easily or at prices that will provide them with a yield comparable to similar investments that have a developed secondary market. Illiquidity may have a materially adverse effect on the market value of the Bonds.

An active trading market for the Bonds may not develop

There can be no assurance that an active trading market for the Bonds will develop, or, if one does develop, that it will be maintained. If an active trading market for the Bonds does not develop or is not maintained, the market or trading price and liquidity of the Bonds may be adversely affected. The Issuer or its Affiliates (as defined below) are entitled to issue further Bonds. Such transactions may favourably or adversely affect the price development of the Bonds. If additional and competing products are introduced in the markets, this may adversely affect the value of the Bonds.

Scope of cover under the Financial Guarantees

Save as set out below, the coverage provided by the Financial Guarantees is the payment of scheduled payments of principal and interest only, and does not cover any amounts due in respect of the Bonds:

(a) attributable to any increase in interest margin, penalty or other sum payable by the Issuer for whatever reason;

(b) attributable to any present or future taxes, duties, withholding, deduction, assessment or other charge imposed by the laws any sovereign state (including the United Kingdom), or any political subdivision or governmental or taxing authority thereof, (including interest and penalties in respect of such taxes, duties, withholding, deduction, assessment or other charge) with respect to any payment by the Issuer due under the Bonds or any gross-up or make whole

payment payable by the Issuer in respect of any such taxes, duties, withholding, deduction, assessment or other charge;

(c) attributable to any default interest;

(d) attributable to any amount relating to prepayment, early redemption, broken-funding indemnities, penalties, premium, "spens", any make-whole amount or similar types of payments payable in respect of the Bonds; or

(e) in respect of which AGM or AGE has made an Accelerated Payment (as defined in the relevant Financial Guarantee) on or prior to a Scheduled Payment Date.

Rating of the Bonds

The rating anticipated to be assigned to the Bonds are based on the financial strength rating of the Financial Guarantors and reflect only the views of S&P.

A rating is not a recommendation to buy, sell or hold securities and will depend, amongst other things, on certain underlying characteristics of the business and financial condition of the Financial Guarantors from time to time.

There is no assurance that any such rating will continue for any period of time or that they will not be reviewed, revised, suspended or withdrawn entirely by S&P as a result of changes in, or unavailability of, information or if, in S&P's judgment, circumstances so warrant. If any rating assigned to the Bonds is lowered or withdrawn, the market price of the Bonds is likely to be reduced and no person or entity will be obliged to provide any additional credit enhancement in respect of the Bonds.

The Financial Guarantors have not covenanted to maintain any ratings by S&P or S&PGRS or any other rating agency during the life of the Bonds.

Priority of Claims

The Security Trust and Intercreditor Deed provides for an order of priority of payment under which the proceeds of enforcement of the security and the joint and several guarantees granted by the Obligors are to be applied following enforcement of such security. This is relevant to Bondholders to the extent that an amount due to be paid to the Bondholders is not covered by, or paid under, the Financial Guarantees (see the sections entitled "*Form of AGE Financial Guarantee*" and "*Form of AGM Financial Guarantee*" below).

Certain claims of the other Senior Creditors will, in accordance with such order of priority, be paid in priority to payment of certain amounts due to the Bondholders (see the section entitled "*Refinancing of the Project – The Security Arrangements – Security Trust and Intercreditor Deed*" below).

Mandatory Early Redemption of the Bonds

Following termination of the Project Agreement, the University must pay Compensation on Termination to ProjectCo aimed at ensuring, amongst other things, that ProjectCo can prepay the Issuer under its on-loan agreement thus enabling the Issuer to redeem the Bonds.

The level of Compensation on Termination due to ProjectCo depends on the ground for termination of the Project Agreement.

If the Project Agreement is terminated as a result of a University Termination Event (being broadly the termination of the Project Agreement by ProjectCo following a default by the University) or a Compulsory Change Termination Event (being broadly the termination of the Project Agreement following a Compulsory Change Event), the amount of Compensation on Termination due should be sufficient to compensate the holder of each Bond at the higher of that Bond’s outstanding principal amount (adjusted for indexation) and an amount calculated by discounting the remaining principal and interest payments in respect of that Bond in accordance with Condition 6(b), each with accrued interest.

If the Project Agreement is terminated as a result of a ProjectCo Termination Event (being broadly the termination of the Project Agreement following a default by ProjectCo), the amount of Compensation on Termination due should be sufficient to compensate the holder of each Bond at that Bond's outstanding principal amount (adjusted for indexation), with accrued interest.

If the Compensation on Termination is sufficient to, regardless of the ground for termination of the Project Agreement, repay all amounts outstanding under the Senior Finance Documents, including any spens and similar amounts payable to compensate for early termination, as certified by the Security Trustee under the Security Trust and Intercreditor Deed, then the Bonds will be redeemed ten days after ProjectCo receives the Compensation on Termination. See Condition 6(d) (*Mandatory Early Redemption – University Termination Event and Compulsory Change Termination Event*) and Condition 6(e) (*Mandatory Early Redemption – ProjectCo Termination Event*).

If the Compensation on Termination is not sufficient to, regardless of the ground for termination of the Project Agreement, repay all of the amounts outstanding under the Senior Finance Documents described above:

A. in the case of a mandatory early redemption under Condition 6(d) (*Mandatory Early Redemption – University Termination Event and Compulsory Change Termination Event*):

   i. where the Compensation on Termination is sufficient to pay the aggregate principal amount outstanding on the Bonds, adjusted for indexation and all amounts payable in priority thereto in accordance with the Security Trust and Intercreditor Deed, then, subject as provided below, each Bond will be redeemed at its Indexed Par Amount (plus its *pro rata* share of any amounts in excess thereof) ten days after ProjectCo receives the Compensation on Termination; or

   ii. where the Compensation on Termination is not sufficient to pay the aggregate principal amount outstanding on the Bonds, adjusted for indexation and all amounts payable in priority thereto in accordance with the Security Trust and Intercreditor Deed, then, subject as provided below, each Bond will be redeemed at its *pro rata* share of the Compensation on Termination ten days after ProjectCo receives the Compensation on Termination; and

B. in the case of a mandatory early redemption under Condition 6(e) (*Mandatory Early Redemption – ProjectCo Termination Event*), subject as provided below, each Bond will be redeemed at its pro rata share of the Compensation on Termination ten days after ProjectCo receives the Compensation on Termination.

Notwithstanding the above, in any case where the Compensation on Termination is not sufficient to repay all of the amounts outstanding under the Senior Finance Documents, holders of at least 25 per cent. of the aggregate principal amount outstanding of the Bonds may, through an instruction of the Bond Trustee in writing or by Extraordinary Resolution, elect not to receive such amounts but to be paid the Scheduled Payments under the Financial Guarantees. This election may be overridden at any time by the Financial Guarantors, who may choose to accelerate payments. See Condition 6(d) (*Mandatory Early Redemption – University Termination Event and Compulsory Change Termination Event*) and Condition 6(e) (*Mandatory Early Redemption – ProjectCo Termination Event*).

The Financial Guarantors are not liable to pay any amounts in excess of the Indexed Par Amount. Payment of the difference between the Compensation on Termination and the Indexed Par Amount will be paid by the Financial Guarantors on the Scheduled Payment Dates even if the Bonds are redeemed early, unless the Financial Guarantors decide to accelerate such payments. Therefore, if the Compensation on Termination is not sufficient to repay all amounts outstanding to the Senior Creditors, Bondholders are subject to the following risks:

- that they elect to receive payments on the Scheduled Payment Dates rather than on an accelerated basis but the Financial Guarantors nevertheless decide to pay on an accelerated basis, and

- if the Compensation on Termination is not sufficient to pay the aggregate principal amount outstanding on the Bonds, adjusted for indexation and all amounts payable in priority thereto in accordance with the Security Trust and Intercreditor Deed, that they receive part of the payment on an accelerated basis and the balance on each Scheduled Payment Date.

Mandatory Early Redemption of the Bonds where the Controlling Creditor allows the University to pay in instalments

If a ProjectCo Termination Event (being broadly the termination of the Project Agreement by the University following a default by ProjectCo) has occurred, the University may request that the Service Provider Default Sum (as defined in the Project Agreement) be payable in instalments rather than in a lump sum. However, the University's ability to pay the Service Provider Default Sum by instalments is at the sole and absolute discretion of the Controlling Creditor.

Should the Controlling Creditor permit the University to pay the Compensation on Termination in instalments, the Issuer, the Controlling Creditor and, where the Bond Trustee is not the Controlling Creditor, the Bond Trustee shall agree revisions to the schedule of payments set forth in column B of Condition 9(a) (*Scheduled Payments*). See Condition 6(f) (*Mandatory Early Redemption – ProjectCo Termination Even (and the Controlling Creditor allows the University to exercise its instalment option*).

In this situation, certain Bondholders may have the repayment profile of their Bonds amended in a way that is not envisaged on the date such Bonds were acquired.

Changes to the risk weighted asset framework

In Europe, the U.S. and elsewhere there is increased political and regulatory scrutiny of the asset-backed securities industry. This has resulted in numerous measures for increased regulation which are currently at various stages of implementation and which may have an adverse impact on the regulatory capital charge to certain investors and/or the incentives for certain investors to invest in securities issued under such structures, and may thereby affect the price and liquidity of such securities. The exact scope of this increased regulation is often unclear and it is possible that it could be argued that the Bonds were subject to some or all of it.

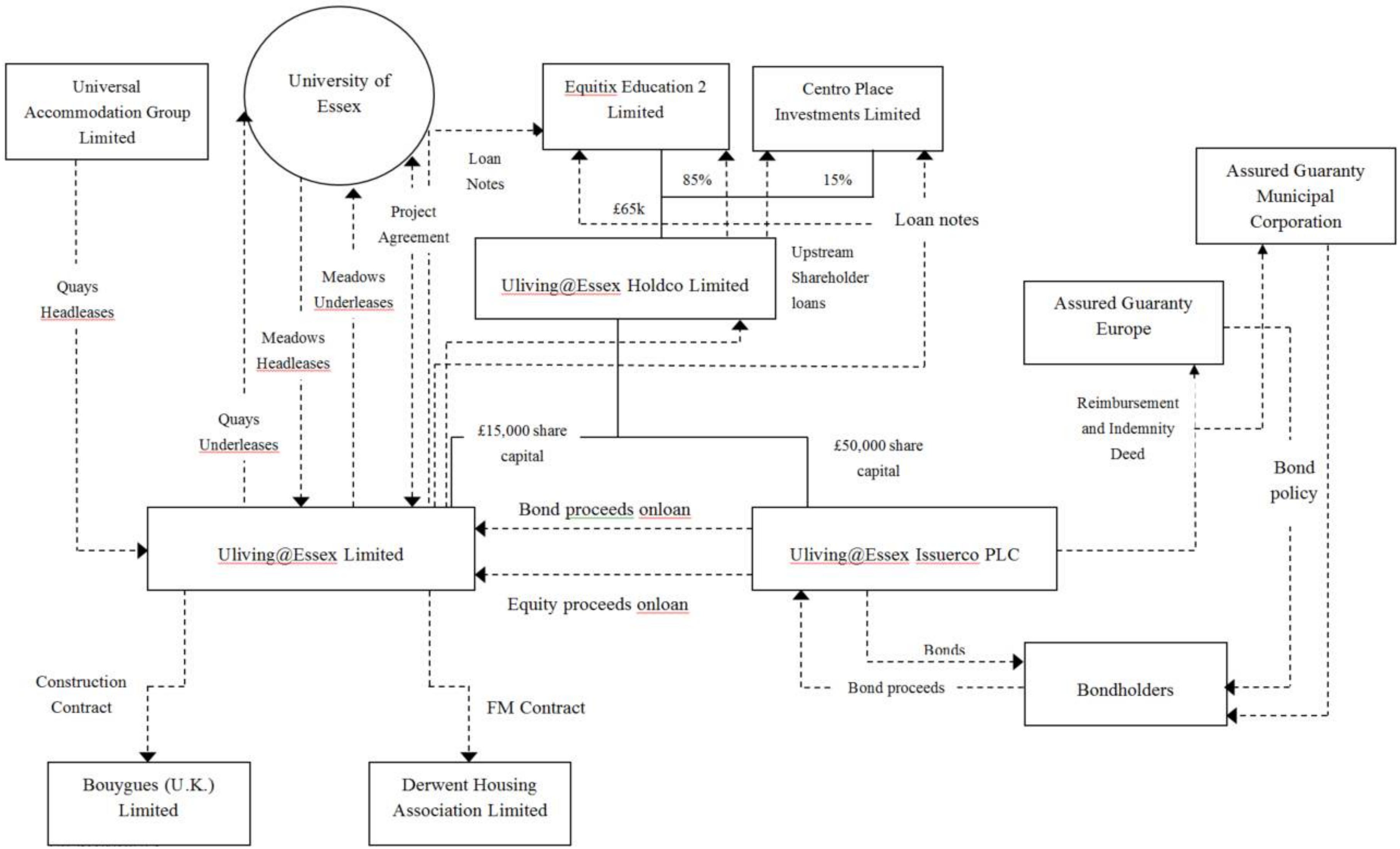
Investors in the Bonds are responsible for analysing their own regulatory position and neither the Issuer nor the Manager accept responsibility for the regulatory treatment of their investment in the Bonds. Investors should consult their own advisers as to the regulatory capital requirements in respect of the Bonds and as to the consequences and effect on them of any pending or future regulatory changes. No predictions can be made as to the precise effects of such matters on any investor or otherwise.

Liability of the Bond Trustee and the Security Trustee

Neither the Bond Trustee nor the Security Trustee will be responsible for (a) monitoring or supervising the performance by the Issuer or any other party to the transaction documents of their respective functions and obligations under the transaction documents or the operation of any account opened pursuant to the transaction documents and each of the Bond Trustee and the Security Trustee will be entitled to assume, until it has written notice to the contrary, that all such persons are properly performing their duties, or (b) considering the basis on which approvals or consents are granted by the Issuer, the Controlling Creditor or any other party to the transaction documents under the transaction documents. Neither the Bond Trustee nor the Security Trustee will be liable to any Bondholder or other Senior Creditor for any failure to make or to cause to be made on its behalf the searches, investigations and enquiries which would normally be made by a prudent chargee in relation to the secured assets and has no responsibility in relation to the legality, validity, value, sufficiency and enforceability of the transaction security and the Relevant Documents.

Unless the Security Trustee is satisfied that it will not incur any liability (whether environmental or otherwise) arising from it enforcing the security, or that it is prefunded and/or indemnified and/or secured to its satisfaction in respect of any such liability, it will not be obliged to enforce the security when instructed to do so by the Controlling Creditor.

The chart below shows the corporate structure and the principal Finance Documents and Project Documents.



SUMMARY OF THE PROJECT

The following is a summary of the Project. It should be read in conjunction with the rest of this Prospectus.

ProjectCo entered into a project agreement (the "**Project Agreement**") with the University of Essex (the "**University**") dated 7 August 2012. Under the Project Agreement, ProjectCo:

(a) has designed and built new student accommodation (known as the Meadows Phase 1 Residential Premises and other facilities (the **Meadows Premises**").

(b) acquired the existing University accommodation known as the Quays (the "**Quays Premises**")), together with all supporting infrastructure, external hard-standings, specialist surfaces and other amenities (the Quays Premises and the Meadows Premises, together the "**Accommodation**"); and

(c) is providing "**core**" facilities management and lifecycle services for the Accommodation;

(collectively, the "**Project**").

Construction of the Meadows Premises concluded in September 2013. The refurbishment works at the Quays Premises was undertaken in stages: the Quays Works completed on 24 September 2013; the catch-up works completed on 24 September 2013; and the Further Works completed on 24 September 2014.

The Project Agreement expires at the end of the 50th consecutive Contract Year (a "**Contract Year**" being 7 August 2012 to 31 August 2013, and then twelve month periods commencing on 1 September) following the last Service Commencement Date (30 January 2014) unless terminated earlier in accordance with its terms (the "**Term**").

The University granted headleases to ProjectCo for the Meadows Premises to take effect from the Original Financial Close Date for a term of 50 years. ProjectCo granted underleases back to the University for the Meadows Premises for a term commencing on 30 January 2014 and ending on 1 July 2063. Such underleases terminate on determination of the headleases.

The Universal Accommodation Group Limited granted headleases to ProjectCo for the Quays Premises to take effect from 8 July 2013 for a term of 50 years. ProjectCo granted underleases to the University for the Quays Premises for a term commencing on 8 July 2013 and ending on 1 July 2063. Such underleases terminate on determination of the headleases.

The headleases grant ProjectCo an option to extend the term of its interest by taking new leases for a term ending on the 109th anniversary of the commencement of the contractual term (7 August 2012 in respect to the Meadows Premises and 8 July 2013 in respect to Quays Premises).

The University grants licences of rooms and flats within the Accommodation to the occupational students and, where permitted, to other persons (the "**occupational tenants**") under a form of student licence.

ProjectCo must provide “core” facilities management and lifecycle services (the "**Core Services**") to the Accommodation. It does this under a sub-contract (the "**FM Service Contract**") with Derwent Housing Association Limited (the "**FM Service Contractor**"). This provides that the FM Service Contractor must carry out the facilities management. This includes planned and reactive maintenance, the repair, renewal and replacement of fixtures and fittings, major plant and machinery lifecycle, cleaning, security, car parking and IT services.

Demand risk

The Project is demand based and the sole source of income in the operational period is the income that is derived from the rents paid by occupational tenants.

The University is entitled to "**nominate**" annually all or any of the rooms or flats comprised in the Accommodation. If a room or flat is nominated (collectively referred to as "**Reserved Rooms**") then

the University will be obliged to pay the rent attributable to the Reserved Rooms for the full year, even if no occupational tenant is found or if there is one and he or she ceases to be an occupational tenant or fails to pay the rent due. For Reserved Rooms, the University takes credit and void risk in exchange for a charge equal to a portion of the rent.

If the University does not nominate, it is required to market the non-nominated rooms or flats (collectively referred to as the "**Non-Reserved Rooms**"). ProjectCo also has rights to market Non-Reserved Rooms. Where an occupational tenant is found for a Non–Reserved Room, the University takes credit risk in exchange for a charge equal to a portion of the rent and most of the void risk if that tenant is a student of the University.

The University must make regular payments (the "**Total Reserved Rent**") to ProjectCo (see the section entitled "*Summary of the Project Documents – The Project Agreement – Payment*" below).

The rent for rooms and flats comprised within the Premises is set annually (see the section entitled "*Summary of the Project Documents – The Project Agreement – Rent Setting*" below). The forecast base rent is indexed annually and adjusted to record specified additional costs.

REFINANCING OF THE PROJECT

The following is a summary of the refinancing of the Project and should be read in conjunction with the rest of this Prospectus. The summaries of the documents do not purport to be complete and are subject to the detailed provisions of the relevant documents.

1. General

ProjectCo's indebtedness in respect of the Project will be refinanced by:

(a) the proceeds of the issue of the Bonds by the Issuer (see the section entitled "Overview of the Bond Issue" above) which proceeds will be on-lent by the Issuer to ProjectCo pursuant to an Issuer On-Loan Agreement between the Issuer and ProjectCo dated on or about the Issue Date. ProjectCo will receive or be deemed to receive an amount equal to the gross proceeds of the Bonds and ProjectCo shall be responsible for various transaction costs;

(b) the £50,000 paid up share capital of the Issuer.

The Bonds (excluding those held by or on behalf of any Obligor or any Affiliate of an Obligor or Shareholder of an Obligor) will have the benefit of the Financial Guarantees. Under each of the Financial Guarantees, AGE or AGM, as the case may be, unconditionally and irrevocably guarantees in favour of the Bond Trustee amounts unpaid by the Issuer in respect of scheduled payments of principal and interest (in each case adjusted for indexation, but excluding in each case any amounts due in respect of the Bonds (i) attributable to any increase in interest margin, penalty or other sum payable by the Issuer for whatever reason; (ii) attributable to any present or future taxes, duties, withholding, deduction, assessment or other charge (including interest and penalties in respect of such taxes, duties, withholding, deduction, assessment or other charge) of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state (including the United Kingdom), or any political subdivision or governmental or taxing authority therein or thereof; (iii) attributable to any default interest; (iv) attributable to any amount relating to prepayment, early redemption, broken-funding indemnities, penalties, premium, "**spens**", any make-whole amount or similar types of payments payable in respect of the Bonds; or (v) in respect of which AGM or AGE has made an Accelerated Payment (as defined in the relevant Financial Guarantee) on or prior to a Scheduled Payment Date.

Under a Reimbursement and Indemnity Deed to be entered into between the Obligors, AGE and AGM (the "**Reimbursement and Indemnity Deed**") on or before the Issue Date, the Obligors agree to reimburse AGE and AGM for any payments made by them under the Financial Guarantees. In addition AGE and AGM will be subrogated to the rights of the Bondholders and the Bond Trustee in respect of any payments made by AGE or AGM under the relevant Financial Guarantee. The rights to reimbursement of AGE and AGM in respect of the relevant Financial Guarantees will have the benefit of the security granted by the Obligors to the Security Trustee. Under the terms of the Collateral Deed, the Obligors will grant a joint and several guarantee of their obligations to make, *inter alia*, reimbursements to AGE and AGM under the Reimbursement and Indemnity Deed.

Payments in respect of the Bonds will be made pursuant to the paying agency agreement (the "**Paying Agency Agreement**", which expression includes any modification or supplement thereto) to be entered into on or before the Issue Date between the Issuer, the Financial Guarantors, the Bond Trustee, The Bank of New York Mellon, acting through its London Branch as principal paying agent (the "**Principal Paying Agent**", which expression includes any successor principal paying agent under the Paying Agency Agreement) and as paying agent (the "**Paying Agent**" and together with the Principal Paying Agent, the "**Paying Agents**", which expression shall include any additional or successor paying agent appointed in accordance with the Paying Agency Agreement).

The Issuer will pay or procure to be paid to:

(a) the Financial Guarantors that portion of the financial guarantee fee which is payable in accordance with the Financial Guarantee Fee Letters in consideration for the issuance of the Financial Guarantees;

(b) the Bond Trustee for its services as Bond Trustee remuneration on the issue of the Bonds and on each anniversary of the issue of the Bonds and upon such terms as agreed with the Issuer;

(c) the Security Trustee, for its services as Security Trustee, fees and remuneration and upon such terms as may from time to time be agreed between the relevant Obligor and/or AGE and/or AGM and the Security Trustee under the relevant Finance Documents;

(d) the Principal Paying Agent (for the account of the Paying Agents) for their services as Paying Agents under the Paying Agency Agreement, fees in such amounts and upon such terms as agreed by the Issuer;

(e) the Manager, an arrangement fee on the Issue Date; and

(f) the Manager, all fees, costs and expenses payable in connection with the listing and structuring of the Bonds on the Issue Date upon such terms as agreed by the Issuer.

The Issuer will also pay to each of the Bond Trustee, Security Trustee, the Paying Agents, the Manager and the Financial Guarantors their fees, costs, charges, liabilities and expenses in connection with the issue of the Bonds, upon such terms as agreed by the Issuer. Other fees are also payable to each of the Bond Trustee, the Security Trustee and the Principal Paying Agent under the Finance Documents.

The Collateral Deed

The following is a summary of certain of the provisions of the Collateral Deed. It is not exhaustive and is subject to the Collateral Deed's detailed provisions. Capitalised terms used in this section entitled "Collateral Deed" have the meanings given to them in the Master Definitions Schedule unless otherwise defined. Copies of the Collateral Deed are available for inspection by Bondholders during normal business hours at the specified offices (as set out below) of each of the Paying Agents.

On or before the Issue Date, the Obligors, the Security Trustee, the Bond Trustee and the Financial Guarantors will enter into the collateral deed (the "**Collateral Deed**") in which the Obligors will give certain representations and covenants to, *inter alios*, the Financial Guarantors, the Bond Trustee and the Security Trustee.

Definitions

"**Bond Documents**" means the Bonds, the Bond Trust Deed (including the Conditions of the Bonds), the Paying Agency Agreement, the Issuer ICSD Agreement, the Effectuation Authorisation Agreement, the Subscription Agreement and any other agreements or documents between any Obligor and any Senior Creditor which the Controlling Creditor may, from time to time, designate as a Bond Document.

"**Building Contractor Guarantee**" means the guarantee confirmed on or about the Issue Date given by the Building Contractor Guarantor in favour of ProjectCo, of the obligations of the Building Contractor under the Building Contract, or any other guarantee in form and substance acceptable to the Controlling Creditor provided from time to time in respect of any Building Contractor in accordance with the Collateral Deed.

"**Building Contractor Guarantor**" means Bouygues Batiment International or any other person or persons from time to time acceptable to the Controlling Creditor guaranteeing the obligations of the Building Contractor under the Building Contract in accordance with the Collateral Deed.

"**Building Contract**" means the agreement dated 7 August 2012 between ProjectCo and the Building Contractor, as amended, relating to the design, construction and completion of the works by the Building Contractor and includes any other agreement entered into by ProjectCo in relation to the design, construction and completion of the works.

"**Controlling Creditor**" has the meaning given to it in section 3, "*The Security Arrangements — Security Trust and Intercreditor Deed*" below.

"**Direct Agreements**" means the Funders' Direct Agreement, the FM Service Contractor Direct Agreement, Building Contractor Direct Agreement and any other agreements or documents between any Obligor and any Senior Creditor which the Controlling Creditor may from time to time designate as a Direct Agreement.

"**Equity On-Loan**" means the equity on-loan made available to ProjectCo under the Issuer On-Loan Agreement pursuant to which the Issuer lends the proceeds of subscription of its shares by HoldCo.

"**Finance Documents**" means the Senior Finance Documents and the Junior Finance Documents.

"**Financial Guarantors**" means, unless AGE and AGM jointly notify the Obligors, the Security Trustee, the Bond Trustee, the Paying Agents and the Account Bank that AGM or AGE or an affiliate of AGE and/or AGM (as applicable) will assume such role, for the purposes of the Finance Documents:

(a) AGE on its behalf and on behalf of AGM, in the context of:

(i) delivering information or notices;

(ii) consenting to any agreement;

(iii) providing instructions;

(iv) acting as Controlling Creditor;

(v) providing an opinion;

(vi) granting approvals; and/or

(vii) anything being satisfactory to the Financial Guarantors,

(b) both AGE and AGM, in the context of:

(i) signatories or officers; and/or

(ii) receiving information and/or notices, subject to clause 21.2 (Electronic Communication) of the Collateral Deed;

(c) AGE, in the context of the AGE Financial Guarantee in its capacity as "Financial Guarantor" therein; and

(d) AGM, in the context of the AGM Financial Guarantee in its capacity as "Financial Guarantor" therein;

"**Global Deed of Release**" means the deed of release in relation to the Existing Aviva Security, including inter alia, the existing debenture dated 7 August 2012 between ProjectCo and the Aviva Commercial Finance Limited and the existing debenture dated 7 August 2012 between HoldCo and the Aviva Commercial Finance Limited.

"**HoldCo Debenture**" means the first ranking debenture dated on or about the Issue Date given by HoldCo in favour of the Security Trustee.

"**Issuer On-Loan Agreement**" " means the intercompany loan agreement dated on or about the Issue Date between the Issuer (as lender) and ProjectCo (as borrower) pursuant to which the proceeds of the issue of the Bonds and an equity loan are on-lent to ProjectCo.

"**Issuer Debenture**" " means the first ranking debenture dated on or about the Issue Date given by the Issuer in favour of the Security Trustee.

"**Junior Finance Documents**" means the Shareholders' Agreement, the ProjectCo Loan Note Instrument, any ProjectCo Loan Notes, (in respect of the Equity On-Loan only) the Issuer On-Loan Agreement and any other agreements or documents which any Obligor and the Controlling Creditor may from time to time designate as a Junior Finance Document.

"**Master Definitions Schedule**" means the master definitions schedule dated on or about the Issue Date between, *inter alios*, the Obligors and the Financial Guarantors.

"**Material Adverse Effect**" is to be construed as a reference to an event or matter which, in the opinion of the Controlling Creditor (acting reasonably), might have a material adverse effect on:

(a) the present or future financial condition of any Obligor;

(b) the present or future ability of any Obligor duly to perform all or any of its material obligations (including, without limitation, its payment obligations) which it is expressed to undertake under any of the Relevant Documents (other than the Junior Finance Documents); or

(c) the interests of any of the Senior Creditors under the Senior Finance Documents.

"**Material Project Parties**" means:

(a) the Issuer;

(b) HoldCo;

(c) ProjectCo;

(d) each Parallel Loan Provider; and

(e) the FM Service Contractor,

and Material Project Party means any of them.

"**Parallel Loan Agreements**" means the loan agreement between ProjectCo and the Parallel Loan Provider in respect of:

(a) the Building Contract; and

(b) the FM Service Contract.

"**Parallel Loan Provider**" means, as applicable, the FM Service Contractor and the Building Contractor and/or any other person or persons providing loan agreements under agreements replacing either of the Parallel Loan Agreements.

"**Project Documents**" means:

(a) the Project Agreement;

(b) the Agreement for Lease;

(c) the Leases;

(d) the Building Contract;

(e) the FM Service Contract;

(f) the Interface Agreement;

(g) the Guarantees;

(h) the Parallel Loan Agreement; and

(i) such other documents as may from time to time be agreed between the Controlling Creditor and ProjectCo (each acting reasonably) to be a Project Document,

and Project Document means any one of them.

"**ProjectCo Loan Notes**" means the loan notes issued by ProjectCo and subscribed for by the Stockholders pursuant to the ProjectCo Loan Note Instrument.

"**ProjectCo Loan Note Instrument**" means the instrument dated 7th August 2012 constituting the ProjectCo Loan Notes (as amended by the amendment letter dated on or before Financial Close).

"**ProjectCo Debenture** " means the first ranking debenture dated on or about the Issue Date given by ProjectCo in favour of the Security Trustee.

"**Relevant Documents**" means the Project Documents and the Finance Documents and a Relevant Document means any one of these.

"**Secured Obligations**" means all money or liabilities due, owing or incurred to any Senior Creditor by any Obligor under any Finance Document at present or in the future, in any manner whether actual or contingent, whether incurred solely or jointly with any other person and whether as principal or surety, together with all interest accruing thereon.

"**Security Documents**" means the ProjectCo Debenture, the HoldCo Debenture, the Issuer Debenture, the Security Trust and Intercreditor Deed and any other document from time to time executed in favour of the Security Trustee for the purpose of securing all or any of the Secured Obligations and any deed of accession entered into in respect of any of the above.

"**Senior Creditors**" means each of the Financial Guarantors, the Bond Trustee, the Bondholders, the Paying Agents, the Account Bank and the Security Trustee and Senior Creditor means each such person.

"**Senior Finance Documents**" means:

(a) the Collateral Deed;

(b) the Master Definitions Schedule;

(c) the Security Documents;

(d) the Accounts Agreement;

(e) the Bond Documents;

(f) each Financial Guarantee;

(g) the Reimbursement and Indemnity Deed;

(h) each Financial Guarantee Fee Letter,

(i) (save in respect of the Equity On-Loan) the Issuer On Loan Agreement;

(j) the Direct Agreements;

(k) the ICA Deed of Novation;

(l) the Assignment of Collateral Warranties;

(m) the Global Deed of Release; and

(n) any other agreements or documents between any Obligor and any Senior Creditor which the Controlling Creditor may from time to time designate as a Senior Finance Document;

and **Senior Finance Document** means any one of them.

"**Shareholder**" means the person who holds shares in HoldCo from time to time, being as at the Issue Date, Equitix Education and Centro.

"**Shareholders' Agreement**" means the shareholder's agreement dated on or about the Issue Date between the Shareholders, the Issuer, HoldCo and ProjectCo.

"**Stockholders**" means Equitix Education and Centro and Stockholder means any one of them.

"**University**" means the University of Essex.

Covenants by the Obligors

The covenants contained in the Collateral Deed will, *inter alia*, require the Obligors (subject, in some cases, to agreed exceptions, *de minimis* amounts and qualifications as to materiality):

(a) to comply with the terms of the Relevant Documents to which they are a party;

(b) not to create or permit to subsist any encumbrance over all or any of their present or future rights, claims, revenues or assets except as permitted in the Collateral Deed;

(c) not to incur, assume or permit to exist any financial indebtedness except as permitted in the Collateral Deed;

(d) not to make any loans except as permitted in the Collateral Deed;

(e) not to dispose of assets except as permitted in the Collateral Deed; and

(f) not voluntarily to enter into liquidation, dissolution or voluntarily enter into a merger or consolidation with any other person.

Covenants by ProjectCo

The covenants contained in the Collateral Deed will, inter alia, require ProjectCo (subject, in some cases, to agreed exceptions, de minimis amounts and qualifications as to materiality):

(a) to maintain specified levels of insurance with insurers of certain acceptable rating levels;

(b) to replace the FM Service Contract in accordance with the Collateral Deed;

(c) to carry out the Services in accordance with, inter alia, the Project Documents;

(d) not to make any loan or provide any other form of credit or make any deposit with any person except deposits made in the Accounts, in accordance with any of the Senior Finance Documents (including the loans pursuant to the Junior Finance Documents) or in accordance with the ProjectCo Upstream Shareholder Loan Agreements;

(e) not to enter into any material transaction with any person except on the basis of an arm's length transaction, except as permitted in the Collateral Deed;

(f) not to carry on any business or engage in any business other than the Project or engage in any business or activity other than as expressly permitted by the Senior Finance Documents; and

(g) not to incur expenditures or commitments for expenditures for fixed and other non-current assets, tax or operating expenditure, except as permitted in the Collateral Deed.

Trigger Events and Remedial Plan Trigger Events

Following the occurrence of any of the trigger events ("**Trigger Events**") or remedial plan trigger events ("**Remedial Plan Trigger Events**") specified in the Collateral Deed, unless such Trigger Event or Remedial Plan Trigger Event has been waived or deemed remedied in accordance with the Collateral Deed or otherwise remedied to the satisfaction of the Controlling Creditor, the Controlling Creditor will have certain additional rights to investigate, monitor and influence certain of the activities of ProjectCo. This will include appointing experts and providing the Controlling Creditor with any other additional information the Controlling Creditor may reasonably request including updates as to the steps taken and progress made towards remedying the relevant Trigger Event and, in the case of Remedial Plan Trigger Events, agreeing a remedial plan with ProjectCo. Until a Trigger Event or Remedial Plan Trigger Event has been waived or deemed remedied or remedied to the satisfaction of the Controlling Creditor, ProjectCo will not be permitted to pay any dividends or make any distributions or other similar payments to the ProjectCo Distribution Account.

The Trigger Events and Remedial Plan Trigger Events will include, *inter alia*:

(a) the occurrence of any Potential Event of Default (as defined below) or Event of Default (as defined below);

(b) ProjectCo being issued with a certain number of Service Warning Notices within a certain time period pursuant to the Project Agreement; or

(c) certain specified financial coverage ratios not being met by ProjectCo on the dates they are required by the Collateral Deed to be tested.

Events of Default

The Collateral Deed provides that the occurrence of any of the following events of default (amongst others) will constitute an event of default ("**Event of Default**"), unless and until such Event of Default has been remedied to the satisfaction of the Controlling Creditor or waived for the purposes of the Collateral Deed. Events of Default will include (subject, in some cases, to agreed exceptions, de minimis amounts and qualifications as to materiality):

(a) failure by any Obligor to pay any sum due from it under any of the Senior Finance Documents within, other than with respect to the Bonds, certain specified grace periods;

(b) any representation or statement made or repeated by any Obligor in the Senior Finance Documents or certain documents pursuant to or in connection with any Senior Finance Document is, or proves to have been, incorrect or misleading in any material respect and, in specified cases, if it has or would reasonably be expected to have a Material Adverse Effect;

(c) failure by any Obligor duly to perform or comply with certain specified covenants and obligations under the Collateral Deed or other Senior Finance Documents subject to specified grace periods and materiality or implementation of an agreed remedial plan;

(d) breach or default by any Obligor under any agreement to which it is a party or which is binding on it or any of its assets, and which failure, breach or default could reasonably be expected to a Material Adverse Effect;

(e) the appointment of a liquidator, receiver, administrator, administrative receiver or similar officer or any other insolvency and rescheduling event, winding up event or creditor's process or analogous event in terms of the Collateral Deed occurs with respect to any Obligor, or any other Material Project Party subject to materiality, remedy or replacement provisions;

(f) by or under the authority of any government, the management as a whole of any Obligor is wholly or materially displaced or the authority of any Obligor in the conduct of its business is wholly or materially curtailed or fettered or all or a majority of the shares of any Material Project Party is seized, nationalised, expropriated or compulsorily acquired, or the Project Agreement is voluntarily terminated by the University;

(g) subject to materiality, ProjectCo or certain other parties do not have certain licences, approvals or consents necessary to carry out its business;

(h) subject to certain provisions relating to remedial plans, the occurrence of an event which, with the giving of notice, would become an event under the Project Agreement which entitles either party to terminate the Project Agreement;

(i) specified financial coverage ratios are not met by ProjectCo on the dates they are required by the Collateral Deed;

(j) ProjectCo fails to maintain the insurances required by the Collateral Deed;

(k) ProjectCo permits, recommends or agrees to the abandonment of the Project in whole or in any material part which would constitute a Default Event in accordance with the terms of the Project Agreement.

Any event which (with the passage of time, the giving of notice, the making of any determination under the Collateral Deed or any combination thereof), if not remedied or waived, would constitute an Event of Default, is a "**Potential Event of Default**".

If an Event of Default has occurred and is outstanding, the consequences may include the Controlling Creditor: (a) requiring the exercising of any remedies or rights in respect of Trigger Events or Remedial Plan Trigger Events; (b) directing the Security Trustee to exercise any rights available to the Security Trustee under the Direct Agreements; (c) directing ProjectCo to: (i) terminate any existing contract or agreement or procure the termination of the FM Service Contract (if such contract or agreement or FM Service Contract is capable of termination at such time in accordance with its terms and those of the Project Documents); (ii) making specified changes to management, systems or advisers or other operational changes; (iii) tendering for such new contracts as the Controlling Creditor may specify on a basis approved in writing by the Controlling Creditor and in any event on reasonable commercial terms; (iv) exercising any other rights expressed to arise under any Finance Document or Project Document upon an Event of Default; and (v) making, compromising, settling or discontinuing any claim which ProjectCo may have or purport to have against any other person; (d) requiring ProjectCo to pay immediately to the Senior Debt Service Account an amount equal to all outstanding amounts of principal, interest and default interest and other amounts due or owing under or relating to the Bonds and the Reimbursement and Indemnity Deed; (e) instructing the Security Trustee to take all steps necessary to enforce the Security granted by any Obligor to the Security Trustee and/or to exercise all or any other rights granted to the Security Trustee pursuant to the Senior Finance Documents and which the Security Trustee is entitled to exercise on the occurrence and continuance of an Event of Default, in each case in accordance with the terms of the Security Trust and Intercreditor Deed (as defined in "*The Refinancing of the Project — 4. The Security Arrangements — Security Trust and Intercreditor Deed*" below); (f) directing the Bond Trustee to declare that each Bond is immediately due and payable (see the sections entitled "*Terms and Conditions of the Bonds*"; (g) instructing the Security Trustee to notify the relevant underwriters or insurers that an Event of Default has occurred (provided that the Controlling Creditor shall instruct the Security Trustee to notify the relevant underwriters or insurers as soon as reasonably practicable upon the waiver or remedy of such an Event of Default); and/or (h) giving notice to the Account Bank that no further withdrawals may be made from any Account. No action is required to be taken by either the Bond Trustee or the Security Trustee unless it has been prefunded and/or indemnified and/or secured to its satisfaction.

Where there is any reference in any of the Finance Documents (other than the Funders' Direct Agreement) to the Bond Trustee (or the Controlling Creditor where it is the Bond Trustee) or the Security Trustee acting reasonably or properly, or doing an act or coming to a determination, opinion or belief that is reasonable or proper, or any similar or analogous reference, the Bond Trustee (in its capacity as such or in its capacity as Controlling Creditor) or, as the case may be, the Security Trustee should be deemed to be acting reasonably and properly or to do an act or come to a determination, opinion or belief that is reasonable if it acts on the instructions of the Controlling Creditor (in the case both of the Bond Trustee, if it is not at that time also the Controlling Creditor, and of the Security Trustee) or (in the case of the Bond Trustee) the Bondholders.

Where there is in any of the Finance Documents (other than the Funders' Direct Agreement) a provision to the effect that the Bond Trustee (or the Controlling Creditor, if it is then the Bond Trustee) or the Security Trustee is not to unreasonably withhold or delay its consent or approval, it shall be deemed not to have so withheld or delayed its consent or approval if the withholding or delay is caused by instructions being sought from the Controlling Creditor or the Bondholders and the Controlling Creditor or, as the case may be, the Bondholders withhold or delay in giving its or their consent or approval.

Each party has acknowledged and agreed that, when it is acting under or pursuant to the Finance Documents (other than the Funders' Direct Agreement), each of the Security Trustee and the Bond Trustee shall be entitled to rely on and shall have all the benefits and protection afforded to it under the Security Trust and Intercreditor Deed and the Bond Trust Deed.

The Security Arrangements

The Bonds will also have the benefit of the security arrangements summarised below. Attention is drawn to Security Trust and Intercreditor Deed below. The ability of the Bond Trustee to exercise

rights in respect of such security arrangements will be restricted by the Security Trust and Intercreditor Deed and Bondholders will have no independent entitlement to exercise such rights.

Security from the Issuer

Pursuant to an English law debenture to be granted by the Issuer in favour of the Security Trustee on or before the Issue Date (the "**Issuer Debenture**"), the obligations of the Issuer under the Finance Documents will be secured by fixed and/or floating charges in favour of the Security Trustee over substantially all the undertaking and assets, both present and future, of the Issuer, which will include, *inter alia*, charges over its credit balances, book debts and its rights in and under the Issuer On-Loan Agreement.

Security from ProjectCo

Pursuant to an English law debenture to be granted by ProjectCo in favour of the Security Trustee on or before the Issue Date (the "**ProjectCo Debenture**"), the obligations of ProjectCo under the Finance Documents will be secured by fixed and/or floating charges in favour of the Security Trustee over substantially all the undertaking and assets, both present and future, of ProjectCo, which will include, *inter alia*, charges over its credit balances, book debts, insurances and its rights in connection with the Project.

Security from HoldCo

Pursuant to an English law debenture to be granted by HoldCo in favour of the Security Trustee on or before the Issue Date (the "**HoldCo Debenture**"), the obligations of HoldCo under the Finance Documents will be secured by fixed and/or floating charges in favour of the Security Trustee over substantially all the undertaking and assets, both present and future, of HoldCo, which will include, *inter alia*, charges over its credit balances, book debts and its rights in connection with the Project.

Security Trust and Intercreditor Deed

The Obligors, the Security Trustee, the Bond Trustee, the Principal Paying Agent, the Account Bank and the Financial Guarantors have entered into a security trust and intercreditor deed (the "**Security Trust and Intercreditor Deed**") on or before the Issue Date which will set out the relationship of various Senior Creditors and Junior Creditors. The Security Trust and Intercreditor Deed will regulate, *inter alia*, the ranking of debt and security and the rights of parties in the case of default on certain obligations and will provide that, *inter alia*, the Junior Creditors will be subordinated to the Senior Creditors in the circumstances set out therein.

Each of the Senior Creditors will appoint the Security Trustee to act as trustee in connection with the security and the Security Trust and Intercreditor Deed. In such capacity, the Security Trustee will agree in the Security Trust and Intercreditor Deed that it will, subject to being prefunded and/or indemnified and/or secured to its satisfaction, exercise any right which it may have in respect of the Financing Rights (subject to the operation of certain entrenched rights and reserved matters, i.e. rights which cannot be exercised without the consent of the person having reserved to them such entrenched rights and reserved matters and the other express provisions of the Security Trust and Intercreditor Deed) as directed by the Controlling Creditor.

When exercising the Financing Rights in accordance with the instructions of the Controlling Creditor, the Security Trustee is not required to have regard to the interests of any Senior Creditor or other persons in relation to the exercise of such rights and has no liability to any Senior Creditor or other persons as a consequence of so exercising such rights.

The provisions of the Security Trust and Intercreditor Deed and the Security Documents will allow the Controlling Creditor (subject to the entrenched rights and reserved matters therein) to instruct the Security Trustee to enforce the security under the Security Documents in accordance with the terms thereof and the terms of the Security Trust and Intercreditor Deed (an "**Enforcement**").

Following an Enforcement, any proceeds of such Enforcement (including without limitation any proceeds received by the Security Trustee pursuant to a novation of the Funder's Direct Agreement) or other monies paid to or collected by the Security Trustee under the Security Trust and Intercreditor Deed or under any of the Security Documents or otherwise held by the Security Trustee on account of the Obligors as part of the Security shall be held by the Security Trustee on trust and (after taking into account any payments that have been made to the Principal Paying Agent either for its own account or that are due to be distributed by the Principal Paying Agent to Bondholders in accordance with the Paying Agency Agreement) applied in the following order:

(a) in payment, to the Security Trustee or any receiver of any unpaid remuneration payable under the Security Trust and Intercreditor Deed or the other Relevant Documents (including that agreed pursuant to clauses 11.16, 11.17, 11.18, 11.19 and 11.20 of the Security Trust and Intercreditor Deed) and all costs, charges, expenses, liabilities, indemnity payments, legal fees and disbursements, other fees and disbursements or other amounts expended or incurred by or other amounts due to the Security Trustee or any receiver or Appointee in connection with the trusts of the Security Trust and Intercreditor Deed or in enforcing the rights and remedies of the Security Trustee under any of the Relevant Documents;

(b) in payment to the Bond Trustee of all unpaid remuneration, and all costs, charges, expenses, liabilities, indemnity payments, legal fees and disbursements, accountants' and other Appointees fees and disbursements expended or incurred by or other amounts due to the Bond Trustee in connection with the trusts of the Security Trust and Intercreditor Deed and the Bond Trust Deed or in enforcing the rights and remedies of the Bond Trustee under the Relevant Documents;

(c) pro rata in payment to the Principal Paying Agent and any other Paying Agent and the Account Bank, of all unpaid remuneration, and all costs, charges, expenses, liabilities, indemnity payments, legal fees and disbursements, accountants' and other Appointees fees and disbursements expended or incurred by or other amounts due to the Principal Paying Agent and any other Paying Agent and the Account Bank in connection with the trusts of the Security Trust and Intercreditor Deed, the Paying Agency Agreement and the Accounts Agreement or in enforcing the rights and remedies of the Principal Paying Agent and the Account Bank and any other Paying Agent under the Relevant Documents;

(d) in payment to the Step-In Creditor until it has received any and all unpaid costs and expenses incurred by the Step-In Creditor;

(e) in payment to the Financial Guarantors (and *pro rata* between each Financial Guarantor) until they have received any and all costs, fees or expenses due and payable under the Reimbursement and Indemnity Deed (other than pursuant to clauses 3.2.4, 3.3.1 or 3.9 of the Reimbursement and Indemnity Deed);

(f) only if and for so long as the Financial Guarantors are not the Controlling Creditor, to the Senior Creditors until they have received any and all costs and expenses due and payable pursuant to clauses 18.1 and 18.3 of the Collateral Deed;

(g) in payment, *pro rata*, to the Financial Guarantors until they have received any and all amounts due and payable under clause 3.2.4 of the Reimbursement and Indemnity Deed and the Financial Guarantee Fee Letters (as such term is defined in the Reimbursement and Indemnity Deed);

(h) in payment, *pro rata* to the Bond Trustee on behalf of Bondholders of any and all scheduled interest due and payable on the Bonds; provided that, the amount payable pursuant to this paragraph (h) on any date shall be limited to the Scheduled Interest Liability as at that date. For this purpose, "**Scheduled Interest Liability**" means the amount in respect of interest on the Bonds which the Financial Guarantors have become actually and presently liable to pay on or prior to that date pursuant to the

Financial Guarantees or would be or become so liable subject only to a claim being made in accordance with the Financial Guarantees;

(i) in payment, *pro rata*, to the Financial Guarantors until they have received any and all amounts due and payable under clauses 3.3.1 and 3.9 of the Reimbursement and Indemnity Deed with respect to interest on the Bonds (including pursuant to any right of subrogation the Financial Guarantors have acquired in respect of any payments made by the Financial Guarantors under the Financial Guarantees with respect to interest on the Bonds);

(j) in payment, *pro rata*, to the Bond Trustee on behalf of Bondholders of any and all principal due and payable on the Bonds; provided that, the amount payable pursuant to this paragraph (j) on any date shall be limited to the Scheduled Principal Liability as at that date. For this purpose, "**Scheduled Principal Liability**" means the amount in respect of principal of the Bonds which the Financial Guarantors have become actually and presently liable to pay on or prior to that date pursuant to the Financial Guarantees or would be or become so liable subject only to a claim being made in accordance with the Financial Guarantees;

(k) in payment, *pro rata*, to the Financial Guarantors until they have received any and all amounts due and payable under clauses 3.3.1 and 3.9 of the Reimbursement and Indemnity Deed with respect to principal on the Bonds (including pursuant to any right of subrogation the Financial Guarantors have acquired in respect of any payments made by the Financial Guarantors with respect to principal on the Bonds);

(l) in payment to the Bond Trustee on behalf of Bondholders of any and all amounts due and payable pursuant to Condition 6 (*Redemption and Purchase*);

(m) if the Bonds have been accelerated in accordance with Condition 11 (*Events of Default*), in payment, *pro rata*, to the Bond Trustee on behalf of Bondholders of any and all outstanding principal due and payable on the Bonds;

(n) if the Controlling Creditor agrees to the University's request to pay the Service Provider Termination Sum in instalments ("Instalment Option") pursuant to paragraph 6 of schedule 5 (*Termination Provisions*) of the Project Agreement, in payment to the relevant obligor (or if the relevant obligor so directs to the Junior Creditors) of the Estimated Fair Value of the Agreement, but only for so long as Clause 13.2 of the Security Trust and Intercreditor Deed does not apply;

(o) if the Bonds have not been accelerated pursuant to Condition 11 (*Events of Default*), any and all amounts remaining after application of paragraphs (a) to (m) above shall be held in trust by the Security Trustee on behalf of the Senior Creditors and invested in Authorised Investments as instructed by the Controlling Creditor and, unless otherwise instructed by the Controlling Creditor, applied by the Security Trustee in payment of amounts becoming due and payable under paragraphs (a) to (m) as and when such amounts become so due and payable;

(p) following discharge in full of all Financial Guarantor Liabilities and payment in full of all outstanding principal due and payable on the Bonds, if any other Senior Liabilities remain outstanding, towards payment, *pro rata*, of all remaining sums or liabilities due or owed to the Senior Creditors in respect of such Senior Liabilities;

(q) following discharge in full of all Senior Liabilities, in payment to the Junior Creditors (other than HoldCo in its capacity as holder of the Issuer Shares and the ProjectCo Shares or any amounts already paid pursuant to clause 13.1(n)) until all Junior Liabilities are satisfied in full; and

(r) following discharge in full of all Liabilities, all remaining amounts in payment to the Issuer.

Definitions

"**Appointed Representative**" as the meaning given to such term in any relevant Direct Agreement.

"**Controlling Creditor**" means:

(a) until the Senior Creditors Release Date, the Financial Guarantors unless and until such time:

(i) as both of the Financial Guarantees have been terminated in accordance with Condition 2(b) (*Financial Guarantees*); or

(ii) as the Security Trustee has received notice from the Bond Trustee that a Financial Guarantor Default has occurred,

in which case it shall be the Bond Trustee, unless:

(x) a successor financial guarantor or a monitoring advisor has been appointed by the Bondholders under Condition 2(b) (*Financial Guarantees*), in which case it shall be such successor financial guarantor or monitoring advisor, as applicable; or

(y) such Financial Guarantor Default has been remedied or waived, in which case it shall be the Financial Guarantors; and

(b) without prejudice to clauses 11.15 and 24 of the Security Trust and Intercreditor Deed, after the Senior Creditors Release Date, the Stockholder.

"**Financial Guarantor Default**" means any of the following events:

(a) any Guaranteed Amount which is due for payment by AGM in accordance with the terms of the AGM Financial Guarantee is not paid by AGM on the date stipulated in the AGM Financial Guarantee;

(b) AGM disclaims, disaffirms, repudiates and/or challenges the validity of any of its obligations under the AGM Financial Guarantee or seeks to do so (in each case in writing);

(c) AGM (i) files a petition or commences a case or proceeding under any provision or chapter of the United States Bankruptcy Code or any other similar federal or state law relating to insolvency, bankruptcy, liquidation or reorganisation, or (ii) makes a general assignment for the benefit of its creditors, or (iii) has a final and non-appealable order for relief entered against it under the United States Bankruptcy Code or any other similar federal or state law relating to insolvency, bankruptcy, liquidation or reorganisation; or

(d) a court of competent jurisdiction, the New York Department of Insurance or other competent regulatory authority enters a final and non-appealable order, judgment or decree (i) appointing a custodian, trustee, agent or receiver for AGM or for all or any material portion of its property or (ii) authorising the taking of possession by a custodian, trustee, agent or receiver of AGM or of all or any material portion of its property.

"**Financial Guarantor Downgrade Event**" has the meaning given to it in Condition 2(b) (*Financial Guarantees*).

"**Financial Guarantor Liabilities**" means all present and future sums, liabilities and obligations whatsoever (actual or contingent) payable, owing, due or incurred by (a) any Obligor to either Financial Guarantor (by way of subrogation or otherwise) in respect of the Bonds, the Bond Trust Deed, the Financial Guarantees, the Financial Guarantee Fee Letters, the Accounts Agreement, the Collateral Deed or under the Reimbursement and Indemnity

Deed or (b) ProjectCo to the Issuer pursuant to the terms of the Bond Proceeds Facility in the Issuer On-Loan Agreement.

"**Financing Rights**" means, in respect of the Security Trustee or any other Senior Creditor, all rights which it has the benefit of pursuant to any Finance Document or any Project Document (other than any Reserved Matter or any right to amend the provisions of the Security Trust and Intercreditor Deed) including:

(a) the right, or the right to direct the Security Trustee, or another Senior Creditor, to consent to any amendment, waiver, modification and/or extension of any provision of any Finance Document;

(b) the right, or the right to direct the Security Trustee, or another Senior Creditor, to exercise any right, power and discretion of or under any of the provisions of the Finance Documents (including, without limitation, the right to refuse to advance sums upon non-satisfaction of, or to waive, any conditions precedent contained in any Finance Document);

(c) the right, or the right to direct the Security Trustee, or another Senior Creditor, to bring any litigation, arbitration, administrative or other proceedings arising from or in connection with the Finance Documents; and

(d) the exercise of any right expressed to be favour of the Controlling Creditor under the Collateral Deed.

"**Guaranteed Amounts**" has the meaning given to that term in the Financial Guarantees.

"**Guarantees**" means:

(a) the Building Contract Guarantee; and

(b) any other document designated as such by ProjectCo and the Controlling Creditor in writing.

"**HoldCo Upstream Shareholder Loan Agreements**" means:

(a) the upstream loan agreement between (1) HoldCo (as lender) and (2) Equitix Education (as borrower) dated on or about the Issue Date; and

(b) the upstream loan agreement between (1) HoldCo (as lender) and (2) Centro (as borrower) dated on or about the Issue Date.

"**Junior Creditors**" means:

(a) the Shareholders (in their capacities as holders of the HoldCo Shares);

(b) the Stockholders (in their capacities as holders of the ProjectCo Loan Notes);

(c) HoldCo (in its capacity as holder of the Issuer Shares and the ProjectCo Shares);

(d) the Issuer (in its capacity as lender of the Equity On-Loan under the Issuer On-Loan Agreement); and

(e) ProjectCo (in its capacity as lender of the Upstream Shareholder Loans),

and any other junior creditor who has become a party to the Security Trust and Intercreditor Deed under the terms of clause 17 (*Assignments and Transfers*) of the Security Trust and Intercreditor Deed.

"**Junior Liabilities**" means any indebtedness of any Obligor to:

(a) each and every Junior Creditor; and

(b) any other Obligor,

under the Junior Finance Documents.

"**Liabilities**" means the Senior Liabilities and the Junior Liabilities or any of them.

"**ProjectCo Upstream Shareholder Loan Agreements**" means:

(a) the upstream loan agreement in respect of the Equitix Education refinancing gain between (1) ProjectCo (as lender) and (2) HoldCo (as borrower) dated on or about the Issue Date; and

(b) the upstream loan agreement in respect of the Centro refinancing gain between (1) ProjectCo (as lender) and (2) HoldCo (as borrower) dated on or about the Issue Date.

"**Relevant Documents**" means the Project Documents and the Finance Documents and a Relevant Document means any one of these.

"**Scheduled Principal Liability**" means the amount in respect of principal of the Bonds which the Financial Guarantors have become actually and presently liable to pay on or prior to that date pursuant to the Financial Guarantees or would be or become so liable subject only to a claim being made in accordance with the Financial Guarantees.

"**Security**" means the security created or contemplated by the Security Documents or otherwise in respect of the Secured Obligations.

"**Senior Creditors**" means each of the Financial Guarantors, the Bond Trustee, the Bondholders, the Paying Agents, the Security Trustee, the Account Bank and their respective successors and permitted assigns and transferees from time to time.

"**Senior Liabilities**" means the Financial Guarantor Liabilities, the Bond Liabilities, the Security Trustee Liabilities and, the Account Bank Liabilities, the Paying Agent Liabilities (each as defined in the Security Trust and Intercreditor Deed).

"**Step-In Creditor**" means any Appointed Representative (in respect of the Funders' Direct Agreement) or Senior Creditors' Nominee (in respect of the Building Contractor Direct Agreement and the FM Service Contractor Direct Agreement) at such time.

"**Upstream Loan Agreements**" means the ProjectCo Upstream Shareholder Loan Agreements and the HoldCo Upstream Shareholder Loan Agreements.

"**Upstream Shareholder Loans**" means the loans made pursuant to the Upstream Loan Agreements.

ProjectCo Loan Notes

Pursuant to the ProjectCo Loan Note Instrument, ProjectCo issued and the Stockholders subscribed for loan notes.

Funders' Direct Agreement

The University, the Security Trustee and ProjectCo have entered into the Funders' Direct Agreement in connection with the Project pursuant to which the University, following a Default Event under the Project Agreement, agrees not to terminate the Project Agreement for a limited period. The Security Trustee is entitled during such limited period to propose, in accordance with instructions from the Controlling Creditor under the Security Trust and Intercreditor Deed, a representative to step in and undertake ProjectCo's obligations under the Project Agreement. Such representative will not be the Security Trustee.

The Bond Trustee will not, at any time whilst the Financial Guarantors are the Controlling Creditor, be able to control the exercise of step-in rights under the Funders' Direct Agreement. For the ranking of step-in expenses, see the section entitled "*The Security Arrangements — Security Trust and Intercreditor Deed*" above.

Guarantee

Pursuant to the terms of the Collateral Deed, each of the Issuer, HoldCo and ProjectCo, jointly and severally, irrevocably and unconditionally, guarantees to each Senior Creditor the performance of all the terms, conditions and covenants on the part of each of the Issuer, HoldCo and ProjectCo contained in the Senior Finance Documents, which includes the obligations of the Issuer in respect of the Bonds (the "**Obligor Guarantees**").

Accounts Agreement

The Issuer has entered into an accounts agreement with, amongst others, ProjectCo, HoldCo, the Security Trustee, the Bond Trustee, the Financial Guarantors, the Principal Paying Agent and The Bank of New York Mellon, London Branch, or any other bank or banks agreed between the parties which is or are party to such accounts agreement, as account bank (the "**Account Bank**") (the "**Accounts Agreement**") on or before the Issue Date, which will regulate payments into and out of each of the accounts intended, *inter alia*, to ensure the paying up of the relevant debt service accounts and the prevention of certain prohibited payments.

Sums standing to the credit of certain of the accounts may be invested (subject to certain restrictions as to maturity) in certain authorised investments approved in accordance with the provisions of the Accounts Agreement.

Upstream Loan Agreements

The relevant proportion of the refinancing gain, resulting from the refinancing funded by the bond issue proceeds on-lent to ProjectCo pursuant to the terms of the Issuer On-Loan Agreement, is made available to the Shareholders on the terms of the Upstream Loan Agreements. An amount representing the refinancing gain is on-lent to HoldCo pursuant to the ProjectCo Upstream Shareholder Loan Agreements, and subsequently on-lent from HoldCo to the Shareholders pursuant to the HoldCo Upstream Shareholder Loan Agreements. Amounts on-lent to Equitix will be drawn by Equitix on completion. Amount to be on-lent to Centro will be available for drawing following the bond issue and, until drawn, will be held in the Holdco Distribution Account.

Rights and responsibilities of the Security Trustee, the Bond Trustee and the Principal Paying Agent

1. The Security Trust and Intercreditor Deed, *inter alia*, provide as follows:

(a) The Security Trustee shall not be responsible for monitoring the obligations of any person to any Obligor or any other obligation of any party under the Relevant Documents and shall assume that all such persons are duly performing the same.

(b) In the absence of manifest error, the Security Trustee shall be entitled to assume that any instructions or certificates received by it from the Controlling Creditor under or pursuant to the Security Trust and Intercreditor Deed or any of the other Finance Documents are given, where appropriate, in accordance with directions of persons or the provisions of agreements by which the other Senior Creditors are bound and the Security Trustee shall not be liable to any other person for any action taken or omitted under or in connection with the Security Trust and Intercreditor Deed in accordance with any such instructions or certificates unless caused by its fraud, negligence or wilful misconduct. The Security Trustee shall be entitled to act upon any notice, request or other communication of any party to the Security Trust and Intercreditor Deed for the purposes of the Security Trust and Intercreditor Deed or any of the Finance Documents if such notice, request or other communication purports to be signed or sent by or on behalf of an authorised signatory of such party.

(c) The Security Trustee is under no obligation to investigate nor is it responsible or liable for any loss arising as a result of any failure to investigate the title in relation to, or the legality, validity, value, sufficiency, enforceability or effectiveness of, the Security purported to be created by any Security Document or the legality, validity or enforceability of any contracts over which the Security is created and the Security Trustee shall accept without investigation, requisition or objection and without any responsibility or liability for doing so such right and title as any Obligor may have to the property, assets or rights over which Security is created pursuant to the Security Documents. The Security Trustee will not be responsible for or liable for loss which results should any deficiency arise between the amount realised in respect of the property, assets and rights over which Security is given by the Security Documents and sums due in respect of the Senior Liabilities or the Junior Liabilities because the Security Trustee is liable to tax in respect of the property, assets and rights over which such security is created.

(d) Save as expressly otherwise provided in the Security Trust and Intercreditor Deed, the Security Trustee shall act pursuant to the provisions of the Security Trust and Intercreditor Deed or any other Finance Document only at the request or direction of the Controlling Creditor; save that the Security Trustee shall not be bound to act unless it is first indemnified and/or secured and/or prefunded to its satisfaction against all actions, proceedings, claims and demands to which it may render itself liable and all claims, losses, costs, demands, charges, damages, expenses, judgments (including legal fees and expenses) and liabilities which it may incur by so doing.

2. The Bond Trust Deed, *inter alia*, provides as follows:

(a) The Bond Trustee shall be under no obligation to monitor or supervise the functions of any other person or the operation of any account opened pursuant to the Relevant Documents or the performance or observance of any obligation under any Relevant Document or to consider the basis on which any approval or consent is granted by any party to the Relevant Documents, and shall be entitled, in the absence of notice in writing of a breach of obligation, to assume that each such person is properly performing its obligations. In particular, the Bond Trustee shall not be bound to take any steps to ascertain whether any Event of Default, Potential Event of Default, Trigger Event, Financial Guarantor Default or Financial Guarantor Downgrade Event has occurred and, until it has notice in writing to the contrary, the Bond Trustee shall be entitled to assume that no such event has occurred and that such person is properly performing its obligations. Where the Bond Trustee is not the Controlling Creditor, it may rely and act upon any notice from either Financial Guarantor that an Event of Default has occurred and any instructions from either Financial Guarantor to declare the Original Bonds immediately due and payable without any liability for any loss which might be suffered by the Issuer, the Bondholders, Receiptholders or Couponholders if the same is later shown to be incorrect.

(b) The Bond Trustee is under no obligation to investigate nor is it responsible or liable for any loss arising as a result of any failure to make or cause to be made on its behalf any of the searches, investigations or enquiries which would normally be made by a prudent chargee in relation to such security or the assets secured or to investigate the legality, validity, value, sufficiency or enforceability of the security created by the Security Documents or of the Financial Guarantees, or the validity or enforceability of any contracts over which such security is created or of the Financial Guarantees and the Bond Trustee shall accept without investigation, requisition or objection and without any responsibility or liability for doing so such right and title as the Issuer or any other person may have to the property, assets and rights over which security is created pursuant to the Security Documents. The Bond Trustee will not be responsible for or liable for loss which results should any deficiency arise between the amount realised in respect of the property, assets and rights over which security is given by the Security Documents and sums due in respect of the Original Bonds because the Bond Trustee is liable to tax in respect of the property, assets and rights over which such security is created.

(c) Where the Bond Trustee is not the Controlling Creditor (subject to certain provisions of the Bond Trust Deed and the Security Trust and Intercreditor Deed), the Bond Trustee (unless it shall expressly be required to take such action or exercise such right, power, authority or discretion by the Bond Trust Deed, the Security Trust and Intercreditor Deed, the Financial

Guarantees or the other Relevant Documents to which it is a party) shall refrain from taking any action or exercising any right, power, authority or discretion vested in it under the Bond Trust Deed, the Security Trust and Intercreditor Deed, the Financial Guarantees and the other Relevant Documents to which it is a party unless and until it shall have been instructed or directed to take such action or to exercise such right, power, authority or direction by the Controlling Creditor.

(d) Where the Bond Trustee is also then the Controlling Creditor (subject to certain provisions of the Bond Trust Deed and the Security Trust and Intercreditor Deed) the Bond Trustee (unless it shall expressly be required to take such action or exercise such right, power, authority or discretion by the Bond Trust Deed, the Security and Intercreditor Deed, the Financial Guarantees or the other Relevant Documents to which it is a party) may refrain from taking any such action or exercising any such right, power, authority or discretion unless and until it shall have been directed to take such action or to exercise such right, power, authority or discretion by the holders of at least 25 per cent. in aggregate amount outstanding of the Bonds by written direction on by Extraordinary Resolution. The Bond Trustee shall at all times be entitled to consult with the Bondholders in such manner and for such purposes as it may in its absolute discretion determine.

(e) The Bond Trustee shall not be obliged to take any action unless it is prefunded and/or indemnified and/or secured to its satisfaction in respect of any loss, cost or expense.

The Paying Agency Agreement provides, *inter alia*, that except as expressly provided otherwise in the Paying Agency Agreement, no Paying Agent has any responsibility to monitor compliance by any other party of its obligations under the Paying Agency Agreement, the Bonds or any other Finance Document.

TERMS AND CONDITIONS OF THE BONDS

The following is the text, subject to completion and minor amendment and save for the text in italics, (other than headings) of the terms and conditions which will be endorsed on each Bond in definitive form. Bonds in definitive form will only be issued in certain limited circumstances. For a summary of the provisions of the Bonds in global form, see the section Summary of Provisions relating to the Bonds while in Global Form.

The issue of the £98,200,000 0.100 per cent. index-linked guaranteed secured bonds due 31 August 2058 (the "**Bonds**", which expression includes any further bonds issued pursuant to Condition 20 (*Further Issues*) and forming a single series therewith) was authorised by a resolution of the Board of Directors of Uliving@Essex Issuerco PLC (the "**Issuer**") passed on 17 February 2017. The Bonds are subject to, and have the benefit of, a bond trust deed dated the Issue Date (as defined in Condition 4 (*Interest*) below) (as amended or supplemented from time to time, the "**Bond Trust Deed**") between the Issuer, Assured Guaranty (Europe) Ltd. ("**AGE**"), Assured Guaranty Municipal Corp. ("**AGM**") and, together with AGE, the "**Financial Guarantors**") and BNY Mellon Corporate Trustee Services Limited as Bond Trustee (the "**Bond Trustee**", which expression includes all persons for the time being acting as bond trustee or bond trustees appointed under the Bond Trust Deed). These terms and conditions include summaries of and are subject to the detailed provisions of the Bond Trust Deed which includes the form of the Bonds and the Receipts and Coupons (as defined below) relating to them and the security trust and intercreditor deed dated on or before the Issue Date (as amended, supplemented or replaced from time to time, the "**Security Trust and Intercreditor Deed**") between the Issuer, Uliving@Essex Limited ("**ProjectCo**"), Uliving@Essex HoldCo Limited ("**HoldCo**") and, together with the Issuer and ProjectCo, the "**Obligors**"), Equitix Education 2 Limited ("**Equitix Education**", Centro Place Investments Limited ("**Centro**"and together with Equitix Education, the "**Shareholders**" and each a "**Shareholder**"), BNY Mellon Corporate Trustee Services Limited as security trustee (the "**Security Trustee**", which expression includes all persons for the time being acting as security trustee or security trustees appointed under the Security Trust and Intercreditor Deed), BNY Mellon Corporate Trustee Services Limited as bond trustee (the "**Bond Trustee**" (for itself and on behalf of the Bondholders) and the Financial Guarantors.

The Bonds (excluding those held by or on behalf of any Obligor or any Affiliate of an Obligor or Shareholder of an Obligor) are unconditionally and irrevocably guaranteed as to scheduled payments of principal and interest (in each case adjusted for indexation, but excluding any amounts due in respect of the Bonds (i) attributable to any increase in interest margin, penalty or other sum payable by the Issuer for whatever reason; (ii) attributable to any present or future taxes, duties, withholding, deduction, assessment or other charge (including interest and penalties in respect of such taxes, duties, withholding, deduction, assessment or other charge) of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state (including the United Kingdom), or any political subdivision or governmental or taxing authority therein or thereof; (iii) attributable to any default interest; (iv) attributable to any amount relating to prepayment, early redemption, broken-funding indemnities, penalties, premium, "**spens**", any make-whole amount or similar types of payments payable in respect of the Bonds; or (v) in respect of which AGM or AGE has made an Accelerated Payment (as defined in the relevant Financial Guarantee) on or prior to a Scheduled Payment Date) in respect of the Bonds, pursuant to a financial guarantee to be dated the Issue Date issued by AGE (the "**AGE Financial Guarantee**") and a financial guarantee dated the Issue Date issued by AGM (the "**AGM Financial Guarantee**", and together with the AGE Financial Guarantee, the "**Financial Guarantees**").

Payments in respect of the Bonds will be made pursuant to a paying agency agreement dated the Issue Date (as amended or supplemented from time to time, the "**Paying Agency Agreement**") between the Issuer, the Bond Trustee, The Bank of New York Mellon acting through its London Branch as principal paying agent (the "**Principal Paying Agent**", which expression includes any successor principal paying agent appointed under the Paying Agency Agreement and together with any additional or successor paying agents appointed under the Paying Agency Agreement, the "**Paying Agents**") and which expression shall also include The Bank of New York Mellon, London Branch acting in its capacity as calculation agent in connection with Conditions 7 (*Indexation*) and 8 (*Changes in circumstances affecting the Index*) the "**Calculation Agent**").

The holders of the Bonds (the "**Bondholders**") and the holders of the related principal receipts (the "**Receiptholders**" and the "**Receipts**" , respectively) and interest coupons (the "**Couponholders**" and

the "**Coupons**", respectively) will be entitled to the benefit of, will be bound by and are deemed to have notice of, all the provisions of the Bond Trust Deed, the Financial Guarantees, the Collateral Deed (as defined in Condition 2(f) (*Collateral Deed*)), the Security Documents (as defined in Condition 2(e) (*Security*)) and the Paying Agency Agreement applicable to them and the master definitions schedule dated on or about the date hereof and for the purpose of identification signed by or on behalf of the parties to the transaction (the "**Master Definitions Schedule**") and each Finance Document to which the Bond Trustee or the Security Trustee are a party.

Copies of the Bond Trust Deed, the Financial Guarantees, the Collateral Deed, the Security Documents, the Paying Agency Agreement and the Master Definitions Schedule are available for inspection by Bondholders during normal business hours at the registered office for the time being of the Bond Trustee presently at One Canada Square, London E14 5AL and at the specified offices of each of the Paying Agents.

Capitalised terms used in these conditions have the meanings given to them in the Master Definitions Schedule unless otherwise defined.

1. **Form, Denomination and Title**

(a) *Form and Denomination*

The Bonds are in bearer form, serially numbered, in denominations of £100,000 and integral multiples of £1,000 in excess thereof with Receipts for principal, Coupons for interest and talons (each a "**Talon**") for further Receipts or Coupons attached at the time of issue. Bonds of one denomination will not be exchangeable for Bonds of any other denomination.

(b) *Title*

Title to the Bonds, the Receipts, the Coupons and the Talons will pass by delivery. The holder of any Bond, Receipt, Coupon or Talon shall (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any other interest therein, any writing thereon or any notice of any previous loss or theft thereof) and no person shall be liable for so treating such holder.

2. **Status, Financial Guarantees and Security**

(a) *Status of the Bonds*

The Bonds constitute direct, secured obligations of the Issuer which rank *pari passu* and rateably without any preference or priority among themselves and will rank in priority to all unsecured obligations of the Issuer, save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.

(b) *Financial Guarantees*

A "**Financial Guarantor Downgrade Event**" means if at any time while the Bonds remain outstanding, both: (i) AGM's insurer financial strength rating by Moody's ceases to be at least "Baa3" and (ii) AGM's insurer financial strength rating by Standard & Poor's Global Ratings Services ("**S&PGRS**") ceases to be at least "BBB-"; provided, that during such time as AGM's insurer financial strength is not rated by either Moody's or S&PGRS, then a "Financial Guarantor Downgrade Event" means at any time while the Bonds remain outstanding, that AGM's insurer financial strength rating is not rated at least "BBB-" or the equivalent by at least one other credit rating agency which is registered with the United States Securities and Exchange Commission as a nationally recognized statistical rating organization (such rating agency during such time, an "**Alternative Rating Agency**").

If a Financial Guarantor Downgrade Event has occurred and is continuing, then the Issuer shall notify the Bondholders and the Bond Trustee that a Financial Guarantor Downgrade Event has occurred and of their rights pursuant to and in accordance with the Bond Trust Deed and the Conditions. If directed by Bondholders acting by way of an Extraordinary Resolution, the Bond Trustee shall, subject to being prefunded and/or indemnified and/or secured to its satisfaction by the Bondholders, issue a notice (the "**Financial Guarantor Removal Notice**")

to the Financial Guarantors specifying that, unless the Financial Guarantor Downgrade Event has been remedied or waived by the date that is three calendar months after the date of delivery of the Financial Guarantor Removal Notice (the "**Financial Guarantor Removal Date**"), each of the Financial Guarantees shall be unconditionally and irrevocably terminated and cancelled in whole (and not in part) effective on and from the Financial Guarantor Removal Date, and no further claim may be made on the Financial Guarantees on and from the Financial Guarantor Removal Date and any such further claim shall be null and void and of no force or effect.

Where a Financial Guarantor Downgrade Event has occurred, the Financial Guarantors may remedy such Financial Guarantor Downgrade Event and the related Financial Guarantor Removal Notice by transferring the AGM Financial Guarantee to an affiliate of AGM that is rated at least "Baa3" by Moody's or "BBB-" by S&PGRS at any time prior to the Financial Guarantor Removal Date in which case the Financial Guarantor Downgrade Event shall be deemed to have been remedied.

The Issuer will immediately notify the Bondholders upon (i) any remedy or waiver of a Financial Guarantor Downgrade Event (including by way of transfer of the AGM Financial Guarantee) or (ii) termination of the Financial Guarantees pursuant to this Condition 2(b) (*Financial Guarantees*).

If a continuing Financial Guarantor Downgrade Event has not been remedied or waived prior to the Financial Guarantor Removal Date, on the Financial Guarantor Removal Date:

- the Issuer shall pay to the Financial Guarantors an amount equal to (i) all amounts paid by such Financial Guarantors under the Financial Guarantees, (ii) all other amounts due and payable in accordance with the Reimbursement and Indemnity Deed including without limitation, indemnifications, gross up, taxes, reimbursements, interest, charges, fees, costs and expenses, (iii) any and all financial guarantee fees due and payable in accordance with the Financial Guarantee Fee Letters and (iv) any other amounts of any nature whatsoever due and payable to the Financial Guarantors pursuant to the Senior Finance Documents (such amounts collectively the "**Financial Guarantor Removal Payments**", as set forth in a notice in writing delivered to the Issuer and the Bond Trustee by the Financial Guarantors)

- the Financial Guarantees shall be unconditionally and irrevocably terminated and cancelled in whole (and not in part) and shall cease to have any further force or effect and the term of the Financial Guarantees shall be deemed to have expired

- all Senior Finance Documents (including without limitation the Reimbursement and Indemnity Deed and the Financial Guarantee Fee Letters) other than the Financial Guarantees shall continue in full force and effect

- the financial guarantee fees shall cease to be paid to the Financial Guarantors, and Bondholders may by Extraordinary Resolution sanction to use the amounts no longer required to be paid as such financial guarantee fees in accordance with this Condition 2(b) (*Financial Guarantees*)

If and to the extent that the Financial Guarantor Removal Payments have not been finally and irrevocably paid in full on the Financial Guarantor Removal Date by the Issuer, the Financial Guarantors shall be entitled to charge and receive from the Issuer interest on all Financial Guarantor Removal Payments (on and from the Financial Guarantor Removal Date until the date on which the Financial Guarantors (acting reasonably) have notified the Issuer and the Bond Trustee in writing that the Financial Guarantor Removal Payments have been finally and irrevocably paid in full (the "Financial Guarantor Removal Effective Date")) at the rate and in the amount specified in the Reimbursement and Indemnity Deed with respect to interest charged and payable on unpaid amounts. The Financial Guarantors' rights to be paid the Financial Guarantor Removal Payments shall survive the termination of the Financial Guarantees and continue in full force and effect until the Financial Guarantor Removal Effective Date shall have occurred.

For the purposes of paragraph (a)(i) of the definition of Controlling Creditor, no termination shall occur until the Financial Guarantor Removal Effective Date (and not on the occurrence of the Financial Guarantor Removal Date).

If both (i) the rating of the Bonds and AGM's insurer financial strength rating by S&P is less than "BBB-" or is withdrawn and (ii) each of AGM's insurer financial strength rating and the rating of the Bonds from an Alternative Rating Agency is less than "BBB-" (or such equivalent rating) or is withdrawn, and AGM has an insurer financial strength rating of at least "Baa3" by Moody's on the date that such downgrades or withdrawals occur, then the Financial Guarantors shall request the Issuer obtains and the Issuer shall use reasonable endeavours to obtain within 2 months of such date (A) a rating for the Bonds from Moody's, at the cost of AGE and (B) that the rating of the Bonds by S&P is withdrawn.

If the Financial Guarantor Removal Date has occurred, financial guarantee fees shall cease to be paid to the Financial Guarantors and the Bondholders may sanction by Extraordinary Resolution to use the amounts no longer required to be paid as such financial guarantee fees:

(i) to pay a replacement financial guarantor (if available) to act as Controlling Creditor;

(ii) to pay a monitoring adviser (if available) to act as Controlling Creditor;

(iii) to increase the amount of interest payable on the Bonds by the amount of such financial guarantee fees; or

(iv) for such other purpose as the Bondholders may determine.

The Issuer will immediately notify the Bondholders (i) upon any remedy or waiver of a Financial Guarantor Downgrade Event (including by way of transfer of the AGM Financial Guarantee) or (ii) termination of the Financial Guarantees pursuant to this Condition 2(b), in accordance with Condition 17 (*Notices*) of the occurrence of such event.

(c) *Status of Financial Guarantees*

The AGE Financial Guarantee provided by AGE constitutes a direct, unsecured obligation of AGE which will rank at least *pari passu* with all other unsecured obligations of AGE, save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.

The AGM Financial Guarantee provided by AGM constitutes a direct, unsecured obligation of AGM which will rank at least *pari passu* with all other unsecured obligations of AGM, save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.

(d) *Subrogation of the Financial Guarantors*

The Bond Trust Deed and the Financial Guarantees each provide that the Financial Guarantors shall be subrogated to the rights of the Bond Trustee and each Bondholder, Receiptholder and Couponholder in respect of amounts due under the Bonds which have been paid under the AGE Financial Guarantee and the AGM Financial Guarantee.

(e) *Security*

The obligations of the Issuer under the Bonds have the benefit of the security constituted by:

(i) a fixed and floating charge English law debenture dated on or before the Issue Date granted by the Issuer in favour of the Security Trustee (the "**Issuer Debenture**");

(ii) a fixed and floating charge English law debenture dated on or before the Issue Date granted by ProjectCo in favour of the Security Trustee (the "**ProjectCo Debenture**");

(iii) a fixed and floating charge debenture dated on or before the Issue Date granted by HoldCo in favour of the Security Trustee (the "**HoldCo Debenture**")

(together, with the Security Trust and Intercreditor Deed, any other document from time to time executed in favour of the Security Trustee for the purpose of securing all or any of the Secured Obligations and any deed of accession entered into in respect of any of the above, the "**Security Documents**").

(f) *Collateral Deed*

The Bond Trustee on behalf of the Bondholders has the benefit of certain representations and covenants set out in a collateral deed (the "**Collateral Deed**"), dated on or about the Issue Date between, *inter alios*, the Obligors, the Financial Guarantors and the Bond Trustee. The Collateral Deed also contains a guarantee of the Issuer's obligations under the Bonds from the other Obligors.

(g) *Security Trust and Intercreditor Deed*

The Bonds are subject to the Security Trust and Intercreditor Deed pursuant to which the exercise by the Bond Trustee of rights under the Bond Trust Deed and under the Bonds may in certain circumstances be directed by, and is in most circumstances subject to the prior consent of, other parties to the Security Trust and Intercreditor Deed.

The Controlling Creditor has the exclusive right, power and authority to direct, or to refrain from directing, the Senior Creditors in the exercise of the Financing Rights subject to Reserved Matters or Entrenched Rights (as defined in the Security Trust and Intercreditor Deed), in each case without regard to the interests of any other person and the Controlling Creditor will not owe fiduciary duties to any person.

When exercising the Financing Rights in accordance with the instructions of the Controlling Creditor, neither the Bond Trustee nor the Security Trustee is required to have regard to the interests of the Bondholders in relation to the exercise of such rights and has no liability to the Bondholders as a consequence of so acting.

"**Creditors**" means the Issuer, in its capacity as lender under the Issuer On-Loan Agreement, each of the Senior Creditors and each of the Junior Creditors and "**Creditor**" means any of them.

"**Controlling Creditor**" means:

(a) until the Senior Creditors Release Date, the Financial Guarantors unless and until such time:

(i) as both of the Financial Guarantees have been terminated in accordance with Condition 2(b) (*Financial Guarantees*); or

(ii) as the Security Trustee has received notice from the Bond Trustee that a Financial Guarantor Default has occurred,

in which case it shall be the Bond Trustee, unless:

(x) a successor financial guarantor or a monitoring advisor has been appointed by the Bondholders under Condition 2(b) (*Financial Guarantees*), in which case it shall be such successor financial guarantor or monitoring advisor, as applicable; or

(y) such Financial Guarantor Default has been cured or waived, in which case it shall be the Financial Guarantors; and

(b) without prejudice to clauses 11.15 and 24 of the Security Trust and Intercreditor Deed, after the Senior Creditors Release Date, the Stockholder.

"**Equity On-Loan** " means the equity on-loan made available to ProjectCo under the Issuer On-Loan Agreement pursuant to which the Issuer lends the proceeds of subscription of its shares by HoldCo.

"**Financial Guarantor Default**" means any of the following events:

(a) any Guaranteed Amount (as defined in the Financial Guarantees) which is due for payment by AGM in accordance with the terms of the AGM Financial Guarantee is not paid by AGM on the date stipulated in the AGM Financial Guarantee;

(b) AGM disclaims, disaffirms, repudiates and/or challenges the validity of any of its obligations under the AGM Financial Guarantee or seeks to do so (in each case in writing);

(c) AGM (i) files a petition or commences a case or proceeding under any provision or chapter of the United States Bankruptcy Code or any other similar federal or state law relating to insolvency, bankruptcy, liquidation or reorganisation, or (ii) makes a general assignment for the benefit of its creditors, or (iii) has a final and non-appealable order for relief entered against it under the United States Bankruptcy Code or any other similar federal or state law relating to insolvency, bankruptcy, liquidation or reorganisation; or

(d) a court of competent jurisdiction, the New York Department of Insurance or other competent regulatory authority enters a final and non-appealable order, judgment or decree (i) appointing a custodian, trustee, agent or receiver for AGM or for all or any material portion of its property or (ii) authorising the taking of possession by a custodian, trustee, agent or receiver of AGM or of all or any material portion of its property.

"**Financing Rights**" means, in respect of the Security Trustee or any other Senior Creditor, all rights which it has the benefit of pursuant to any Finance Document or any Project Document (other than any Reserved Matter (as defined in the Security Trust and Intercreditor Deed) or any right to amend the provisions of the Security Trust and Intercreditor Deed) including:

(a) the right, or the right to direct the Security Trustee or another Senior Creditor, to consent to any amendment, waiver, modification and/or extension of any provision of any Finance Document;

(b) the right, or the right to direct the Security Trustee or another Senior Creditor, to exercise any right, power and discretion of or under any of the provisions of the Finance Documents (including, without limitation, the right to refuse to advance sums upon non-satisfaction of, or to waive, any conditions precedent contained in any Finance Document);

(c) the right, or the right to direct the Security Trustee or another Senior Creditor, to bring any litigation, arbitration, administrative or other proceedings arising from or in connection with the Finance Documents; and

(d) the exercise of any right expressed to be in favour of the Controlling Creditor under the Collateral Deed.

"**Junior Creditors**" means:

(a) the Shareholders (in their capacities as holders of the HoldCo Shares);

(b) the Stockholders (in their capacities as holders of the ProjectCo Loan Notes);

(c) HoldCo (in its capacity as holder of the Issuer Shares and the ProjectCo Shares);

(d) the Issuer (in its capacity as lender of the Equity On-Loan under the Issuer On-Loan Agreement); and

(e) ProjectCo (in its capacity as lender of the Upstream Shareholder Loans),

and any other junior creditor who has become a party to the Security Trust and Intercreditor Deed under the terms of clause 17 (*Assignments and Transfers*) of the Security Trust and Intercreditor Deed.

"**Senior Creditors**" means each of the Financial Guarantors, the Bond Trustee, the Bondholders, the Paying Agents, the Account Bank and the Security Trustee and Senior Creditor means each such person.

"**Senior Creditors Release Date**" means the later of (a) the date upon which all the Senior Liabilities have been fully and irrevocably paid or discharged to the satisfaction of the Controlling Creditor and (b) the date on which the Reimbursement and Indemnity Deed ceases to be in effect in accordance with clause 4.1 (*Term of Deed*) thereof, in each case as evidenced by a confirmation given pursuant to clause 4.8 (*Senior Creditors Release Date*) of the Security Trust and Intercreditor Deed.

3. **Covenants of the Issuer**

The Issuer shall perform all its obligations and exercise all its rights under and in accordance with the Finance Documents and the documents relating to the Project to which it is party. In particular, the Issuer has undertaken to:

(a) provide a report to Bondholders either through an electronic website or through the Principal Paying Agent via the bond clearing system following Financial Close (x) if and for so long as the Bond Trustee is not the Controlling Creditor, annually on or before the date which is 20 business days prior to the Scheduled Payment occurring on 28 February (or 29 February in each leap year) in each year and (y) if and for so long as the Bond Trustee is the Controlling Creditor semi-annually on or before the date which is 20 business days prior to each Scheduled Payment Date, giving details of the progress of the Project in the form scheduled to the Collateral Deed;

(b) use its reasonable endeavours to maintain a rating of the Bonds by S&P;

(c) procure and thereafter maintain the maintenance of the listing of the Bonds on the Irish Stock Exchange or, if it is unable to do so having used all reasonable endeavours or if it is unduly burdensome to maintain such listing, it shall obtain and maintain the listing of the Bonds on such other stock exchange, which shall be in any case a recognised stock exchange for the purposes of Section 1005 of the Income Tax Act 2007, as it may decide, with the prior written approval of the Controlling Creditor; and

(d) procure that there will at all times be furnished to any stock exchange on which the Bonds are for the time being listed such information as such stock exchange may require to be furnished in accordance with its normal requirements or in accordance with any arrangements for the time being made with any such stock exchange.

4. **Interest**

The Bonds bear interest on their Outstanding Principal Amount (as defined in Condition 7(a) (*Definitions*)) ("**Scheduled Interest**") from 24 February 2017 (the "**Issue Date**") at the rate of 0.100 per cent. per annum (the "**Rate of Interest**"). Scheduled Interest will be payable semi-annually in arrear on each scheduled payment date listed in Condition 9(a) (*Scheduled Payments*) (each, a "**Scheduled Payment Date**"), subject as provided in Condition 9 (*Payments and Exchange of Talons*). Each period beginning on (and including) the Issue Date or any Scheduled Payment Date and ending on (but excluding) the next Scheduled Payment Date is herein called an "**Interest Period**". The first Scheduled Payment Date will be on 28 February 2017 in respect of the Interest Period from, and including the Issue Date to, but excluding, 28 February 2017. The amount of interest payable in respect of each Bond for any Interest Period shall be calculated by the Principal Paying Agent by applying the Rate of Interest to the Outstanding Principal Amount of such Bond, dividing the product by two and adjusting for indexation in accordance with Condition 7 (*Indexation*) except that the amount of interest payable in respect of each Bond for the Interest Period ending on 28 February 2017 will amount to £1.00 in respect of each Bond of £100,000 denomination (including indexation) and £0.01 in respect of

each £1,000 in aggregate principal amount of the Bonds in excess of £100,000 (including indexation).

If interest is required to be calculated in respect of a Bond for a period which is not an Interest Period, it shall be calculated by applying the Rate of Interest to the Outstanding Principal Amount of such Bond, multiplying the product by the relevant Day Count Fraction and adjusting for indexation in accordance with Condition 7 (*Indexation*), where:

"**Day Count Fraction**" means:

(a) if the Calculation Period is equal to or shorter than the Regular Period (as defined below) during which it falls, the number of days in the Calculation Period divided by the product of (1) the number of days in such Regular Period and (2) two; and

(b) if the Calculation Period is longer than one Regular Period, the sum of:

(i) the number of days in such Calculation Period falling in the Regular Period in which it begins divided by the product of (1) the number of days in such Regular Period and (2) two; and

(ii) the number of days in such Calculation Period falling in the next Regular Period divided by the product of (1) the number of days in such Regular Period and (2) two;

"**Calculation Period**" means the relevant period for which interest is to be calculated from (and including) the first day in such period to (but excluding) the last day in such period; and

"**Regular Period**" means each period from (and excluding) 28 February (or 29 February in each leap year) or 31 August in any year to (but including) the next 28 February (or 29 February in each leap year) or 31 August.

5. **Default Interest**

(a) *Default Interest*

The Outstanding Principal Amount of each Bond will cease to bear interest (adjusted for indexation in accordance with Condition 7 (*Indexation*)) from the Scheduled Payment Date for the payment of such principal amount (or part thereof) unless, upon due presentation, payment is improperly withheld or refused, in which case the unpaid amount will bear default interest ("**Default Interest**") at the Rate of Interest (adjusted for indexation) (after as well as before judgment) until whichever is the earlier of:

(i) the day on which all principal sums due in respect of such Bond up to that day are received by or on behalf of the relevant Bondholder; and

(ii) the day which is seven days after the Principal Paying Agent or the Bond Trustee has notified the Bondholders that it has received all principal sums due in respect of the Bonds up to such seventh day (except to the extent that there is any subsequent default in payment in which case interest shall continue to accrue on any principal amount until such principal amounts are received by or on behalf of the relevant Bondholders).

(b) *Default Interest Payment*

Accrued Default Interest shall be payable prior to the final Scheduled Payment Date on each date (each a "**Default Interest Payment Date**") on which any amount of Scheduled Principal (as defined in Condition 6(a) (*Scheduled Redemption*)) remains unpaid and which is an integral multiple of six months after the due date for payment of such Scheduled Principal or upon any earlier date upon which Scheduled Principal becomes due in accordance with the conditions. Any amounts of Default Interest arising after the final Scheduled Payment Date shall be immediately due and payable. Each period beginning on (and including) the date on which the relevant payment is improperly withheld or refused or any Default Interest Payment Date and ending on (but excluding) the next Default Interest Payment Date is herein called a

"**Default Interest Period**". References herein to 'interest' shall include for the avoidance of doubt, Default Interest.

(c) *Default Interest Calculation*

The amount of Default Interest payable in respect of each Bond for any Default Interest Period shall be calculated by the Principal Paying Agent on the basis of the Day Count Fraction.

Default Interest does not accrue on Scheduled Interest or Default Interest. The payment of Default Interest is not guaranteed by the Financial Guarantors under the Financial Guarantees.

6. **Redemption and Purchase**

Early redemption of the Bonds for whatever reason does not accelerate AGE and/or AGM's payment obligation under the Financial Guarantees. AGE and/or AGM shall only be liable to make payments in respect of the Bonds (pursuant to the Financial Guarantees) in the amounts and on the dates on which such payments would have been required to be made if such amounts had not become immediately due and payable.

(a) *Scheduled Redemption*

Unless previously redeemed, or purchased and cancelled the Issuer will redeem the Bonds in instalments by the payment on each Scheduled Payment Date of the scheduled principal (which, in respect of each £1,000 of Bonds will be the relevant amount set out in Condition 9(a) (*Scheduled Payments*) under "Scheduled Principal per £1,000 (before indexation)" (the "**Scheduled Principal**")). Payments of Scheduled Principal will be adjusted for indexation in accordance with Condition 7 (*Indexation*). The first instalment will be payable on the Scheduled Payment Date falling in 28 February 2017. The final Scheduled Payment Date is the Scheduled Payment Date falling in 31 August 2058. For the avoidance of doubt, the Outstanding Principal Amount of each Bond will be reduced for each payment of principal on the Scheduled Payment Dates as provided in Condition 9 (*Payments and Exchange of Talons*) and such payment will not result in a reduction of the number of Bonds in issue.

(b) *Redemption at the option of the Issuer*

The Issuer may at any time, with the approval of the Financial Guarantors if they are the Controlling Creditor, having given not less than 30 nor more than 60 days' notice of redemption to the Bondholders in accordance with Condition 17 (*Notices*) (which notice shall be irrevocable and shall oblige the Issuer to redeem the Bonds), redeem each of the Bonds in whole, but not in part, at an amount (the "**Early Redemption Amount**") equal to the higher of:

(i) the Indexed Par Amount; and

(ii) an amount calculated by discounting the remaining principal and interest payments (ignoring future changes in the RPI(0,6) Index Ratio) in respect of that Outstanding Principal Amount at a rate equal to the Relevant Benchmark Yield plus 0.20 per cent.,

together with any payment of interest due but unpaid up to and including the date of redemption, all adjusted for indexation in accordance with Condition 7 (*Indexation*).

On the date specified for redemption in the notice given by the Issuer, the Issuer shall redeem each of the Bonds at the Early Redemption Amount.

(c) *Redemption for Index Reasons*

If either (a) the Index Figure (as defined in Condition 7(a) (*Indexation*)) for three consecutive Interest Periods falls to be determined on the basis of an Index Figure previously published as provided in Condition 8(b)(ii) and the Bond Trustee has been notified by Calculation Agent that publication of the Index (as defined in Condition 7(a) (*Indexation*)) has ceased, or (b)

written notice of any fundamental change made to the coverage or the basic calculation of the Index has been sent by the Principal Paying Agent to the Bond Trustee who (acting solely on the advice of the Indexation Adviser) considers such change to be materially prejudicial to the interests of the Bondholders, and (in either case) no amendment to or substitution of the Index shall have been notified to the Issuer and become effective pursuant to Condition 8(c)(iv) and such circumstances are continuing, the Issuer shall, having given not more than 60 nor less than 30 days' notice to Bondholders in accordance with Condition 17 (*Notices*), subject to the consent of the Financial Guarantors so long as they are the Controlling Creditor, redeem all, but not some only, of the Bonds at the Indexed Par Amount together with accrued interest up to and including the date of redemption (adjusted for indexation as provided in these Conditions), the RPI(0,6) Index Ratio (as defined in Condition 7(a) (*Definitions*)) for this purpose being that applicable to the month in which redemption takes place.

(d) *Mandatory Early Redemption – University Termination Event and Compulsory Change Termination Event*

Upon a University Termination Event or a Compulsory Change Termination Event, the amount paid by the University (the "**Compensation on Termination**") into an account designated by ProjectCo which is secured in favour of the Security Trustee under the ProjectCo Debenture shall, if the Compensation on Termination is sufficient to pay the Early Redemption Amount for the Bonds (together with accrued interest, adjusted for indexation in accordance with Condition 7 (*Indexation*)) and the Bond Trustee has received a Sufficiency Certificate (as defined in the Security Trust and Intercreditor Deed), subject to the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed, be used to redeem each Bond at the Early Redemption Amount (together with accrued interest, adjusted for indexation in accordance with Condition 7 (*Indexation*)) on the date falling ten days after deposit of the Compensation on Termination by the University into such account.

If the Compensation on Termination is not sufficient to redeem each Bond at its Early Redemption Amount but is greater than or equal to the Indexed Par Amount together with any amounts ranking in priority thereto (in accordance with the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed) and any accrued interest thereon (as adjusted for indexation in accordance with Condition 7 (*Indexation*)), then each Bond will, subject to the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed, be redeemed at its Indexed Par Amount plus its *pro rata* share of the difference between the Compensation on Termination and the Indexed Par Amount (the "**Above Par Redemption Amount**") on the date that is ten days after (x) if no AP Non-Redemption Instruction is in effect, the date of deposit of the Compensation on Termination by the University into such account or (y) if an AP Non-Redemption Instruction is in effect, the date (if any) on which such AP Non-Redemption Instruction is no longer in effect.

If the Compensation on Termination is not sufficient to redeem each Bond at its Early Redemption Amount and is less than the Indexed Par Amount together with any amounts ranking in priority thereto (in accordance with the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed) and any accrued interest thereon (as adjusted for indexation), then each Bond will, subject to the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed, be redeemed at its Below Par Redemption Amount on the date that is ten days after (x) if no BP Non-Redemption Instruction is in effect, the date of deposit of the Compensation on Termination by the University into such account or (y) if a BP Non-Redemption Instruction is in effect, the date (if any) on which such BP Non Redemption Instruction is no longer in effect (the "**BP Redemption Date**").

(e) *Mandatory Early Redemption – ProjectCo Termination Event*

Upon a ProjectCo Termination Event where the Controlling Creditor has either not allowed the University to pay by instalments or had allowed the University to pay by instalments but the University's entitled to so pay has ceased, the Compensation on Termination paid into an account designated by ProjectCo which is secured in favour of the Security Trustee under the ProjectCo Debenture shall, if the Compensation on Termination is sufficient to pay the Indexed Par Amount in respect of the Bonds (together with accrued interest, adjusted for indexation in accordance with Condition 7 (*Indexation*)) and the Bond Trustee has received a

Sufficiency Certificate (as defined in the Security Trust and Intercreditor Deed), subject to the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed, be used by the Issuer to redeem each of the Bonds in whole, but not in part, at the Indexed Par Amount, together with accrued interest (adjusted for indexation in accordance with Condition 7 (*Indexation*)) on the date falling ten days after deposit of the Compensation on Termination by the University into such account.

If the Compensation on Termination is less than the Indexed Par Amount together with any amounts ranking in priority thereto (in accordance with the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed) and any accrued interest thereon (as adjusted for indexation), then each Bond will, subject to the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed, be redeemed at its Below Par Redemption Amount on the date (the "**BP Redemption Date**") that is ten days after (x) if no BP Non-Redemption Instruction is in effect, the date of deposit of the Compensation on Termination by the University into such account or (y) if a BP Non-Redemption Instruction is in effect, the date (if any) on which such BP Non Redemption Instruction is no longer in effect.

(f) *Mandatory Early Redemption – ProjectCo Termination Event (and the Controlling Creditor allows the University to exercise its instalment option)*

Upon a ProjectCo Termination Event where the Controlling Creditor allows the University to pay the Compensation on Termination in instalments (each a "**Compensation on Termination Instalment**"), the Bonds will be redeemed according to a schedule agreed between the Issuer, the Controlling Creditor and, where the Controlling Creditor is not the Bond Trustee, the Bond Trustee (the "**Revised Redemption Schedule**") which shall replace and supersede the schedule of payments set forth in column B of Condition 9(a) (*Scheduled Payments*). Each Compensation on Termination Instalment that is paid into an account designated by ProjectCo which is secured in favour of the Security Trustee under the ProjectCo Debenture shall, subject to the priority of payments set out in clause 13 of the Security Trust and Intercreditor Deed, be applied to redeem each Bond in accordance with the Revised Redemption Schedule.

(g) *Definitions*

For the purposes of this Condition 6:

"**AP Non-Redemption Instruction**" means that the holders of at least 25 per cent. of the Outstanding Principal Amount have, by written notice to the Bond Trustee or the holders have by Extraordinary Resolution, instructed the Bond Trustee that each Bond shall not be redeemed at its Above Par Redemption Amount, subject to the Bond Trustee being indemnified and/or secured and/or prefunded to its satisfaction, provided that no such instruction may be given if the Bonds have already been accelerated and provided further that any such instruction shall be deemed to be immediately revoked if the Bonds are subsequently accelerated.

"**BP Non-Redemption Instruction**" means that the holders of at least 25 per cent. of the Outstanding Principal Amount have, by written notice to the Bond Trustee or the holders have by Extraordinary Resolution, instructed the Bond Trustee that each Bond shall not be redeemed at its Below Par Redemption Amount, subject to the Bond Trustee being indemnified and/or secured and/or prefunded to its satisfaction, provided that no such instruction may be given if the Bonds have already been accelerated and provided further that any such instruction shall be deemed to be immediately revoked if the Bonds are subsequently accelerated.

"**Below Par Redemption Amount**" means, in respect of each Bond, its *pro rata* share of the Compensation on Termination which *pro rata* share will be applied on the BP Redemption Date to reduce the Outstanding Principal Amount of each Bond *pro rata* and the payments of Scheduled Principal due on the Bonds set forth in column B of Condition 9(a) (*Scheduled Payments*) shall be adjusted to reflect such reduction by applying such reduction to the payments of Scheduled Principal due on the Bonds sequentially, commencing with the

Scheduled Payment Date occurring immediately after the BP Redemption Date, until the Below Par Redemption Amount is applied in full.

"**Compulsory Change Termination Event**" means, following a Compulsory Change Event (as defined in the Project Agreement), the termination of the Project Agreement under clause 11.10, clause 22.1.6, to the Project Agreement and/or on termination of the Project Agreement following termination of the Agreement for Lease under clauses 5.5, 5.6 or 18.6 of the Agreement for Lease.

"**Indexed Par Amount**" means the Outstanding Principal Amount of the relevant Bond multiplied by the RPI(0,6) Index Ratio applicable to the month in which the date on which the notice is given that the Bonds are immediately due and payable falls (an RPI(0,6) Index Ratio of 1 being expressed as 100 per cent).

"**ProjectCo Termination Event**" means, following a default by ProjectCo in its capacity as servicer provider under the Project Agreement, the termination of the Project Agreement under clause 25A and/or clause 39.2 (where clause 39.4 applies) of the Project Agreement and/or on termination of the Agreement for Lease under clauses 5.7 or 19.1 of the Agreement for Lease

"**Reference Date**" means for the purpose of calculating the Early Redemption Amount under (i) Condition 6(b), the date that is two business days prior to the despatch of the notice of redemption under that Condition and (ii) Condition 6(d), the date that is two business days prior to the date on which Compensation on Termination is payable under the Project Agreement (as the case may be):

"**Relevant Benchmark Yield**" means the higher of (A) and (B) below where:

(A) is the lower of (i) the real yield on the index-linked UK Government Gilt whose maturity date most closely matches the weighted average life of the Bonds on the Reference Date as an Indexation Adviser shall determine to be appropriate and (ii) the nominal yield on the conventional (ie not index-linked) UK Government Gilt whose maturity date most closely matches the weighted average life of the Bonds on the Reference Date as an Indexation Adviser shall determine to be appropriate; and

(B) is the nominal yield on the conventional (ie not index-linked) UK Government Gilt whose maturity date most closely matches the weighted average life of the Bonds on the Reference Date as an Indexation Adviser shall determine to be appropriate less 6%.

"**UK Government Gilt**" means Sterling denominated gilt or stock issued by or on behalf of Her Majesty's Treasury.

"**University Termination Event**" means, following a default by the University, the termination of the Project Agreement pursuant to clause 26 and/or clause 39.2 (where clause 39.3 applies) and/or clause 9.5.2 of the Project Agreement.

(h) *No other Redemption*

Without prejudice to Condition 11 (*Events of Default*), the Issuer, any Affiliate of the Issuer or any Shareholder shall not be entitled to redeem, purchase or cancel the Bonds (other than those held by or on behalf of any Obligor or any Affiliate of an Obligor or Shareholder of an Obligor) in whole or in part otherwise than as provided in Conditions 6(a) (*Scheduled Redemption*), 6(b) (*Redemption at the option of the Issuer*), 6(c) (*Redemption for Index Reasons*), 6(d) (*Mandatory Redemption – Above Par Redemption*), 6(e) (*Mandatory Redemption – Below Par Redemption*), 6(i) (*Purchase*) and 6(j) (*Cancellation*).

(i) *Purchase*

The Issuer, any Affiliate of the Issuer or any Shareholder may at any time purchase Bonds in the open market or otherwise and at any price, provided that all unmatured Coupons and

unexchanged Talons appertaining thereto are purchased therewith. Any purchase by tender by the Issuer shall be made available to all Bondholders alike. Any Bonds so purchased shall be surrendered and cancelled.

(j) *Cancellation*

All Bonds so redeemed or purchased and surrendered for cancellation by the Issuer and any unmatured Receipts or Coupons or unexchanged Talons attached to or surrendered with them shall be cancelled and may not be reissued or resold

7. **Indexation**

(a) *Definitions*

"**Base Index Figure**" means (subject to Condition 8(a)(ii) the Index Figure relating to November 2016, being 265.5.

"**Index**" means, subject as provided in Condition 7, the UK All Items Retail Prices Index as published by the United Kingdom Office for National Statistics (January 1987 = 100) contained in the Monthly Digest of Statistics (or contained in any official publication substituted therefor) or any comparable index which may replace the Index for the purpose of calculating the amount payable on repayment of the Reference Gilt.

"**Index Figure**" means, at any relevant time, the "value" of the Index.

Any reference to the Index Figure "applicable to a particular month" shall, subject as provided in Condition 8 (*Changes in circumstances affecting the Index*), be construed as a reference to the Index Figure for the third month prior to that particular month.

"**Indexation Adviser**" means a leading broker, primary dealer or other expert operating in the index-linked gilt market selected by the Issuer and the Controlling Creditor.

"**LPI Semi-Annual Ratio**" means:

(A) in respect of a date falling less than six months after the Issue Date, the ratio of:

(1) the Index Figure for such date; over

(2) the Base Index Figure,

provided that;

(a) if such ratio is greater than 106%^(N/12) it shall be deemed to be 106%^(N/12); and

(b) if such ratio is less than 100%, it shall be deemed to be 100%.

(B) in respect of any date falling thereafter, the ratio of Index Figures for:

(1) such date; over

(2) the date falling six months prior to such date, provided that:

(a) if such ratio is greater than 106%^(N/12), it shall be deemed to be 106%^(N/12); and

(b) if such ratio is less than 100% , it shall be deemed to be 100%

Where N = number of full months since the later of the Issue Date and the previous Scheduled Payment Date.

"**Limited Index Figure**" means:

(A) as applicable on any date in the period up to and excluding the six month anniversary of the Issue Date, subject as provided in Condition 8 (*Changes in circumstances affecting the index*), the Base Index Figure multiplied by (the LPI Semi-Annual Ratio applicable to such date – X*N/12); and

(B) as applicable to any subsequent date, subject as provided in Condition 8 (*Changes in circumstances affecting the index*), the Limited Index Figure as previously calculated in respect of the date six months prior thereto, multiplied by (the LPI Semi-Annual Ratio applicable to such date – X*N/12),

Where:

"X" = 0.319%

"N" = the number of full months since the later of the Issue Date and the previous Scheduled Payment Date.

"**Outstanding Principal Amount**" means, in respect of each Bond, the principal amount (or, as the context may require, the relevant number thereof or an individual Bond) outstanding for the time being before indexation as described in this Condition 7 as reduced by payments of Scheduled Principal or other amounts in respect of principal (each unadjusted for indexation) in accordance with Condition 6 (*Redemption and Purchase*).

"**RPI(0,6) Index Ratio**" applicable to any month means the Limited Index Figure applicable to such month divided by the Base Index Figure.

(b) *Application of the RPI(0,6) Index Ratio*

Each payment of interest and principal in respect of the Bonds shall, except where the context otherwise requires, be the amount provided in or determined in accordance with the foregoing Conditions, multiplied by the RPI(0,6) Index Ratio applicable to the month in which such payment falls to be made and rounded in accordance with Condition 19 (*Rounding*).

If the Calculation Agent is applying the RPI(0,6) Index Ratio to any payment of principal or interest in accordance with the paragraph above, it shall notify the Issuer and the Bond Trustee of the RPI(0,6) Index Ratio applied by it. For the avoidance of doubt, no additional monitoring of the Index is required by the Calculation Agent.

8. **Changes in circumstances affecting the Index**

(a) *Change in base*

If at any time and from time to time the Index shall be changed by the substitution of a new base therefor, then with effect from the calendar month from and including that in which such substitution takes effect:

(i) the definition of "Index" in Condition 7(a) (*Definitions*) shall be deemed to refer to the new date or month in substitution for January 1987 (or, as the case may be, to such other date or month as may have been substituted therefor); and

(ii) the new Base Index Figure shall be the product of the existing Base Index Figure and the Index Figure immediately following such substitution, divided by the Index Figure immediately prior to such substitution.

For the purposes of determining whether the Index is changed by the substitution of a new base therefor, the Calculation Agent shall refer in all cases to the information provided in https://www.ons.gov.uk/economy/inflationandpriceindices or such successor websites as are made publically available by the Office of National Statistics or any successor body responsible for publishing the Index and shall notify the Bond Trustee and Issuer of such change.

(b) *Delay in publication of Index*

If the Index Figure relating to any month (the "**relevant month**") which is required to be taken into account for the purposes of the determination of the Index Figure applicable for any date is not published on or before the fourteenth business day before the date (the "**date for payment**") on which such payment is due, the Index Figure applicable to the month in which the date of payment falls shall be:

(i) such substitute index figure (if any) as the Controlling Creditor determines to have been published by the Bank of England for the purposes of indexation of payments on any one or more issues of index-linked Gilts selected by the Indexation Adviser and approved by the Controlling Creditor; or

(ii) if no such determination is made by the Controlling Creditor within seven days, the Index Figure last published (or, if later, the substitute index figure last determined pursuant to Condition 9(b)(ii)) before the date for payment.

Where the provisions of this Condition 9(b) apply, the determination of the Controlling Creditor as to the Index Figure applicable to the month in which the date for payment falls shall be conclusive and binding. If, an Index Figure having been applied pursuant to Condition 9(b)(i), the Index Figure relating to the relevant month is subsequently published while a Bond is still outstanding, then:

(i) in relation to a payment of principal or interest in respect of such Bond other than upon final redemption of such Bond, the principal or interest (as the case may be) next payable after the date of such subsequent publication shall be increased or reduced by an amount equal to (respectively) the shortfall or excess of the amount of the relevant payment made on the basis of the Index Figure applicable by virtue of Condition 9(b)(ii), below or above the amount of the relevant payment that would have been due if the Index Figure subsequently published had been published on or before the fourteenth business day before the date for payment; and

(ii) in relation to a payment of principal or interest upon final redemption, no subsequent adjustment to amounts paid will be made.

(c) *Cessation of or fundamental changes to the Index*

(i) If (a) the Bond Trustee has been notified by the Calculation Agent that the Index has ceased to be published or (b) any change is made to the coverage or the basic calculation of the Index which constitutes a fundamental change which would, in the opinion of the Bond Trustee acting solely on the advice of an Indexation Adviser, be materially prejudicial to the interests of the Bondholders, the Bond Trustee will give written notice of such occurrence to the Issuer, AGE and AGM (collectively the "**Parties**"), and the Parties together shall seek to agree for the purpose of the Bonds one or more adjustments to the Index or a substitute index (with or without adjustments) with the intention that the same should leave the Parties and the Bondholders in no better and no worse position than they would have been had the Index not ceased to be published or the relevant fundamental change not been made.

(ii) For the purposes of determining whether the Index has ceased to be published or any change is made to the coverage or the basic calculation of the Index, the Calculation Agent shall refer in all cases to the information provided on https://www.ons.gov.uk/economy/inflationandpriceindices or such successor websites as are made publically available by the Office of National Statistics or any successor body responsible for publishing the Index and shall notify the Bond Trustee and Issuer of such change.

(iii) If the Parties fail to reach agreement as mentioned above within 20 business days following the giving of notice as mentioned in paragraph (i), a bank or other person in London shall be appointed by the Parties (in each case, such bank or other person so appointed being referred to as the "**Expert**"), to determine for the purpose of the Bonds

one or more adjustments to the index or a substitute index (with or without adjustments) with the intention that the same should leave the Parties and the Bondholders in no better and no worse position than they would have been had the Index not ceased to be published or the relevant fundamental change not been made. Any Expert so appointed shall act as an expert and not as an arbitrator and all fees, costs and expenses of the Expert and of any Indexation Adviser and of any of the Parties in connection with such appointment shall be borne by the Issuer. In this Condition 8, "**business day**" means any day on which commercial banks and foreign exchange markets are open for business in London.

(iv) The Index shall be adjusted or replaced by a substitute index as agreed by the Parties and the Bond Trustee or as determined by the Expert and as advised in writing to the Issuer, the Calculation Agent and the Bond Trustee pursuant to the foregoing paragraphs, as the case may be, and references in these Conditions to the Index and to any Index Figure shall be deemed amended in such manner as the Controlling Creditor agrees notifies to the Parties, as appropriate to give effect to such adjustment or replacement. Such amendments shall be effective from the date of such notification and binding upon the Parties, the Bond Trustee and the Bondholders, and the Issuer shall give notice to the Bondholders in accordance with Condition 17 (*Notices*) of such amendments as promptly as practicable following such notification.

9. Payments and Exchange of Talons

(a) *Scheduled Payments*

The Issuer will in respect of each £1,000 in original principal amount of Bonds then outstanding on each Scheduled Payment Date make a total payment, comprising the relevant payment of Scheduled Interest and, if applicable, the relevant payment of Scheduled Principal (both adjusted for indexation in accordance with Condition 7 (*Indexation*)) on each Scheduled Payment Date:

Without prejudice to Condition 4 (*Interest*) and Condition 6 (*Redemption and Purchase*), the figures for Scheduled Interest and Total Payment set out below are intended to illustrate the Scheduled Interest and Total Payment in respect of each £1000 in original principal amount of the Bonds and are set out unadjusted for indexation. The figures for Scheduled Principal and Outstanding Principal Amount set out below provide the Outstanding Principal Amount (assuming all payments are made on the due date in full) and Scheduled Principal in respect of each £1,000 in original principal amount of the Bonds and are set out unadjusted for indexation.

A. Scheduled Payment Date	B. Scheduled Principal per £1,000 (before indexation)	C. Scheduled Interest per £1,000 (before indexation)	D. Total Payment per £1,000 (before indexation)	E. Outstanding Principal Amount per £1,000
28 Feb 17	0.41	0.01	0.42	999.59
31 Aug 17	16.89	0.50	17.39	982.70
28 Feb 18	11.29	0.49	11.78	971.41
31 Aug 18	11.43	0.49	11.92	959.98
28 Feb 19	11.57	0.48	12.05	948.41
31 Aug 19	11.58	0.47	12.05	936.83
29 Feb 20	11.74	0.47	12.21	925.09
31 Aug 20	11.72	0.46	12.18	913.37
28 Feb 21	11.93	0.46	12.39	901.44
31 Aug 21	11.87	0.45	12.32	889.57
28 Feb 22	11.99	0.44	12.43	877.58
31 Aug 22	11.94	0.44	12.38	865.64
28 Feb 23	12.02	0.43	12.45	853.62

A. Scheduled Payment Date	B. Scheduled Principal per £1,000 (before indexation)	C. Scheduled Interest per £1,000 (before indexation)	D. Total Payment per £1,000 (before indexation)	E. Outstanding Principal Amount per £1,000
31 Aug 23	12.05	0.43	12.48	841.57
29 Feb 24	12.03	0.42	12.45	829.54
31 Aug 24	12.03	0.41	12.44	817.51
28 Feb 25	12.04	0.41	12.45	805.47
31 Aug 25	11.37	0.40	11.77	794.10
28 Feb 26	11.17	0.40	11.57	782.93
31 Aug 26	11.12	0.39	11.51	771.81
28 Feb 27	11.26	0.39	11.65	760.55
31 Aug 27	11.19	0.38	11.57	749.36
29 Feb 28	11.28	0.37	11.65	738.08
31 Aug 28	11.31	0.37	11.68	726.77
28 Feb 29	11.34	0.36	11.70	715.43
31 Aug 29	11.33	0.36	11.69	704.10
28 Feb 30	11.38	0.35	11.73	692.72
31 Aug 30	11.30	0.35	11.65	681.42
28 Feb 31	11.35	0.34	11.69	670.07
31 Aug 31	11.27	0.34	11.61	658.80
29 Feb 32	11.42	0.33	11.75	647.38
31 Aug 32	11.37	0.32	11.69	636.01
28 Feb 33	10.78	0.32	11.10	625.23
31 Aug 33	10.83	0.31	11.14	614.40
28 Feb 34	10.82	0.31	11.13	603.58
31 Aug 34	10.82	0.30	11.12	592.76
28 Feb 35	10.84	0.30	11.14	581.92
31 Aug 35	10.87	0.29	11.16	571.05
29 Feb 36	10.89	0.29	11.18	560.16
31 Aug 36	10.92	0.28	11.20	549.24
28 Feb 37	11.03	0.27	11.30	538.21
31 Aug 37	11.02	0.27	11.29	527.19
28 Feb 38	11.10	0.26	11.36	516.09
31 Aug 38	11.08	0.26	11.34	505.01
28 Feb 39	11.25	0.25	11.50	493.76
31 Aug 39	11.24	0.25	11.49	482.52
29 Feb 40	11.41	0.24	11.65	471.11
31 Aug 40	11.40	0.24	11.64	459.71
28 Feb 41	11.57	0.23	11.80	448.14
31 Aug 41	11.55	0.22	11.77	436.59
28 Feb 42	11.60	0.22	11.82	424.99
31 Aug 42	11.61	0.21	11.82	413.38
28 Feb 43	11.71	0.21	11.92	401.67
31 Aug 43	11.69	0.20	11.89	389.98
29 Feb 44	11.79	0.20	11.99	378.19
31 Aug 44	11.78	0.19	11.97	366.41
28 Feb 45	11.88	0.18	12.06	354.53
31 Aug 45	11.86	0.18	12.04	342.67

A. Scheduled Payment Date	B. Scheduled Principal per £1,000 (before indexation)	C. Scheduled Interest per £1,000 (before indexation)	D. Total Payment per £1,000 (before indexation)	E. Outstanding Principal Amount per £1,000
28 Feb 46	12.10	0.17	12.27	330.57
31 Aug 46	12.08	0.17	12.25	318.49
28 Feb 47	12.32	0.16	12.48	306.17
31 Aug 47	12.30	0.15	12.45	293.87
29 Feb 48	12.53	0.15	12.68	281.34
31 Aug 48	12.58	0.14	12.72	268.76
28 Feb 49	12.54	0.13	12.67	256.22
31 Aug 49	12.70	0.13	12.83	243.52
28 Feb 50	12.74	0.12	12.86	230.78
31 Aug 50	12.85	0.12	12.97	217.93
28 Feb 51	12.90	0.11	13.01	205.03
31 Aug 51	13.01	0.10	13.11	192.02
29 Feb 52	13.06	0.10	13.16	178.96
31 Aug 52	13.06	0.09	13.15	165.90
28 Feb 53	13.13	0.08	13.21	152.77
31 Aug 53	13.17	0.08	13.25	139.60
28 Feb 54	13.22	0.07	13.29	126.38
31 Aug 54	13.27	0.06	13.33	113.11
28 Feb 55	13.32	0.06	13.38	99.79
31 Aug 55	13.36	0.05	13.41	86.43
29 Feb 56	13.41	0.04	13.45	73.02
31 Aug 56	13.46	0.04	13.50	59.56
28 Feb 57	13.51	0.03	13.54	46.05
31 Aug 57	13.55	0.02	13.57	32.50
28 Feb 58	13.61	0.02	13.63	18.89
31 Aug 58	18.89	0.01	18.90	0.00

Following any payment of the Below Par Redemption Amount in accordance with Condition 6(e) (*Mandatory Early Redemption – ProjectCo Termination Event*), the amounts listed in Columns B to E above will be adjusted to reflect such payment from the Scheduled Payment Date following such payment.

For the avoidance of doubt, the number of Bonds in issue will not be reduced by the scheduled payments of Scheduled Principal in Column B and payment pursuant to Condition 6(d) (*Mandatory Early Redemption – University Termination Event and Compulsory Change Termination Event*) or 6(e) (*Mandatory Early Redemption – ProjectCo Termination Event*). Payments of Scheduled Principal (unadjusted for indexation) will reduce the Outstanding Principal Amount of each Bond *pro rata*.

(b) *Method of Payment*

Payments in respect of the Bonds by the Issuer will be made only against:

(i) presentation and surrender of the appropriate Coupons (in the case of interest) and the relevant Receipt (in the case of principal); and

(ii) in the case of final redemption (provided that payment is made in full) surrender of the relevant Bonds,

at the specified office of any Paying Agent outside the United States by sterling cheque drawn on, or by transfer to a sterling account maintained by the payee with, a bank in London.

(c) *Payments subject to Fiscal Laws*

All payments in respect of the Bonds are subject in all cases to any applicable fiscal or other laws and regulations, but without prejudice to the provisions of Condition 10 (*Taxation*). No commissions or expenses shall be charged to the Bondholders, Receiptholders or Couponholders in respect of such payments.

(d) *Unmatured Receipts and Coupons Void*

On the early redemption in full of any Bond pursuant to Conditions 6(b) (*Redemption at the option of the Issuer*), 6(c) (*Redemption for Index Reasons*), 6(d) (*Mandatory Early Redemption – University Termination Event and Compulsory Change Termination Event*), 6(e) (*Mandatory Early Redemption – ProjectCo Termination Event*), 6(j) (*Cancellation*) or 11 (*Events of Default*), all unmatured Receipts or Coupons relating thereto (whether or not still attached) shall become void and no payment will be made in respect thereof.

(e) *Payments on Business Days*

If the due date for payment of any amount in respect of any Bond, Receipt or Coupon is not a business day in the place of presentation (and in the case of any payment by transfer to a sterling account in London), the holder shall not be entitled to payment in such place of the amount due until the next following business day in such place and shall not be entitled to any further interest or other payment in respect of any such delay. In this paragraph, "**business day**" means, in respect of any place of presentation, any day on which banks are open for business in such place of presentation and, in the case of payment by transfer to a sterling account as referred to above, on which dealings in foreign currencies may be carried on both in London and New York and in such place of presentation.

(f) *Payments otherwise than against the Surrender of Receipts or Coupons*

If a Paying Agent makes a payment in respect of any Bond in circumstances where no Receipt or Coupon is surrendered, such Paying Agent will endorse on such Bond a statement indicating the amount and date of such payment.

(g) *Fractions*

In respect of any payments to Bondholders any fractions of one pound will be rounded in accordance with Condition 19 (*Rounding*).

(h) *Exchange of Talons*

On or after the maturity date of the final Coupon which is (or was at the time of issue) part of a coupon sheet relating to the Bonds (each a "**Coupon Sheet**"), the Talon forming part of such Coupon Sheet may be exchanged at the specified office of the Principal Paying Agent for a further Coupon Sheet excluding any Coupons in respect of which claims have already become void pursuant to Condition 12 (*Prescription*). Upon the due date for redemption of any Bond, any unexchanged Talon relating to such Bond shall become void and no Coupon will be delivered in respect of such Talon.

10. Taxation

All payments of principal and interest in respect of the Bonds by the Issuer shall be made free and clear of, and without withholding or deduction for, any taxes, duties, assessments or governmental charges of whatsoever nature unless such withholding or deduction is required by law.

In that event, the Issuer shall account to the relevant authorities for the amount to be withheld or deducted and shall make such payment of principal or interest, as the case may be, after such withholding or deduction has been made.

The Issuer shall notify the Bond Trustee of any such withholding or deduction and shall take reasonable measures available to it to avoid such obligation including the replacement of the Principal Paying Agent, the addition, replacement or removal of a Paying Agent or changing the specified office of any Paying Agent. Should the Issuer still be obliged to make the withholding or deduction, it will, on written request from any Bondholder, provide to the Bondholder copies of any documentation or correspondence with the tax authority regarding the deduction or withholding as the Bondholder may reasonably require to assist it to reclaim such deduction or withholding.

The Issuer will not be obliged to make any additional payments to Bondholders, Receiptholders or Couponholders in respect of any such withholding or deduction.

To the extent that the Issuer is obliged to make any such deduction or withholding, there is no obligation on the Financial Guarantors to make good any such amount so deducted or withheld under the Financial Guarantees.

11. **Events of Default**

After any event of default pursuant to the terms of the Collateral Deed (an "**Event of Default**") occurs and is continuing, then:

(a) if and for so long as the Financial Guarantors are the Controlling Creditor, the Bond Trustee shall, upon being (a) so directed by the Financial Guarantors in accordance with the Security Trust and Intercreditor Deed; and (b) prefunded, and/or indemnified and/or secured to its satisfaction, declare by written notice to the Issuer that the Bonds are immediately due and payable; or

(b) if and for so long as the Financial Guarantors are not the Controlling Creditor, the Bond Trustee may at any time and shall, upon being (a) so requested in writing by the holders of at least 25 per cent. in Outstanding Principal Amount of the then outstanding Bonds (as defined in the Bond Trust Deed) or so directed by a resolution passed at any meeting of the Bondholders by a majority of not less than three quarters of the votes cast (an "**Extraordinary Resolution**"); and (b) prefunded and/or indemnified and/or secured to its satisfaction, declare by written notice to the Issuer that the Bonds are immediately due and payable,

whereupon without further action or formality each Bond shall become due and payable at its Early Redemption Amount, together with accrued interest up to the date of redemption adjusted for indexation (the Index Ratio for this purpose being that applicable to the month in which the date on which the notice is given that the Bonds are immediately due and payable falls).

For a summary description of the Events of Default, see the section entitled "Refinancing of the Project —Collateral Deed".

Such an acceleration of sums due on the Bonds does not accelerate AGE's and/or AGM's payment obligation under the Financial Guarantees. AGE and/or AGM shall only be liable to make payments in respect of the Bonds (pursuant to the Financial Guarantees) on the dates on which such payments would have been required to be made if such amounts had not become immediately due and payable.

While the Financial Guarantors are the Controlling Creditor, save in the circumstances set out in Condition 6(d) (*Mandatory Early Redemption – University Termination Event and Compulsory Change Termination Event*) and 6(e) (*Mandatory Early Redemption – ProjectCo Termination Event*) and as described below, neither the Bondholders nor the Bond Trustee will have any rights to call for repayment of the Bonds following the occurrence of an Event of Default or for any enforcement of the security for the Bonds unless instructed or directed by the Financial Guarantors.

12. **Prescription**

Claims for principal and interest shall become void unless the relevant Receipts and/or Coupons and/or the relevant Bonds (as the case may be) are presented for payment within five years (in the case of interest) and ten years (in the case of principal) of the later of (i) the date on which the payment in question first becomes due and (ii) if the full amount payable has not been received by the Principal

Paying Agent or the Bond Trustee on or prior to such due date, the date on which (the full amount having been so received) notice to that effect has been given to the Bondholders.

13. **Replacement of Bonds, Receipts, Coupons and Talons**

If any Bond, Receipt, Coupon or Talon is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Principal Paying Agent, subject to all applicable laws and stock exchange (or other relevant authority) requirements, upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer may reasonably require. Mutilated or defaced Bonds, Receipts, Coupons or Talons must be surrendered before replacements will be issued.

14. **Bond Trustee, Security Trustee and Paying Agents**

(a) Under the Bond Trust Deed, the Bond Trustee is entitled to be indemnified and relieved from responsibility in certain circumstances and monies received by the Bond Trustee will be applied to pay its liabilities, costs and expenses and other amounts due to it in priority to the claims of the Bondholders. In addition, the Bond Trustee is entitled to enter into business transactions with the Obligors, the Financial Guarantors, the Bondholders, the Receiptholders, the Couponholders and any entity related to the Obligors, the Financial Guarantors or any other party to the Relevant Documents without accounting for any profit.

(b) In the exercise of its powers, trusts, authorities and discretions under these Conditions, the Financial Guarantees and the Bond Trust Deed, the Bond Trustee will have regard to the interests of the Bondholders as a class and will not have regard to the consequences of such exercise for individual Bondholders, Receiptholders or Couponholders (whatever their number) whether resulting from their being resident or domiciled in any particular jurisdiction or otherwise and the Bond Trustee shall not be entitled to require from the Obligors, the Financial Guarantors or the Security Trustee, nor shall any Bondholder, Receiptholder or Couponholder be entitled to claim from the Obligors, the Financial Guarantors, the Bond Trustee or the Security Trustee, any indemnification or other payment in respect of any consequence (including, without limitation, any tax consequence) for individual Bondholders, Receiptholders or Couponholders of any such exercise.

(c) Under the Security Trust and Intercreditor Deed, the Security Trustee is entitled to be indemnified and relieved from responsibility in certain circumstances and to be paid its liabilities, costs and expenses and other amounts due to it in priority to the claims of the Bondholders. In addition the Security Trustee is entitled to enter into business transactions with the Obligors, the Financial Guarantors, the Bondholders, the Receiptholders, the Couponholders and any entity related to the Obligors, the Financial Guarantors or any other party to the Relevant Documents without accounting for any profit.

(d) Neither the Bond Trustee nor the Security Trustee has investigated nor are either of them responsible or liable for any loss arising as a result of any failure to investigate the legality, validity, value, sufficiency or enforceability of the security created by the Security Documents or the validity or enforceability of any contracts over which such security is created or of the Financial Guarantees and both the Bond Trustee and the Security Trustee shall accept without investigation, requisition or objection and without any responsibility or liability for doing so such right and title as the Obligors have to the property assets and rights over which security is created pursuant to the Security Documents.

(e) The Security Trustee has no responsibility for the validity or enforceability of any obligation of any other party under any Relevant Documents.

(f) The Bond Trustee has no responsibility for the validity or enforceability of the AGE Financial Guarantee against AGE or any permitted assignee of AGE under the AGE Financial Guarantee or the AGM Financial Guarantee against AGM or any permitted assignee of AGM under the AGM Financial Guarantee.

(g) The Bond Trustee will not be liable to Bondholders for any loss they may suffer as a result of any termination of the AGE Financial Guarantee or the AGM Financial Guarantee resulting

from any act or omission on the part of the Bond Trustee unless the consequences of such act or omission were notified in writing to the Bond Trustee in accordance with the Bond Trust Deed prior to such act or omission occurring and the Bond Trustee so acted or omitted to do so negligently or in wilful default.

(h) Neither the Bond Trustee nor the Security Trustee will be responsible for or liable for loss which results should any deficiency arise between the amount realised in respect of the assets and rights over which security is given by the Security Documents and sums due in respect of the Bonds because the Security Trustee or the Bond Trustee is liable to tax in respect of the property assets and rights over which such security is created.

(i) None of the Security Trustee, the Bond Trustee and the Principal Paying Agent shall be responsible for monitoring the obligations of any person to the Issuer and each of them shall, until they have received notice in writing to the contrary, assume that all persons are duly performing the same.

(j) Neither the Security Trustee nor the Bond Trustee will be obliged to take any action under the Bond Trust Deed or the Security Trust and Intercreditor Deed unless either or each is prefunded and/or indemnified and/or secured to its satisfaction in respect of any liability, loss, cost or expense which it may in its opinion incur. Protection and realisation of the security may be prevented or delayed as a result.

(k) None of the Bond Trustee, the Security Trustee and the Principal Paying Agent shall be responsible for monitoring compliance by the Issuer or any other person with any matter set out in the Collateral Deed including whether an Event of Default or Potential Event of Default has occurred and, if the Bond Trustee is the Controlling Creditor, and is for whatever reason required to make any determination of material adverse change, or like matter, pursuant to the terms of the Collateral Deed, it may, in its absolute discretion, seek directions from the Bondholders or seek advice from an expert, both in accordance with the Bond Trust Deed and the Bond Trustee will not be responsible for the consequences of any delay involved in so doing.

(l) In acting under the Paying Agency Agreement and in connection with the Bonds, the Receipts and the Coupons, the Paying Agents act solely as agents of the Issuer and (to the extent provided therein) the Bond Trustee and do not assume any obligations towards or relationship of agency or trust for or with any of the Bondholders, Receiptholders or Couponholders.

(m) The initial Paying Agents and their initial specified offices are listed below. The Issuer reserves the right (with the prior approval of the Bond Trustee) at any time to vary or terminate the appointment of any Paying Agent and to appoint a successor principal paying agent and additional or successor paying agents; provided, however, that the Issuer shall at all times maintain (i) a Principal Paying Agent (ii) so long as the Bonds are admitted to listing on the Official List and to trading on the Irish Stock Exchange's market for listed securities, at least one Paying Agent with a specified office in the European Union and (iii) if so required by the Controlling Creditor, at least one Paying Agent with a specified office outside the European Union. Notice of any change in any of the Paying Agents or in their specified offices shall promptly be given by the Issuer to the Bondholders in accordance with Condition 17 (*Notices*).

(n) The Issuer has covenanted in the Collateral Deed that, upon delivery to it by ProjectCo, it will publish either through an electronic website or through the Principal Paying Agent via the bond clearing system the Bondholder Report.

(o) The Bond Trustee shall be entitled to rely on certificates and reports of the auditors of the Issuer notwithstanding that such auditors' liability in respect thereof may be limited (by reference to a monetary cap or otherwise) and shall be entitled to enter into letters engaging the auditors to provide any certificate or report.

In acting as Bond Trustee under the Relevant Documents, the Bond Trustee shall, subject to clause 7.4 of the Bond Trust Deed, have regard solely to the interests of the Bondholders and not to any other Creditor or Beneficiary.

15. **Meetings of Bondholders; Modification and Waiver**

(a) *Meetings of Bondholders*

(i) Subject to Condition 15(b) (*Modification and Waiver*), the Bond Trust Deed contains provisions for convening single meetings of Bondholders to consider matters affecting their interests, including the modification of these Conditions, the Bond Trust Deed, the Financial Guarantees and any other Finance Documents, the Security Documents and the Collateral Deed. Any such modification may, subject to the prior written consent of the Financial Guarantors if they are the Controlling Creditor, be made if sanctioned by an Extraordinary Resolution (as defined in the Bond Trust Deed). A meeting of Bondholders will also have the power (exercisable by Extraordinary Resolution) to advise or instruct the Bond Trustee in connection with the exercise by the Bond Trustee, subject to Condition 16(a) (*Exercise and Enforcement*), of any of its rights, powers, trusts, authorities and discretions under the Finance Documents, to remove or approve the appointment of a new Bond Trustee and to appoint any persons (whether Bondholders or not) as a committee to represent the interests of the Bondholders and to confer upon such committee any powers which the Bondholders could themselves exercise by Extraordinary Resolution.

(ii) The quorum for all business other than an Extraordinary Resolution will be one or more persons present in person holding or representing 10 per cent. in aggregate outstanding principal amount of the Bonds, or at any meeting adjourned for want of a quorum, one or more persons being actually present at such meeting in person representing Bondholders whatever the principal amount of Bonds held or represented.

(iii) The quorum at any meeting convened to vote on an Extraordinary Resolution will be one or more persons present in person holding or representing 25 per cent. in outstanding principal amount of the Bonds or, at any adjourned meeting, one or more persons being actually present at such meeting in person representing Bondholders whatever the principal amount of the Bonds held or represented; provided, however, that certain proposals including any proposal:

(A) to change any date fixed for payment of principal, premium (if any) or interest in respect of the Bonds, to reduce the amount of principal, premium (if any) or interest payable on any date in respect of the Bonds to alter the method of calculating the amount of any payment in respect of the Bonds or the date for any such payment;

(B) to effect any exchange of the Bonds for, or the conversion of the Bonds into shares, bonds or other obligations of the Issuer, either Financial Guarantor or any other person or to approve the substitution of any person for the Issuer as principal obligor under the Bonds or the substitution of any person for AGE and/or AGM as guarantors under the Financial Guarantees (save as already provided therein);

(C) to change the currency of payments under the Bonds;

(D) to modify any provisions of the Financial Guarantees;

(E) to change the quorum required at any meeting of the Bondholders or the majority required to pass an Extraordinary Resolution;

(F) to release all or part of the Security other than in accordance with the Security Documents provided that for so long as the Financial Guarantors are the Controlling Creditor, this sub-clause (F) shall not apply;

(G) to alter the rights of priority on enforcement of the Bondholders under Clause 13 of the Security Trust and Intercreditor Deed;

(H) to exercise the rights under Condition 2(b) (*Financial Guarantees*); or

(I) to amend any of the above reserved matters,

(together the "**Reserved Matters**") may only be sanctioned by an Extraordinary Resolution passed at a meeting of Bondholders at which one or more persons present in person holding or representing not less than three-quarters or, at any meeting adjourned for want of a quorum, at least 25 per cent. in aggregate outstanding principal amount of the Bonds form a quorum. Any Extraordinary Resolution duly passed at any such meeting shall be binding on all the Bondholders, Receiptholders and Couponholders whether present or not.

The majority required for an Extraordinary Resolution in respect of:

(A) a matter other than in respect of a Reserved Matter, is 25 per cent of the votes cast, or, at any meeting adjourned for want of a quorum, the votes cast by one or more persons being actually present at such meeting in person representing Bondholders whatever the principal amount of the Bonds held or represented; and

(B) in respect of a Reserved Matter, 75 per cent of the votes cast, or at any meeting adjourned for want of a quorum, the votes cast by one or more persons present in person holding or representing at least 25 per cent. in aggregate outstanding principal amount of the Bonds.

In addition, a resolution in writing signed by or on behalf a majority of Bondholders who for the time being are entitled to receive notice of a meeting of Bondholders under the Bond Trust Deed will take effect as if it were an Extraordinary Resolution. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Bondholders.

(b) *Modification and Waiver*

If it is then the Controlling Creditor, subject to clause 5 (*Consent of Controlling Creditor and Entrenched Rights and Reserved Matters of Senior Creditors*) of the Security Trust and Intercreditor Deed, the Bond Trustee may, without the consent or sanction of the Bondholders, Receiptholders or Couponholders concur with the Issuer, the Financial Guarantors or any other relevant parties in making:

(i) any modification to these Conditions, the Bond Trust Deed, the Financial Guarantees, the Security Documents, the Collateral Deed and any other Relevant Document which is in the opinion of the Bond Trustee of a formal, minor or technical nature or is made to correct a manifest error; or

(ii) any other modification of any such document which is in the opinion of the Bond Trustee not materially prejudicial to the interests of Bondholders.

For the avoidance of doubt, and notwithstanding the foregoing, the Bond Trustee, if it is then the Controlling Creditor, shall have the unfettered right to seek the consent of the Bondholders to the making of any such modification, provided that the Bond Trustee shall act in accordance with the directions in writing to it of the holders of at least 25 per cent. in aggregate principal amount of the Bonds outstanding or with an Extraordinary Resolution where the same are relevant or passed.

If the Bond Trustee is then the Controlling Creditor, subject to clause 5 (*Consent of Controlling Creditor and Entrenched Rights and Reserved Matters of Senior Creditors*) of the Security Trust and Intercreditor Deed, the Bond Trustee may also, without the consent or sanction of any of the Bondholders, Receiptholders or Couponholders, waive or authorise any Event of Default, any Potential Event of Default, any Financial Guarantor Default or any Financial Guarantor Downgrade Event or any other breach or proposed breach of the Bond Trust Deed, the Bonds, the Financial Guarantees, the Security Trust and Intercreditor Deed or any other Relevant Document to which it is a party, or determine that any Financial Guarantor Default or any Financial Guarantor Downgrade or any Event of Default or any Potential Event of Default shall not, or shall not subject to specified conditions, be treated as such or, in the

case of a Financial Guarantor Default or Financial Guarantor Downgrade Event, has been cured to its satisfaction, if the Bond Trustee is of the opinion that so to do will not be materially prejudicial to the interests of the Bondholders.

For the avoidance of doubt, (i) if it is then the Controlling Creditor, the Bond Trustee shall have the unfettered right to seek the consent of Bondholders to any such authorisation or waiver, provided that the Bond Trustee shall act in accordance with the directions in writing to it of the holders of at least 25 per cent. in aggregate principal amount of the Bonds outstanding or with an Extraordinary Resolution where the same are relevant or passed and (ii) if the Bond Trustee is not the Controlling Creditor, the Controlling Creditor controls all Financing Rights of the Senior Creditors under the Finance Documents, including those of the Bondholders and the Bond Trustee, subject only to clause 5 (*Consent of Controlling Creditor and Entrenched Rights and Reserved Matters of Senior Creditors*) of the Security Trust and Intercreditor Deed As further set out in that provision, if the Bond Trustee is not the Controlling Creditor but is asked to consent to any Proposal which is a Bond Trustee Entrenched Matter (each as defined in the Security Trust and Intercreditor Deed) then the Issuer shall call a meeting in accordance with Condition 15(a) to put such Proposal to the Bondholders. If no Extraordinary Resolution is passed, the Bondholders shall be deemed to authorise the Bond Trustee to withhold its consent to the Proposal. If such an Extraordinary Resolution is passed, its implementation shall in certain circumstances be subject to the additional consent of the Bond Trustee.

16. **Exercise and Enforcement**

(a) *Exercise and Enforcement*

As more particularly provided in the Security Trust and Intercreditor Deed, the Bond Trustee will be obliged to take action to exercise or enforce its rights under the Bond Trust Deed or the Security Documents or in respect of the Bonds if required to do so by the Controlling Creditor except in relation to certain specified rights of the Bond Trustee (provided that the Bond Trustee has been prefunded and/or indemnified and/or secured to its satisfaction) but will not in most circumstances be entitled to take any such action without the prior written consent of the Controlling Creditor. In any event, the Bond Trustee shall not be bound as against the Bondholders to take any such action unless:

(i) it has been so requested in writing by the holders of at least 25 per cent. in aggregate principal amount of the outstanding Bonds or has been so directed by an Extraordinary Resolution; and

(ii) it has been prefunded and/or indemnified and/or secured to its satisfaction.

The Bond Trustee is entitled to exercise certain rights reserved for the Bond Trustee's exercise in its sole discretion.

(b) *Action by Bondholders*

No Bondholder may take any action against the Issuer or the Financial Guarantors to enforce its rights in respect of the Bonds or to enforce all or any of the security constituted by the Security Documents or to enforce the Financial Guarantees unless the Bond Trustee having become bound so to proceed fails to do so within a reasonable time and such failure is continuing.

17. **Notices**

Notices to the Bondholders shall be valid if published in a leading English language daily newspaper published in the United Kingdom (which is expected to be the *Financial Times*). Any such published notice shall be deemed to have been given on the date of first publication. Receiptholders and Couponholders shall be deemed for all purposes to have notice of the contents of any notice given to the Bondholders, provided that for so long as the Bonds are admitted to trading on the Irish Stock Exchange, notices to Bondholders will be valid when such notice is filed at the Companies Announcement Office of the Irish Stock Exchange.

18. **Governing Law and Jurisdiction**

(a) *Governing law*

The Bond Trust Deed, the Bonds, the Receipts and the Coupons and all matters arising from or connected with these are governed by, and shall be construed in accordance with, English law. The Financial Guarantees and all matters arising from or connected with them are governed by, and will be construed in accordance with, English law.

(b) *English courts*

The courts of England have jurisdiction to settle any dispute (a "**Dispute**"), arising from or connected with the Bonds and the Bond Trust Deed.

(c) *Appropriate forum*

The Issuer agrees and the Financial Guarantors have agreed in the Bond Trust Deed that the courts of England are the most appropriate and convenient courts to settle any Dispute and, accordingly, that it will not argue to the contrary.

(d) *Rights of the Bondholders to take proceedings outside England*

Condition 18(c) is for the benefit of each of the Bond Trustee, the Bondholders, the Receiptholders and the Couponholders only. As a result, nothing in this Condition 18 prevents the Bond Trustee or any Bondholder from taking proceedings relating to a Dispute ("**Proceedings**") in any other courts with jurisdiction. To the extent allowed by law, the Bond Trustee and the Bondholders may take concurrent Proceedings in any number of jurisdictions.

19. **Rounding**

For the purposes of any calculations referred to in these Conditions (unless otherwise specified in these Conditions), (a) all percentages resulting from such calculations will be rounded, if necessary, to the nearest one hundred-thousandth of a percentage point (with 0.000005 per cent. being rounded up to 0.00001 per cent.), (b) all Sterling amounts used in or resulting from such calculations will be rounded to the nearest penny (with one half penny being rounded up), and (c) all amounts denominated in any other currency used in or resulting from such calculations will be rounded to the nearest two decimal places in such currency, with 0.005 being rounded upwards.

20. **Further Issues**

The Issuer may from time to time, without the consent of the Bondholders, the Receiptholders or Couponholders and in accordance with the Bond Trust Deed but subject to the provisions of the Collateral Deed, create and issue further bonds having the same terms and conditions as the Bonds in all respect (or in all respects except for the first payment of interest and the issue date) so as to form a single series with the Bonds and such further bonds will have the benefit of the Financial Guarantees or, with the Bond Trustee's consent may issue further bonds on such terms as to ranking, interest, conversion, redemption or otherwise as the Issuer may at the date of issue thereof determine.

21. **Rights of Third Parties**

No person shall have any right to enforce any term or condition of the Bonds or the Bond Trust Deed under the Contracts (Rights of Third Parties) Act 1999.

SUMMARY OF PROVISIONS RELATING TO THE BONDS WHILE IN GLOBAL FORM

The Temporary Global Bond and the Permanent Global Bond contain provisions which apply to the Bonds while they are in global form, some of which modify the effect of the terms and conditions of the Bonds set out in this Prospectus. The following is a summary of certain of those provisions:

Initial Issue of Bonds

The Bonds will be issued in new global note ("**NGN**") form and will be delivered on the instructions of the Issuer by the Principal Paying Agent to a common safekeeper for Euroclear and Clearstream, Luxembourg, as described below. The Bonds are intended to be held in a manner which will allow Eurosystem eligibility. However, depositing the Global Bonds with a common safekeeper does not necessarily mean that the Bonds will be recognised as eligible collateral for Eurosystem monetary policy and intra-day credit operations by the Eurosystem either upon issue, or at any or all times during their life. Such recognition will depend upon satisfaction of the Eurosystem eligibility criteria.

The nominal amount of the Bonds shall be the aggregate amount from time to time entered in the records of Euroclear or Clearstream, Luxembourg. The records of such clearing system shall be conclusive evidence of the nominal amount of Bonds represented by the Global Bonds and a statement issued by such clearing system at any time shall be conclusive evidence of the records of the relevant clearing system at that time.

Exchange

The Bonds will initially be represented by a Temporary Global Bond which will be deposited on or around the Issue Date with a common safekeeper for Euroclear and Clearstream, Luxembourg. The Temporary Global Bond will be exchangeable in whole or in part for interests in a Permanent Global Bond not earlier than 40 calendar days from (but not including) the Issue Date upon certification as to non-U.S. beneficial ownership. No payments will be made under the Temporary Global Bond unless exchange for interests in the corresponding Permanent Global Bond is improperly withheld or refused. In addition, interest payments in respect of the Bonds cannot be collected without such certification of non-U.S. beneficial ownership.

The Permanent Global Bond will become exchangeable in whole, but not in part, for Bonds in definitive form ("**Definitive Bonds**") in the denomination of £100,000 and integral multiples of £1,000 in excess thereof each at the request of the bearer of the relevant Permanent Global Bond against presentation and surrender of such Permanent Global Bond to the Principal Paying Agent if either of the following events (each an "**Exchange Event**") occurs: (a) Euroclear or Clearstream, Luxembourg or any additional or substitute clearing system (an "**Additional or Substitute Clearing System**") from time to time nominated by the Issuer or the Bond Trustee and approved by the Controlling Creditor through which the Bonds are cleared is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or does in fact do so (b) the Bonds become due and payable pursuant to Condition 11 (*Events of Default*).

The Permanent Global Bond will also become exchangeable, in whole but not in part only and at the option of the Issuer, for Definitive Bonds if, by reason of any change in the laws of the United Kingdom, the Issuer is or will be required to make any withholding or deduction from any payment in respect of the Bonds which would not be required if the Bonds were in definitive form.

If the Permanent Global Bond is to be exchanged for Definitive Bonds, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Bonds, duly authenticated and with Receipts, Coupons and Talons attached, in an aggregate principal amount equal to the principal amount outstanding of the Permanent Global Bond to the bearer of the Permanent Global Bond against the surrender of such Permanent Global Bond at the specified office of the Principal Paying Agent within 30 days of the occurrence of the relevant Exchange Event. In any such event, the Issuer will procure that details of such exchange be entered *pro rata* in the records of the relevant clearing system.

In addition, the Temporary Global Bond and Permanent Global Bond will contain provisions which modify the Terms and Conditions of the Bonds as they apply to such Temporary Global Bond and Permanent Global Bond. The following is a summary of certain of those provisions:

Payments

All payments in respect of the Temporary Global Bond and Permanent Global Bond will be made against presentation and (in the case of payment of principal in full with all interest accrued thereon) surrender of the Temporary Global Bond or (as the case may be) Permanent Global Bond at the specified office of any Paying Agent and will be effective to satisfy and discharge the corresponding liabilities of the Issuer in respect of the Bonds. The Issuer shall procure that details of each payment shall be entered *pro rata* in the records of the relevant clearing system, and in the case of payments of principal, the nominal amount of the Bonds recorded in the records of the relevant clearing system and represented by the Global Bond will be reduced accordingly.

Notices

Notwithstanding Condition 17 (*Notices*), as the case may be, while all the Bonds are represented by a Permanent Global Bond (or by a Permanent Global Bond and/or a Temporary Global Bond) and such Permanent Global Bond is (or such Permanent Global Bond and/or Temporary Global Bond are) deposited with a common safekeeper for Euroclear and Clearstream, Luxembourg or any Additional or Substitute Clearing System from time to time nominated by the Controlling Creditor, notices to Bondholders may be given by delivery to Euroclear and Clearstream, Luxembourg or any such Additional or Substitute Clearing System and such notices shall be deemed to have been given to the Bondholders in accordance with Condition 17 (*Notices*), as the case may be, on the second day after the day of delivery to Euroclear and Clearstream, Luxembourg or any such Additional or Substitute Clearing System.

Meetings

The holder of, or a proxy for the holder of, the Temporary Global Bond or the Permanent Global Bond will be treated as being two persons for the purposes of any quorum requirements of a meeting of the Bondholders.

Cancellation

Cancellation of any Bond represented by the Temporary Global Bond or the Permanent Global Bond will be effected by reduction in the principal amount of the Temporary Global Bond or the Permanent Global Bond (as the case may be). In any such event, the Issuer will procure that details of such exchange be entered *pro rata* in the records of the relevant clearing system.

USE OF PROCEEDS

The gross proceeds of the issue of the Bonds will amount to £98,200,000 and will be on-lent to ProjectCo to be used to fund the management, refinancing and operating costs and other expenditure (including fees, any refinancing gain (including that to be made available to the Shareholders pursuant to the Upstream Loan Agreements), and incidental costs and expenses) in relation to the Project, to pay commission and expenses incurred in relation to the issue of the Bonds, including the Manager's management commission, the financial guarantee fee payable to the Financial Guarantors in respect of the issue of the Financial Guarantees and certain of the issue and other related costs. The total estimated expenses to be paid by ProjectCo in relation to the admission to trading are approximately €6,641.20.

YIELD

On the basis of the issue price of the Bonds of 100 per cent., the yield of the Bonds is 0.100 per cent. on a semi-annual basis. The yield is calculated as at the issue date and at the issue price and is not a guarantee of future yield.

FORM OF AGE FINANCIAL GUARANTEE

Dated 24 February 2017

ASSURED GUARANTY (EUROPE) LTD.

FINANCIAL GUARANTEE No. 80179-U

in respect of

£98,200,000 0.100 per cent. Index-Linked Guaranteed Secured Bonds due 31 August 2058

This Financial Guarantee is dated 24 February 2017 and given by Assured Guaranty (Europe) Ltd. (Company Number 02510099) whose registered office is at 11th Floor, 6 Bevis Marks, London, EC3A 7BA (the "**Financial Guarantor**") in favour of BNY Mellon Corporate Trustee Services Limited as trustee for the holders of the Guaranteed Bonds (as defined below) (the "**Bond Trustee**", which expression shall, whenever the context admits, include such Persons for the time being the trustee or trustees of the Bond Trust Deed for the Guaranteed Bondholders).

1. **Interpretation**

1.1 **Definitions**

Any capitalised terms used in this Financial Guarantee and not otherwise defined shall have the meaning given to such terms in the Bond Trust Deed or the Master Definitions Schedule (each as defined below) unless the context otherwise requires. In the event of any inconsistency between the provisions of this Financial Guarantee and the provisions of the Bond Trust Deed and/or the Collateral Deed, this Financial Guarantee shall prevail. For the purposes of this Financial Guarantee, the following terms will have the following meanings:

"**Accelerated Payment**" means, following an Acceleration, any payment in full or in part by the Financial Guarantor or AGM, at the Financial Guarantor's or AGM's absolute option, of all or part of the Scheduled Principal in advance of the final Scheduled Payment Date together with accrued but unpaid Scheduled Interest on such Scheduled Principal to the date of such payment (but excluding any amounts referred to in items (i) to (iv) of the definition of "**Guaranteed Amount**").

"**Acceleration**" means, in relation to the Guaranteed Bonds, the giving of notice by the Bond Trustee to the Issuer that the Guaranteed Bonds are immediately due and repayable pursuant to Condition 11 (*Events of Default*), and "**Accelerated**" will be construed accordingly.

"**Account**" has the meaning set out in Clause 3.4.

"**Affiliate**" has the meaning given to it in the Master Definitions Schedule.

"**AGE Proportion**" means the proportion of the Financial Guarantees provided by the Financial Guarantor, which proportion is 8 per cent.

"**Agent**" means The Bank of New York Mellon, acting through its London Branch, as paying agent under the Guaranteed Bonds, and the term Agent shall include any successor to such Agent.

"**AGM**" has the meaning given to it in the Bond Trust Deed.

"**AGM Financial Guarantee**" means the financial guarantee dated on or about the date hereof, provided by AGM as financial guarantor, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with Clause 12.3 thereof.

"**AGM Proportion**" means the proportion of the Financial Guarantees provided by AGM, which proportion is 92 per cent.

"**Avoided Payment**" means any amount that is paid, credited, transferred or delivered to or to the order of the Bond Trustee or a Guaranteed Bondholder by or on behalf of the Issuer in accordance with the terms of the Bond Trust Deed and/or the Guaranteed Bonds in respect of any Guaranteed Amount, which amount has been recovered from, or is otherwise required to be returned or repaid by, the Bond Trustee or a Guaranteed Bondholder as a result of Insolvency Proceedings by or against the Issuer.

"**Bond Trust Deed**" means the bond trust deed dated on or about the date hereof between the Issuer, the Bond Trustee, the Financial Guarantor and AGM, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such bond trust deed with the prior written consent of the Financial Guarantor and AGM.

"**Business Day**" means any day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealings in foreign exchange and foreign currency deposits) in London and New York.

"**Collateral Deed**" means the collateral deed dated on or about the Issue Date between the Obligors, the Bond Trustee, the Security Trustee, the Financial Guarantor and AGM, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such collateral deed with the prior written consent of the Financial Guarantor and AGM.

"**Conditions**" means the terms and conditions of the Guaranteed Bonds as set out in Schedule 4 (Conditions of the Bonds) of the Bond Trust Deed, and "Condition" when used herein means such Condition as set out in Schedule 4 (*Conditions of the Bonds*) of the Bond Trust Deed and referred to herein.

"**Defaulted Amount**" means the portion of a Guaranteed Amount that is Due for Payment and unpaid by reason of Nonpayment by the Issuer, including any portion of any Guaranteed Amount that has become an Avoided Payment.

"**Due for Payment**" means, with respect to:

(a) Scheduled Interest on a Scheduled Payment Date, the amount of Scheduled Interest that is due and payable by the Issuer on such Scheduled Payment Date; and

(b) Scheduled Principal on a Scheduled Payment Date, the amount of Scheduled Principal that is due and payable by the Issuer on such Scheduled Payment Date,

in each case as each such Scheduled Payment Date occurs or would have occurred in accordance with the original terms of the Guaranteed Bonds and without regard to any prepayment, Acceleration or mandatory or optional redemption of the Guaranteed Bonds or any subsequent amendment or modification of the Guaranteed Bonds that has not been consented to in writing by the Financial Guarantor and AGM in accordance with the provisions of the Bond Trust Deed. For the avoidance of doubt, Due for Payment does not refer to any earlier date upon which payment of any Guaranteed Amounts may become due under the Guaranteed Bonds, by reason of prepayment, Acceleration, mandatory or optional redemption or otherwise.

"**Financial Guarantee**" means this Financial Guarantee No. 80179-U, without regard to any amendment, modification or supplement hereto other than any such amendment, modification or supplement made in accordance with Clause 12.3.

"**Financial Guarantees**" means this Financial Guarantee and the AGM Financial Guarantee.

"**Financial Guarantee Fee**" has the meaning given to it in the Financial Guarantee Fee Letter.

"**Financial Guarantee Fee Letter**" means the fee letter dated as of the date of this Financial Guarantee between the Financial Guarantor and the Obligors, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such fee letter with the prior written consent of the Financial Guarantor.

"**Financial Guarantor Default**" has the meaning given to it in the Security Trust and Intercreditor Deed.

"**Fiscal Agent**" has the meaning assigned thereto in Clause 9 (*Fiscal Agent*).

"**Force Majeure Event**" means any unforeseeable event outside the control of the Financial Guarantor that renders the Financial Guarantor's performance under this Financial Guarantee impossible (and not merely impracticable or more onerous).

"**Guaranteed Amount**" means, with respect to a Scheduled Payment Date:

(a) an amount equal to Scheduled Interest Due for Payment on the Guaranteed Bonds on such Scheduled Payment Date; plus

(b) an amount equal to the Scheduled Principal Due for Payment on the Guaranteed Bonds on such Scheduled Payment Date;

but excluding in each case any amounts due in respect of the Guaranteed Bonds:

(i) attributable to any increase in interest margin, penalty or other sum payable by the Issuer for whatever reason;

(ii) attributable to any present or future taxes, duties, withholding, deduction, assessment or other charge (including interest and penalties in respect of such taxes, duties, withholding, deduction, assessment or other charge) of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state (including the United Kingdom), or any political subdivision or governmental or taxing authority therein or thereof;

(iii) attributable to any default interest;

(iv) attributable to any amount relating to prepayment, early redemption, broken-funding indemnities, penalties, premium, "spens", any make-whole amount or similar types of payments payable in respect of the Guaranteed Bonds; or

(v) in respect of which the Financial Guarantor or AGM has made an Accelerated Payment on or prior to such Scheduled Payment Date.

"**Guaranteed Bondholder**" means a holder of Guaranteed Bonds.

"**Guaranteed Bonds**" means the £98,200,000 0.100 per cent. index-linked guaranteed secured bonds due 31 August 2058 constituted by the Bond Trust Deed but excluding any such bonds that are held by or for the account of an Obligor or any Affiliate of an Obligor or Shareholder of any Obligor.

"**HoldCo**" means Uliving@Essex HoldCo Limited, a company incorporated under the laws of England and Wales whose registered office is at 10-11 Charterhouse Square, London, EC1M 6EH (company number 08037507).

"**Insolvency Proceedings**" means the commencement after the date hereof of any bankruptcy, insolvency or similar proceedings by or against the Issuer, or the commencement after the date hereof of any proceedings by or against the Issuer for the winding up or the liquidation of its affairs, or the consent after the date hereof to the appointment of a trustee-in-bankruptcy, conservator, administrator, receiver or liquidator in any bankruptcy, insolvency or similar proceedings relating to the Issuer.

"**Issuer**" means Uliving@Essex Issuerco PLC, a public limited company incorporated with limited liability in England and Wales (company number 10546935).

"**Master Definitions Schedule**" means the master definitions schedule dated on or about the date hereof between, amongst others, the Obligors, the Bond Trustee, the Financial Guarantor and AGM, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such master definitions schedule with the prior written consent of the Financial Guarantor and AGM.

"**Moody's**" means Moody's Investors Service, Inc.

"**Nonpayment by the Issuer**" means, with respect to a Guaranteed Amount at a time when such Guaranteed Amount is Due for Payment, that the funds, if any, remitted to any Agent or the Bond Trustee under the terms of the Guaranteed Bonds or the Bond Trust Deed for payment to Guaranteed Bondholders are insufficient for payment in full of such Guaranteed Amount. In addition to and without limiting the foregoing, "Nonpayment by the Issuer" applies to any portion of any Guaranteed Amount that has become an Avoided Payment.

"**Notice of Demand**" means a notice of demand in the form of the Annex hereto.

"**Obligors**" means the Issuer, HoldCo and ProjectCo, and "**Obligor**" means any of them.

"**Order**" means a final, non-appealable order of a court or other body exercising jurisdiction in an Insolvency Proceeding by or against the Issuer, to the effect that the Bond Trustee, any Agent or any Guaranteed Bondholder is required to return or repay all or any portion of an Avoided Payment.

"**ProjectCo**" means Uliving@Essex Limited, a company incorporated under the laws of England and Wales whose registered office is at 10-11, Charterhouse Square, London, EC1M 6EH (company number 08038090).

"**Rating Agencies**" means Moody's and S&PGRS and such rating agencies as may be substituted for either such rating agency from time to time in accordance with the provisions of the Bond Trust Deed with the prior written consent of the Financial Guarantor and AGM.

"**Receipt**" and "**Received**" shall mean actual delivery to the Financial Guarantor prior to 12:00 noon, London time, on a Business Day; provided, however, that delivery either on a day that is not a Business Day, or after 12:00 noon, London time, on a Business Day, shall be deemed to be "**Received**" on the next succeeding Business Day. For purposes of this definition, "**actual delivery**" to the Financial Guarantor shall mean (i) the delivery of the original Notice of Demand, notice or other applicable documentation to the Financial Guarantor's address for notices in accordance with Clause 11 (*Notices*), or (ii) fax transmission of the original Notice of Demand, notice or other applicable documentation to the Financial Guarantor's fax number for notices in accordance with Clause 11 (*Notices*). If presentation is made by fax transmission, the Bond Trustee (a) shall promptly confirm transmission by telephone to the Financial Guarantor at its telephone number referred to in Clause 11 (*Notices*), and (b) as soon as is reasonably practicable, shall deliver the original Notice of Demand, notice or other applicable documentation to the Financial Guarantor's address for notices in accordance with Clause 11 (*Notices*). If any Notice of Demand, notice or other documentation actually delivered (or attempted to be delivered) under the Financial Guarantee by the Bond Trustee is not in proper form or is not properly completed, executed or delivered, "**Receipt**" by the Financial Guarantor shall be deemed not to have occurred, and the Financial Guarantor shall promptly so advise the Bond Trustee of such deficiency and the nature of the deficiency. In such case, the Bond Trustee may submit an amended or corrected Notice of Demand, notice or other documentation, as the case may be, to the Financial Guarantor.

"**Recovery**" has the meaning set out in Clause 3.2.

"**S&PGRS**" means Standard and Poor's Global Ratings Services.

"**Scheduled Interest**" means, in respect of a Scheduled Payment Date, the amount of scheduled interest on the Guaranteed Bonds then payable in accordance with the original terms of the relevant Conditions, (i) without regard to any amendment or modification of such terms other than any amendment or modification of such terms made in accordance with the provisions of the Bond Trust Deed with the prior written consent of the Financial Guarantor and AGM; and (ii) after giving effect to each amount of principal repaid or prepaid by the Issuer pursuant to the relevant Conditions or otherwise paid following enforcement in accordance with Condition 16 (*Exercise and Enforcement*).

"**Scheduled Payment Date**" has the meaning given to it in the Conditions.

"**Scheduled Principal**" means, in respect of a Scheduled Payment Date, the amount of scheduled principal payable on the Guaranteed Bonds on such Scheduled Payment Date in accordance with Condition 9(a) (*Scheduled Payments*), in accordance with the original terms of the Conditions without regard to any amendment or modification of such terms other than any amendment or modification of such terms made in accordance with the provisions of the Bond Trust Deed with the prior written consent of the Financial Guarantor and AGM, as reduced by each amount of principal repaid or prepaid by the Issuer pursuant to the relevant Conditions or otherwise paid following enforcement in accordance with Condition 16 (*Exercise and Enforcement*).

"**Security Trust and Intercreditor Deed**" means the security trust and intercreditor deed dated on or about the date hereof, between amongst others, the Obligors, the Financial Guarantor, AGM, the Security Trustee and the Bond Trustee, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such security trust and intercreditor deed with the prior written consent of the Financial Guarantor and AGM.

"**Shareholder**" has the meaning given to it in the Master Definitions Schedule.

"**Term of the Financial Guarantee**" means the period from and including the date hereof to and including the earlier of:

(a) the occurrence of the Financial Guarantor Removal Date in accordance with Clause 4.9(*Release of Financial Guarantees*) of the Security Trust and Intercreditor Deed;

(b) the expiration, cancellation or termination of the Financial Guarantee in accordance with Clause 4.9 (*Release of Financial Guarantees*) of the Security Trust and Intercreditor Deed; and

(c) the last to occur of the following:

(i) the date on which all Guaranteed Amounts have been paid under the Guaranteed Bonds;

(ii) the date on which any period during which any Guaranteed Amount could have become, in whole or in part, an Avoided Payment has expired; and

(iii) if the Issuer becomes subject to any Insolvency Proceedings before the occurrence of (i) and (ii) above, the later of (a) the date of the conclusion or dismissal of the Insolvency Proceedings without continuing jurisdiction by the court in such Insolvency Proceedings and (b) if the Bond Trustee or any Guaranteed Bondholder is required to return any payment (or portion thereof) in respect of a Guaranteed Amount that is avoided as a result of such Insolvency Proceedings, the date on which the Financial Guarantor has made all payments required to be made under this Financial Guarantee to or to the order of the Bond Trustee in respect of all such Avoided Payments.

1.2 **Construction**

In this Financial Guarantee, a reference to:

1.2.1 a statutory provision includes a reference to the statutory provision as modified or re-enacted or both from time to time whether before or after the date of this Financial Guarantee and any subordinate legislation made or other thing done under the statutory provision whether before or after the date of this Financial Guarantee;

1.2.2 the singular includes the plural and vice versa (unless the context otherwise requires);

1.2.3 a time of day is a reference to the time in London, unless a contrary indication appears;

1.2.4 each reference to "Clause" or to "Annex", unless the context otherwise requires, is a reference to a clause of or an annex to this Financial Guarantee;

1.2.5 a "**Person**" includes any individual, company, corporation, unincorporated association or body (including a partnership, trust, joint venture or consortium), government, state, agency, organisation or other entity whether or not having separate legal personality; and

1.2.6 a provision of law is a reference to that provision as extended, applied, amended or re-enacted and includes any subordinate legislation.

1.3 **Headings**

The headings in this Financial Guarantee do not affect its construction or interpretation.

2. **Guarantee**

2.1 In consideration of the payment by the Issuer of the Financial Guarantee Fee and subject to the terms of this Financial Guarantee, the Financial Guarantor unconditionally and irrevocably guarantees to the Bond Trustee during the Term of the Financial Guarantee the full and complete payment of the AGE Proportion of:

2.1.1 Guaranteed Amounts that are Due for Payment but are unpaid by reason of Nonpayment by the Issuer, and

2.1.2 Avoided Payments;

provided that any payment by AGM under the AGM Financial Guarantee in respect of the AGE Proportion of any Defaulted Amount shall constitute a discharge of the Financial Guarantor's obligation to make such payment to the Bond Trustee.

2.2 This Financial Guarantee does not guarantee any prepayment or other accelerated payment which at any time may become due in respect of any Guaranteed Amount, other than at the sole option of the Financial Guarantor as specified in Clause 4 (*Acceleration*) of this Financial Guarantee, nor against any risk other than Nonpayment by the Issuer, including failure of the Bond Trustee or any Agent to make any payment due to the Guaranteed Bondholders or any diminution in the market or fair value of the Guaranteed Bonds.

3. **Payments by the Financial Guarantor**

3.1 Following Receipt by the Financial Guarantor of a Notice of Demand in accordance with Clause 8 (*Notice of Demand*) from the Bond Trustee for any Defaulted Amount, the Financial Guarantor will, subject to Clause 7.5, pay the AGE Proportion of the Defaulted Amount to the Bond Trustee by no later than 10.00 a.m., London time, on the later of:

(a) the date such Defaulted Amount becomes Due for Payment; and

(b) the fourth Business Day following the day on which the Financial Guarantor Received such Notice of Demand.

3.2 In the event that any amount shall be received by the Bond Trustee or the Bond Trustee has actual notice that any Guaranteed Bondholder has received any amount in respect of a Defaulted Amount forming the basis of a claim specified in a Notice of Demand submitted hereunder, which amount had not been received by the Bond Trustee, or which the Bond Trustee did not have actual notice had been received by a Guaranteed Bondholder when the Notice of Demand was prepared but which is received by the Bond Trustee or the Bond Trustee has actual notice has been received by such Guaranteed Bondholder prior to the receipt of payment from the Financial Guarantor as contemplated by this Financial Guarantee (each such amount, a "**Recovery**"), the Bond Trustee shall promptly so notify the Financial Guarantor (which notice shall include the amount of any such Recovery). The fact that a Recovery has been received by the Bond Trustee or the Bond Trustee has actual notice that a Recovery has been received by such Guaranteed Bondholder shall be deemed to be incorporated in the applicable Notice of Demand as of the date such Notice of Demand was originally prepared, without the need for any further action by any Person, and the Financial Guarantor shall pay the amount of the claim against the Financial Guarantor specified in paragraph (ii) of the Notice of Demand less the sum of the AGE Proportion of all such Recoveries.

3.3 The Financial Guarantor shall be entitled to elect, in its absolute discretion, to pay part or all of any Defaulted Amount to any such bank account as is specified by the Bond Trustee without the need for the Financial Guarantor to have Received, and irrespective of whether the Financial Guarantor shall have Received, a Notice of Demand therefor. Any such payment shall be considered a payment by the Financial Guarantor under this Financial Guarantee for all purposes. If requested by the Financial Guarantor, the Bond Trustee shall promptly deliver to the Financial Guarantor a properly completed and executed Notice of Demand in respect of any such payment made or to be made by the Financial Guarantor.

3.4 Payments due hereunder in respect of Guaranteed Amounts will be disbursed to or to the order of the Bond Trustee and credited (in immediately available funds) to the bank account (the "**Account**") specified by the Bond Trustee in the applicable Notice of Demand or pursuant to Clause 3.3 or Clause 4.2. Payment in full to the Account shall discharge the obligations of the Financial Guarantor under this Financial Guarantee to the extent of such payment, whether or not such payment is properly applied by or on behalf of the Bond Trustee or any Agent.

3.5 Once payment by or on behalf of the Financial Guarantor of an amount in respect of any Guaranteed Amount (whether on a Scheduled Payment Date or pursuant to Clause 3.3 or on an accelerated basis pursuant to Clause 4.2) has been made to the Account, the Financial Guarantor shall have no further obligations under this Financial Guarantee in respect of such Guaranteed Amount to the extent of such payment.

4. **Acceleration**

4.1 At any time or from time to time following Acceleration, the Financial Guarantor may decide, in its absolute discretion, to make an Accelerated Payment under this Financial Guarantee without the need for the Financial Guarantor to have Received, and irrespective of whether the Financial Guarantor shall have Received, a Notice of Demand.

4.2 The Financial Guarantor shall notify the Bond Trustee in writing of its intention to make an Accelerated Payment and the proposed date of such payment, no later than two Business Days prior to such proposed date of payment. Any such Accelerated Payment shall be considered a payment by the Financial Guarantor under this Financial Guarantee for all purposes. If so requested by the Financial Guarantor at the time the Financial Guarantor gives such written notice, the Bond Trustee shall deliver to the Financial Guarantor and AGM a corresponding Notice of Demand.

5. **Withholding Tax**

All payments by the Financial Guarantor to or to the order of the Bond Trustee under this Financial Guarantee shall be made without withholding or deduction for, or on account of, any taxes, duties, assessments or other governmental charges of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state, or any political subdivision or governmental or taxing authority therein or thereof unless such withholding or deduction is required by law. If any withholding or deduction is so required by law, the Financial Guarantor shall pay such amounts net of such withholding or deduction and shall account to the appropriate tax authority for the amount required to be withheld or deducted. The Financial Guarantor shall not be obliged to pay any amount to or to the order of the Bond Trustee in respect of the amount of such withholding or deduction.

6. **Subrogation**

6.1 The Financial Guarantor will be fully, immediately and automatically subrogated to the Guaranteed Bondholders' and the Bond Trustee's rights to payment of the Guaranteed Amounts, and to any rights relating thereto, to the fullest extent permitted by applicable law to the extent and at the time of any payments made by or on behalf of the Financial Guarantor under this Financial Guarantee, including, for the avoidance of doubt, any Accelerated Payment.

6.2 Any payment made by or on behalf of the Issuer to or for the benefit of the Bond Trustee or any Guaranteed Bondholder in respect of any Guaranteed Amount forming the basis of a claim hereunder (and a corresponding claim under this Financial Guarantee and/or the AGM Financial Guarantee, which claims shall have been paid in full by the Financial Guarantor and AGM respectively) shall be received and held on trust by the recipient for the benefit of the Financial Guarantor and AGM and shall be paid by the recipient over to the Financial Guarantor and AGM *pro rata* in proportion to the respective amounts paid (i) by the Financial Guarantor in respect of a claim made pursuant to this Financial Guarantee, and (ii) by AGM in respect of the related claim made pursuant to the AGM Financial Guarantee.

7. **Waiver of Defences**

7.1 The obligations of the Financial Guarantor under this Financial Guarantee will continue and will not be terminable other than in accordance with Clause 12 (*Termination and Amendment*) of this Financial Guarantee notwithstanding failure to receive payment of the Financial Guarantee Fee or any other amount due in respect of this Financial Guarantee. The Financial Guarantee Fee is not refundable for any reason.

7.2 The Financial Guarantor acknowledges that there is no duty of disclosure by the Bond Trustee under this Financial Guarantee but nonetheless, to the fullest extent permitted by applicable law, hereby waives for the benefit of the Bond Trustee and the Guaranteed Bondholders and agrees not to assert any and all rights (whether by counterclaim, rescission, set-off or otherwise) and any and all equities and defences howsoever arising (including, without limitation, any right, equity or defence based on: (a) any right to require the Bond Trustee or any Guaranteed Bondholder first to proceed against or to enforce any other rights or security against, or to claim payment from, any Person before the Bond Trustee may claim from the Financial Guarantor under this Financial Guarantee; (b) fraud on the part of any Person (including fraud on the part of any agent for the Bond Trustee, but excluding fraud by the Bond Trustee itself); (c) misrepresentation, breach of warranty or non-disclosure of information by any Person; (d) any lack of validity or enforceability of the Guaranteed Bonds or the Bond Trust Deed; (e) any modification or any amendment to the Guaranteed Bonds or the Bond Trust Deed; (f) the granting of any time, indulgence or concession by any Person to the Issuer; (g) any insolvency or similar proceedings in respect of the Issuer or any other Person; (h) any lack of capacity, power or authority or any change in status of the Issuer or any other Person; or (i) the refusal or failure to take up, to hold, to perfect or to enforce by any Person any rights under or in connection with any guarantee, indemnity, security or other document) to the extent such rights, equities and defences may be available to the Financial Guarantor to avoid payment of its obligations under this Financial Guarantee in accordance with the express provisions hereof.

7.3 No warranties are given and nothing in this Financial Guarantee is intended to constitute a warranty or a condition precedent to payment under the Financial Guarantee other than Receipt of a Notice of Demand in accordance with Clause 8 (*Notice of Demand*) of this Financial Guarantee.

7.4 Nothing in this Financial Guarantee shall be construed in any way to limit or otherwise affect the Financial Guarantor's right to pursue recovery or claims (based on contractual or other rights, including to the extent applicable such rights resulting from any Person's fraud, negligence or breach of any agreement to which it is a party) for reimbursement against any Persons for any liabilities, losses, damages, costs and expenses incurred by the Financial Guarantor or to exercise at any time any other remedies that may be available to the Financial Guarantor at law or in equity.

7.5 Nothing in this Financial Guarantee shall be construed to require payment by the Financial Guarantor so long as a Force Majeure Event is continuing, in which event the Financial Guarantor agrees to perform its obligations under this Financial Guarantee promptly following cessation of such Force Majeure Event.

8. **Notice of Demand**

8.1 Subject to Clauses 2.2, 3.3 and 4 (*Acceleration*) of this Financial Guarantee, payments of Guaranteed Amounts (including Avoided Payments) will only be made after presentation of a properly completed Notice of Demand signed by the Bond Trustee and Received by the Financial Guarantor.

8.2 Notices of Demand can only be given by the Bond Trustee in the manner set out in Clause 11 (*Notices*).

8.3 Without limitation to the Financial Guarantor's obligations under Clause 8.5, if any Notice of Demand is not in the proper form or is not properly completed, executed or delivered, the Financial Guarantor will not be deemed to have Received such Notice of Demand.

8.4 Any Notice of Demand in respect of an Avoided Payment will not be deemed properly completed unless it is accompanied by:

8.4.1 a copy of the Order; and

8.4.2 a certificate of the Bond Trustee that the Order has been entered and that, on the basis of legal advice received by the Bond Trustee, the Order is not subject to any stay and specifying (to the extent that the Bond Trustee has actual knowledge sufficient to do so) the Guaranteed Amounts that are Avoided Payments.

8.5 The Financial Guarantor will promptly advise the Bond Trustee if a Notice of Demand is not in the proper form or has not been properly completed, executed or delivered and the Bond Trustee may submit an amended Notice of Demand to the Financial Guarantor.

9. **Fiscal Agent**

9.1 At any time during the Term of the Financial Guarantee, the Financial Guarantor may appoint a fiscal agent (the "**Fiscal Agent**") for purposes of this Financial Guarantee by written notice to the Bond Trustee, specifying the name and notice address of such Fiscal Agent. From and after the date of receipt of such notice by the Bond Trustee:

9.1.1 copies of all notices (including Notices of Demand) and other documents required to be delivered to the Financial Guarantor pursuant to this Financial Guarantee shall be simultaneously delivered to the Fiscal Agent and to the Financial Guarantor; and

9.1.2 all payments required to be made by the Financial Guarantor under this Financial Guarantee may be made directly by the Financial Guarantor or by the Fiscal Agent on behalf of the Financial Guarantor.

9.2 The Fiscal Agent is the agent of the Financial Guarantor only, and the Fiscal Agent shall in no event be liable to the Bond Trustee for any acts of the Fiscal Agent or any failure of the Financial Guarantor to deposit, or cause to be deposited, sufficient funds to make payments due under this Financial Guarantee.

10. **Transfer**

10.1 The rights and obligations of the Financial Guarantor under this Financial Guarantee may be assigned or transferred to, or assumed by, any Affiliate of the Financial Guarantor provided that:

10.1.1 no Financial Guarantor Default has occurred and is continuing at the time of such assignment, transfer or assumption or would occur as a result of such assignment, transfer or assumption;

10.1.2 the Financial Guarantor or such assignee, transferee or party assuming such rights and obligations delivers to the Bond Trustee written confirmation from the Rating Agencies that, at the time of and immediately following any such assignment, transfer or assumption, the financial strength or claims paying ability of such affiliate will be rated at least equal to the financial strength or claims paying ability of the Financial Guarantor at that time; and

10.1.3 the Financial Guarantor or such assignee, transferee or party assuming such rights and obligations thereafter delivers to the Bond Trustee written notice of any such assignment, transfer or assumption.

10.1.4 such transferee assumes the obligations of the Financial Guarantor under this Financial Guarantee and accedes to the relevant Finance Documents to which the Financial Guarantor is party; and

10.1.5 the location of the transferee does not (a) result in any withholding or deduction for any taxes, duties, assessments, or other governmental charges of whatever nature in

respect of any payment by such transferee hereunder, which withholding or deduction is not at the time of the relevant transfer applicable to any such payment by the Financial Guarantor hereunder, and (b) otherwise prevent payment being made in respect of any Guaranteed Amount where payment made by the Financial Guarantor hereunder is not prevented at the time of the relevant transfer.

10.2 The Bond Trustee may not transfer, assign, sub-participate, declare a trust over or otherwise dispose (other than in favour of the Guaranteed Bondholders) of any of its rights under this Financial Guarantee except to a Person as to whom the Financial Guarantor has given its prior written consent. However, if the Bond Trustee transfers or assigns its rights and obligations under the Bond Trust Deed to a new or additional trustee which has been appointed in accordance with the Bond Trust Deed, no such consent shall be required and such new or additional trustee will be able to enforce this Financial Guarantee and references in this Financial Guarantee to "**Bond Trustee**" shall be construed as including such new trustee or such additional trustee, as applicable.

11. **Notices**

11.1 All notices given under this Financial Guarantee shall be in writing (except as otherwise specifically provided herein) and shall be mailed by registered mail or personally delivered or faxed as follows:

To the Financial Guarantor:

Assured Guaranty (Europe) Ltd.
11th Floor
6 Bevis Marks
London, EC3A 7BA

Attention: Managing Director
Re: University of Essex, Financial Guarantee No. 80179-U
Fax: +44 207 562 1901

with a copy to the General Counsel at the above address and fax number. Each Notice of Demand shall be marked to indicate URGENT MATERIAL ENCLOSED.

To the Bond Trustee:

BNY Mellon Corporate Trustee Services Limited
1 Canada Square
London
E145AL

Attention: Trustee Administration Manager / Uliving@EssexIssuerco PLC
Fax: +44 0207 964 2509

If presentation to the Bond Trustee is made by fax transmission, the Financial Guarantor, as soon as is reasonably practicable, shall deliver the original notice or other applicable documentation to the Bond Trustee's address for notices in accordance with this Clause 11 (Notices).

11.2 The Financial Guarantor or the Bond Trustee may designate an additional or different address, or telephone or fax number, by prior written notice. Each notice, presentation, delivery and communication to the Financial Guarantor or the Bond Trustee shall be effective only upon Receipt by the Financial Guarantor or actual receipt by the Bond Trustee, as the case may be.

12. **Termination and Amendment**

12.1 This Financial Guarantee is not cancellable by the Financial Guarantor for any reason, including, without limitation, the failure of the Financial Guarantor to receive payment of any Financial Guarantee Fee due in respect of this Financial Guarantee.

12.2 This Financial Guarantee and the obligations of the Financial Guarantor hereunder shall terminate upon the expiration of the Term of the Financial Guarantee.

12.3 This Financial Guarantee may not be amended, modified or supplemented without the prior written consent of the Bond Trustee.

13. **Miscellaneous**

No waiver of any rights or powers of the Financial Guarantor or the Bond Trustee, or any consent by either of them, shall be valid unless in writing and signed by an authorised officer or agent of the Financial Guarantor or the Bond Trustee, as applicable. The waiver of any right by the Financial Guarantor or the Bond Trustee, or the failure promptly to exercise any such right, shall not be construed as a waiver of any right to exercise the same or any other right at any time thereafter.

14. **Law and Jurisdiction**

14.1 This Financial Guarantee, and any non-contractual obligations arising out of or in connection with it, shall be governed by, and construed in accordance with, the laws of England and Wales.

14.2 With respect to any suit, action or proceedings relating to this Financial Guarantee ("**Proceedings**"), the Financial Guarantor irrevocably submits to the jurisdiction of the English courts and waives any objection which it may have at any time to the laying of venue of any Proceedings brought in any such court, waives any claim that such Proceedings have been brought in an inconvenient forum and further waives the right to object, with respect to such Proceedings that such court does not have any jurisdiction over such party.

15. **Entire Agreement**

This Financial Guarantee constitutes the entire agreement between the Financial Guarantor and the Bond Trustee in relation to the Financial Guarantor's obligation to make payments to the Bond Trustee for the benefit of the Guaranteed Bondholders in respect of the Guaranteed Amounts which become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer, and supersedes any previous agreement between the Financial Guarantor and the Bond Trustee in relation thereto.

16. **Third Party Rights**

No Person other than the Bond Trustee shall have rights under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Financial Guarantee but this shall not affect any such right any Person may have otherwise than by virtue of such Act.

17. **Surrender of Financial Guarantee**

The Bond Trustee shall deliver its original engrossment of this Financial Guarantee to the Financial Guarantor upon expiration of the Term of this Financial Guarantee.

In Witness Whereof, this Financial Guarantee has been executed as a deed and delivered on the date inserted above.

EXECUTED as a DEED for and on behalf of
ASSURED GUARANTY (EUROPE) LTD. by:

Authorised signatory

in the presence of

Signature of Witness:
Name of Witness:
Address:
Occupation:

ANNEX

NOTICE OF DEMAND

Assured Guaranty (Europe) Ltd.
11th Floor
6 Bevis Marks
London, EC3A 7BA

Assured Guaranty Municipal Corp.
1633 Broadway
New York, NY 10019, USA

Attention:

Chief Surveillance Officer

and

General Counsel

The undersigned, BNY Mellon Corporate Trustee Services Limited as Bond Trustee (the "**Bond Trustee**"), hereby certifies to each of Assured Guaranty (Europe) Ltd. ("**AGE**") and Assured Guaranty Municipal Corp. ("**AGM**" and, together with AGE, the "**Financial Guarantors**") with reference to Financial Guarantee Number 80179-U (the "**AGE Financial Guarantee**") and Financial Guarantee Number 51929-N (the "**AGM Financial Guarantee**" and, together with the AGE Financial Guarantee, the "**Financial Guarantees**") that:

(i) [The Guaranteed Amount[s] that [is/are] due and payable on the Scheduled Payment Date falling on [insert applicable payment date] [is/are] [●][insert applicable amount]./The Guaranteed Amount[s] that [was/were] paid, credited, transferred or delivered to or to the order of the Bond Trustee or the Guaranteed Bondholders by or on behalf of the Issuer in accordance with the terms of the Bond Trust Deed and/or the Guaranteed Bonds on [insert applicable payment date] of [●][insert applicable amount] [was/were] recovered from, or was otherwise required to be returned or repaid by, the Bond Trustee or [a/the] Guaranteed Bondholder[s] as a result of Insolvency Proceedings by or against the Issuer on [insert applicable repayment date].]

(ii) [The deficiency with respect to the Guaranteed Amount Due for Payment and unpaid by reason of Nonpayment by the Issuer on the Scheduled Payment Date falling on [insert applicable payment date] is [●][insert applicable amount] (the "**Defaulted Amount**"), the AGE Proportion of such Defaulted Amount is [●] and the AGM Proportion of such Defaulted Amount is [●]]/[The Bond Trustee has been notified by the Account Bank that the deficiency in respect of the Guaranteed Amount[s] which [is/are] Due for Payment on the Scheduled Payment Date falling on [insert applicable payment date] will be [●] [insert applicable amount] (the "**Defaulted Amount**"). The AGE Proportion of such Defaulted Amount is [●] and the AGM Proportion of such Defaulted Amount is [●]].

(iii) The Bond Trustee is making (a) a claim against AGE under the AGE Financial Guarantee for the AGE Proportion of the Defaulted Amount, and (b) a claim against AGM under the AGM Financial Guarantee for the AGM Proportion of the Defaulted Amount, with each such amount to be applied to the payment of the above-described Guaranteed Amount[s].

(iv) To the extent that AGE does not pay the AGE Proportion of any Defaulted Amount when due and payable by AGE in accordance with the terms of the AGE Financial Guarantee, the Bond Trustee is making a claim against AGM under Clause 3.1.2 of the AGM Financial Guarantee for such amount. The Bond Trustee agrees that any payment by AGM of such amount shall discharge AGE from any obligation to make such payment under the AGE Financial Guarantee.

(v) The Bond Trustee agrees that following any payment by the Financial Guarantors made with respect to the Defaulted Amount which is the subject of this Notice of Demand, it (a) will cause such amounts to be applied directly to the payment of the applicable Guaranteed Amount[s] in accordance with Clause 7.9 of the Bond Trust Deed; (b) will ensure that such funds are not applied for any other purpose; and (c) will cause an accurate record of such payment to be maintained with respect to the appropriate Guaranteed Amount(s), the corresponding claim on each Financial Guarantee, and the proceeds of such claim.

(vi) Payments should be made by credit to the following account:

[(insert details of bank account)] (the "**Account**").

Capitalised terms used in this Notice of Demand and not otherwise defined herein shall have the respective meanings ascribed thereto in or pursuant to the applicable Financial Guarantee.

This Notice of Demand may be revoked at any time by written notice of such revocation by the Bond Trustee to each Financial Guarantor, if and only to the extent that moneys are actually received by the Bond Trustee prior to any such revocation from a source other than the Financial Guarantors with respect to the Defaulted Amount set forth herein. The Bond Trustee will withdraw this Notice of Demand, or submit a restated Notice of Demand reducing the amount of the claim hereunder, if the required amount of the Defaulted Amount and accordingly each of the AGE Proportion and the AGM Proportion thereof has been reduced (including reduction to zero) on or prior to the date the Financial Guarantors are required to make payment under the Financial Guarantees.

If the Bond Trustee has received, or the Bond Trustee has actual notice that one or more Guaranteed Bondholders has received, from the Issuer or the Financial Guarantors an amount in excess of a Defaulted Amount, the Bond Trustee shall promptly return to each Financial Guarantor the lesser of (i) such Financial Guarantor's proportionate share in such excess amount (such share being calculated by a fraction equal to the amount of the Defaulted Amount paid by the relevant Financial Guarantor to or to the order of the Bond Trustee divided by the total Defaulted Amount paid by both Financial Guarantors to or to the order of the Bond Trustee) and (ii) the amount of the Defaulted Amount paid by the relevant Financial Guarantor to or to the order of the Bond Trustee and not previously distributed by the Bond Trustee to the Guaranteed Bondholders or to any insolvency official appointed in respect of the Issuer. For the avoidance of doubt the Bond Trustee shall only be required to repay any such amounts to the Financial Guarantors that are in the Bond Trustee's possession and under its control, at the time it becomes aware of the requirement to repay such amounts, and the Bond Trustee shall have no liability to any Person for any amounts received by the Bond Trustee from the Financial Guarantors but distributed by the Bond Trustee in accordance with the preceding sentence.

The Bond Trustee acknowledges that as of the date on which any payment by the relevant Financial Guarantor towards a Defaulted Amount is credited to the Account, the relevant Financial Guarantor shall be deemed fully, immediately and automatically subrogated, to the fullest extent permitted by applicable law, to the rights (including, without limitation, any rights and benefits attached thereto, and any security granted at law, by contract or otherwise) of the Guaranteed Bondholders to payment of the Guaranteed Amounts to the extent and at the time of such payment by the relevant Financial Guarantor towards the Defaulted Amount.

The Bond Trustee hereby (i) assigns to each Financial Guarantor its rights to receive any payment for the account of the Guaranteed Bondholders from the Issuer in respect of the Guaranteed Bonds to the extent of any payments made to (or to the order of) the Bond Trustee by the relevant Financial Guarantor under the applicable Financial Guarantee, including without limitation its right to receive payments of principal and interest on the Guaranteed Bonds (including Recoveries), and (ii) confirms that it has taken or will promptly take all steps reasonably required by, and at the expense of, the Financial Guarantors to effect and perfect such assignments to the Financial Guarantors. The foregoing assignments are in addition to, and not in limitation of, rights of subrogation otherwise available to each Financial Guarantor in respect of such payments. Payments to each Financial Guarantor in respect of the foregoing assignment shall in all cases be subject to and subordinate to the rights of the Bond Trustee to receive all Guaranteed Amounts in respect of the Guaranteed Bonds. The Bond Trustee shall cooperate in all reasonable respects, and at the expense of the Financial Guarantors, with any request by either Financial Guarantor for action necessary to preserve or enforce such Financial Guarantor's rights and remedies, any related security arrangements or otherwise in relation to such subrogation. The

Bond Trustee shall also, at the expense of the Financial Guarantors, deliver any such instruments as may be reasonably requested or required by the Financial Guarantors to effectuate the purpose or provisions of this paragraph.

Any payment made by or on behalf of the Issuer to or for the benefit of the Bond Trustee in respect of any Guaranteed Amount forming the basis of a claim hereunder (which claim shall have been paid in full by the Financial Guarantors) shall be received and held on trust for the benefit of the Financial Guarantors and shall be paid over to each Financial Guarantor *pro rata* in proportion to the respective amounts each Financial Guarantor paid in respect of the Defaulted Amount.

The Bond Trustee hereby agrees that so long as no Financial Guarantor Default shall have occurred and be continuing, each Financial Guarantor may at any time during the continuation of any Insolvency Proceeding by or against the Issuer under any applicable law direct all matters relating thereto, including without limitation, (a) all matters relating to any claim in connection with an Insolvency Proceeding by or against the Issuer seeking the avoidance as a preferential transfer of any payment made with respect to the Guaranteed Bonds (a "**Preference Claim**"), (b) the direction of any appeal of any order relating to any Preference Claim at the expense of the Financial Guarantors and (c) the posting of any surety or performance bond pending any such appeal.

[Pursuant to Clause 8.4 of the Financial Guarantee, the following documents are attached:

- a copy of the Order; and
- a certificate of the Bond Trustee that the Order has been entered and that, on the basis of legal advice received by the Bond Trustee, the Order is not subject to any stay and specifying (to the extent that the Bond Trustee has actual knowledge sufficient to do so), the Guaranteed Amounts that are Avoided Payments.*
- To be inserted if demand relates to Avoided Payments.]

This Notice of Demand, and any non-contractual obligations arising out of or in connection with it, shall be governed by, and construed in accordance with, the laws of England and Wales.

[With respect to any suit, action or proceedings relating to this Notice of Demand ("**Proceedings**"), the Bond Trustee irrevocably submits to the jurisdiction of the English courts and waives any objection which it may have at any time to the laying of venue of any Proceedings brought in any such court, waives any claim that such Proceedings have been brought in an inconvenient forum and further waives the right to object, with respect to such Proceedings that such court does not have any jurisdiction over it.**]

** For use when the Bond Trustee is not incorporated in England and Wales.

No Person, other than each Financial Guarantor, shall have any right under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Notice of Demand but this shall not affect any such right any Person may have otherwise than by virtue of such Act.

In Witness Whereof, the undersigned has executed and delivered this Notice of Demand as a deed on the __ day of _________ of 2__.

EXECUTED as a DEED for and on behalf of
BNY MELLON CORPORATE TRUSTEE
SERVICES LIMITED acting by two of its lawful Attorneys:

Attorney

Attorney

in the presence of

Signature of Witness:
Name of Witness:
Address:
Occupation:

For the Financial Guarantor or
Fiscal Agent Use Only
Wire transfer sent on By:
Confirmation Number:

FORM OF AGM FINANCIAL GUARANTEE

Dated 24 February 2017

ASSURED GUARANTY MUNICIPAL CORP.

FINANCIAL GUARANTEE No. 51929-N

in respect of

£98,200,000 0.100 per cent. Index-Linked Guaranteed Secured Bonds due 31 August 2058

This Financial Guarantee is dated 24 February 2017 and given by Assured Guaranty Municipal Corp. with its principal place of business at 1633 Broadway, New York, NY 10019, USA (the "**Financial Guarantor**") in favour of BNY Mellon Corporate Trustee Services Limited, as trustee for the holders of the Guaranteed Bonds (as defined below) (the "**Bond Trustee**", which expression shall, whenever the context admits, include such Persons for the time being the trustee or trustees of the Bond Trust Deed for the Guaranteed Bondholders).

1. **Interpretation**

1.1 **Definitions**

Any capitalised terms used in this Financial Guarantee and not otherwise defined shall have the meaning given to such terms in the Bond Trust Deed or the Master Definitions Schedule (each as defined below) unless the context otherwise requires. In the event of any inconsistency between the provisions of this Financial Guarantee and the provisions of the Bond Trust Deed and/or the Collateral Deed, this Financial Guarantee shall prevail. For the purposes of this Financial Guarantee, the following terms will have the following meanings:

"**Accelerated Payment**" means, following an Acceleration, any payment in full or in part by the Financial Guarantor or AGE, at the Financial Guarantor's or AGE's absolute option, of all or part of the Scheduled Principal in advance of the final Scheduled Payment Date together with accrued but unpaid Scheduled Interest on such Scheduled Principal to the date of such payment (but excluding any amounts referred to in items (i) to (iv) of the definition of "**Guaranteed Amount**").

"**Acceleration**" means, in relation to the Guaranteed Bonds, the giving of notice by the Bond Trustee to the Issuer that the Guaranteed Bonds are immediately due and repayable pursuant to Condition 11 (*Events of Default*), and **Accelerated** will be construed accordingly.

"**Account**" has the meaning set out in Clause 3.4.

"**Affiliate**" has the meaning given to it in the Master Definitions Schedule.

"**AGE**" has the meaning given to it in the Bond Trust Deed.

"**AGE Financial Guarantee**" means the financial guarantee dated on or about the date hereof, provided by AGE as financial guarantor, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with Clause 12.3 thereof.

"**AGE Proportion**" means the proportion of the Financial Guarantees provided by AGE, which proportion is 8 per cent.

"**Agent**" means The Bank of New York Mellon, acting through its London Branch, as paying agent under the Guaranteed Bonds, and the term Agent shall include any successor to such Agent.

"**AGM Proportion**" means the proportion of the Financial Guarantees provided by the Financial Guarantor, which proportion is 92 per cent.

"**Avoided Payment**" means any amount that is paid, credited, transferred or delivered to or to the order of the Bond Trustee or a Guaranteed Bondholder by or on behalf of the Issuer in accordance with the terms of the Bond Trust Deed and/or the Guaranteed Bonds in respect of any Guaranteed Amount, which amount has been recovered from, or is otherwise required to be returned or repaid by, the Bond Trustee or a Guaranteed Bondholder as a result of Insolvency Proceedings by or against the Issuer.

"**Bond Trust Deed**" means the bond trust deed dated on or about the date hereof between the Issuer, the Bond Trustee, the Financial Guarantor and AGE, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such bond trust deed with the prior written consent of the Financial Guarantor and AGE.

"**Business Day**" means any day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealings in foreign exchange and foreign currency deposits) in London and New York.

"**Collateral Deed**" means the collateral deed dated on or about the Issue Date between the Obligors, the Bond Trustee, the Security Trustee, the Financial Guarantor and AGE, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such collateral deed with the prior written consent of the Financial Guarantor and AGE.

"**Conditions**" means the terms and conditions of the Guaranteed Bonds as set out in Schedule 4 (*Conditions of the Bonds*) of the Bond Trust Deed, and "**Condition**" when used herein means such Condition as set out in Schedule 4 (*Conditions of the Bonds*) of the Bond Trust Deed and referred to herein.

"**Defaulted Amount**" means the portion of a Guaranteed Amount that is Due for Payment and unpaid by reason of Nonpayment by the Issuer, including any portion of any Guaranteed Amount that has become an Avoided Payment.

"**Due for Payment**" means, with respect to:

(a) Scheduled Interest on a Scheduled Payment Date, the amount of Scheduled Interest that is due and payable by the Issuer on such Scheduled Payment Date; and

(b) Scheduled Principal on a Scheduled Payment Date, the amount of Scheduled Principal that is due and payable by the Issuer on such Scheduled Payment Date,

in each case as each such Scheduled Payment Date occurs or would have occurred in accordance with the original terms of the Guaranteed Bonds and without regard to any prepayment, Acceleration or mandatory or optional redemption of the Guaranteed Bonds or any subsequent amendment or modification of the Guaranteed Bonds that has not been consented to in writing by the Financial Guarantor and AGE in accordance with the provisions of the Bond Trust Deed. For the avoidance of doubt, Due for Payment does not refer to any earlier date upon which payment of any Guaranteed Amounts may become due under the Guaranteed Bonds, by reason of prepayment, Acceleration, mandatory or optional redemption or otherwise.

"**Financial Guarantee**" means this Financial Guarantee No. 51929-N, without regard to any amendment, modification or supplement hereto other than any such amendment, modification or supplement made in accordance with Clause 12.3.

"**Financial Guarantees**" means this Financial Guarantee and the AGE Financial Guarantee.

"**Financial Guarantee Fee**" has the meaning given to it in the Financial Guarantee Fee Letter.

"**Financial Guarantee Fee Letter**" means the fee letter dated as of the date of this Financial Guarantee between the Financial Guarantor and the Obligors, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such fee letter with the prior written consent of the Financial Guarantor.

"**Financial Guarantor Default**" has the meaning given to it in the Security Trust and Intercreditor Deed.

"**Fiscal Agent**" has the meaning assigned thereto in Clause 9 (*Fiscal Agent*).

"**Force Majeure Event**" means any unforeseeable event outside the control of the Financial Guarantor that renders the Financial Guarantor's performance under this Financial Guarantee impossible (and not merely impracticable or more onerous).

"**Guaranteed Amount**" means, with respect to a Scheduled Payment Date:

(a) an amount equal to Scheduled Interest Due for Payment on the Guaranteed Bonds on such Scheduled Payment Date; plus

(b) an amount equal to the Scheduled Principal Due for Payment on the Guaranteed Bonds on such Scheduled Payment Date;

but excluding in each case any amounts due in respect of the Guaranteed Bonds:

(i) attributable to any increase in interest margin, penalty or other sum payable by the Issuer for whatever reason;

(ii) attributable to any present or future taxes, duties, withholding, deduction, assessment or other charge (including interest and penalties in respect of such taxes, duties, withholding, deduction, assessment or other charge) of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state (including the United Kingdom), or any political subdivision or governmental or taxing authority therein or thereof;

(iii) attributable to any default interest;

(iv) attributable to any amount relating to prepayment, early redemption, broken-funding indemnities, penalties, premium, "spens", any make-whole amount or similar types of payments payable in respect of the Guaranteed Bonds; or

(v) in respect of which the Financial Guarantor or AGE has made an Accelerated Payment on or prior to such Scheduled Payment Date.

"**Guaranteed Bondholder**" means a holder of Guaranteed Bonds.

"**Guaranteed Bonds**" means the £98,200,000 0.100 per cent. index-linked guaranteed secured bonds due 31 August 2058 constituted by the Bond Trust Deed but excluding any such bonds that are held by or for the account of an Obligor or any Affiliate of an Obligor or Shareholder of any Obligor.

"**HoldCo**" means Uliving@Essex HoldCo Limited, a company incorporated under the laws of England and Wales whose registered office is at 10-11, Charterhouse Square, London, EC1M 6EH (company number 08037507).

"**Insolvency Proceedings**" means the commencement after the date hereof of any bankruptcy, insolvency or similar proceedings by or against the Issuer, or the commencement after the date hereof of any proceedings by or against the Issuer for the winding up or the liquidation of its affairs, or the consent after the date hereof to the appointment of a trustee-in-bankruptcy, conservator, administrator, receiver or liquidator in any bankruptcy, insolvency or similar proceedings relating to the Issuer.

"**Issuer**" means Uliving@Essex Issuerco PLC, a public limited company incorporated with limited liability in England and Wales (company number 10546935).

"**Master Definitions Schedule**" means the master definitions schedule dated on or about the date hereof between, amongst others, the Obligors, the Bond Trustee, the Financial Guarantor and AGE, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such master definitions schedule with the prior written consent of the Financial Guarantor and AGE.

"**Moody's**" means Moody's Investors Service, Inc.

"**Nonpayment by the Issuer**" means, with respect to a Guaranteed Amount at a time when such Guaranteed Amount is Due for Payment, that the funds, if any, remitted to any Agent or the Bond Trustee under the terms of the Guaranteed Bonds or the Bond Trust Deed for payment to Guaranteed Bondholders are insufficient for payment in full of such Guaranteed Amount. In addition to and without limiting the foregoing, "Nonpayment by the Issuer" applies to any portion of any Guaranteed Amount that has become an Avoided Payment.

"**Notice of Demand**" means a notice of demand in the form of the Annex hereto.

"**Obligors**" means the Issuer, HoldCo and ProjectCo, and "**Obligor**" means any of them.

"**Order**" means a final, non-appealable order of a court or other body exercising jurisdiction in an Insolvency Proceeding by or against the Issuer, to the effect that the Bond Trustee, any Agent or any Guaranteed Bondholder is required to return or repay all or any portion of an Avoided Payment.

"**ProjectCo**" means Uliving@Essex Limited, a company incorporated under the laws of England and Wales whose registered office is at 10-11 Charterhouse Square, London, EC1M 6EH (company number 08038090).

"**Rating Agencies**" means Moody's and S&PGRS and such rating agencies as may be substituted for either such rating agency from time to time in accordance with the provisions of the Bond Trust Deed with the prior written consent of the Financial Guarantor and AGE.

"**Receipt**" and "**Received**" shall mean actual delivery to the Financial Guarantor prior to 12:00 noon, London time, on a Business Day; provided, however, that delivery either on a day that is not a Business Day, or after 12:00 noon, London time, on a Business Day, shall be deemed to be "**Received**" on the next succeeding Business Day. For purposes of this definition, "**actual delivery**" to the Financial Guarantor shall mean (i) the delivery of the original Notice of Demand, notice or other applicable documentation to the Financial Guarantor's address for notices in accordance with Clause 11 (Notices), or (ii) fax transmission of the original Notice of Demand, notice or other applicable documentation to the Financial Guarantor's fax number for notices in accordance with Clause 11 (Notices). If presentation is made by fax transmission, the Bond Trustee (a) shall promptly confirm transmission by telephone to the Financial Guarantor at its telephone number referred to in Clause 11 (Notices), and (b) as soon as is reasonably practicable, shall deliver the original Notice of Demand, notice or other applicable documentation to the Financial Guarantor's address for notices in accordance with Clause 11 (Notices). If any Notice of Demand, notice or other documentation actually delivered (or attempted to be delivered) under the Financial Guarantee by the Bond Trustee is not in proper form or is not properly completed, executed or delivered, "**Receipt**" by the Financial Guarantor shall be deemed not to have occurred, and the Financial Guarantor shall promptly so advise the Bond Trustee of such deficiency and the nature of the deficiency. In such case, the Bond Trustee may submit an amended or corrected Notice of Demand, notice or other documentation, as the case may be, to the Financial Guarantor.

"**Recovery**" has the meaning set out in Clause 3.2.

"**S&PGRS**" means Standard and Poor's Global Ratings Services.

"**Scheduled Interest**" means, in respect of a Scheduled Payment Date, the amount of scheduled interest on the Guaranteed Bonds then payable in accordance with the original terms of the relevant Conditions, (i) without regard to any amendment or modification of such terms other than any amendment or modification of such terms made in accordance with the provisions of the Bond Trust Deed with the prior written consent of the Financial Guarantor and AGE; and (ii) after giving effect to each amount of principal repaid or prepaid by the Issuer pursuant to the relevant Conditions or otherwise paid following enforcement in accordance with Condition 16 (*Exercise and Enforcement*).

"**Scheduled Payment Date**" has the meaning given to it in the Conditions.

Scheduled Principal" means, in respect of a Scheduled Payment Date, the amount of scheduled principal payable on the Guaranteed Bonds on such Scheduled Payment Date in accordance with Condition 9(a) (*Scheduled Payments*), in accordance with the original terms of the Conditions without regard to any amendment or modification of such terms other than any amendment or modification of such terms made in accordance with the provisions of the Bond Trust Deed with the prior written consent of the Financial Guarantor and AGE as reduced by each amount of principal repaid or prepaid by the Issuer pursuant to the relevant Conditions or otherwise paid following enforcement in accordance with Condition 16 (*Exercise and Enforcement*).

"**Security Trust and Intercreditor Deed**" means the security trust and intercreditor deed dated on or about the date hereof, between amongst others, the Obligors, the Financial Guarantor, AGE, the Security Trustee and the Bond Trustee, without regard to any amendment, modification or supplement thereto other than any such amendment, modification or supplement made in accordance with the provisions of such security trust and intercreditor deed with the prior written consent of the Financial Guarantor and AGE.

"**Shareholder**" has the meaning given to it in the Master Definitions Schedule.

"**Term of the Financial Guarantee**" means the period from and including the date hereof to and including the earlier of:

(a) the occurrence of the Financial Guarantor Removal Date in accordance with Clause 4.9 (*Release of Financial Guarantees*) of the Security Trust and Intercreditor Deed;

(b) the expiration, cancellation or termination of the Financial Guarantee in accordance with Clause 4.9 (*Release of Financial Guarantees*) of the Security Trust and Intercreditor Deed; and

(c) the last to occur of the following:

(i) the date on which all Guaranteed Amounts have been paid under the Guaranteed Bonds;

(ii) the date on which any period during which any Guaranteed Amount could have become, in whole or in part, an Avoided Payment has expired; and

(iii) if the Issuer becomes subject to any Insolvency Proceedings before the occurrence of (i) and (ii) above, the later of (a) the date of the conclusion or dismissal of the Insolvency Proceedings without continuing jurisdiction by the court in such Insolvency Proceedings and (b) if the Bond Trustee or any Guaranteed Bondholder is required to return any payment (or portion thereof) in respect of a Guaranteed Amount that is avoided as a result of such Insolvency Proceedings, the date on which the Financial Guarantor has made all payments required to be made under this Financial Guarantee to or to the order of the Bond Trustee in respect of all such Avoided Payments.

1.2 **Construction**

In this Financial Guarantee, a reference to:

1.2.1 a statutory provision includes a reference to the statutory provision as modified or re-enacted or both from time to time whether before or after the date of this Financial Guarantee and any subordinate legislation made or other thing done under the statutory provision whether before or after the date of this Financial Guarantee;

1.2.2 the singular includes the plural and vice versa (unless the context otherwise requires);

1.2.3 a time of day is a reference to the time in London, unless a contrary indication appears;

1.2.4 each reference to "Clause" or to "Annex", unless the context otherwise requires, is a reference to a clause of or an annex to this Financial Guarantee;

1.2.5 a "Person" includes any individual, company, corporation, unincorporated association or body (including a partnership, trust, joint venture or consortium), government, state, agency, organisation or other entity whether or not having separate legal personality; and

1.2.6 a provision of law is a reference to that provision as extended, applied, amended or re-enacted and includes any subordinate legislation.

1.3 **Headings**

The headings in this Financial Guarantee do not affect its construction or interpretation.

2. **Guarantee**

2.1 In consideration of the payment by the Issuer of the Financial Guarantee Fee and subject to the terms of this Financial Guarantee, the Financial Guarantor unconditionally and irrevocably

guarantees to the Bond Trustee during the Term of the Financial Guarantee the full and complete payment of:

2.1.1 the AGM Proportion of:

(a) Guaranteed Amounts that are Due for Payment but are unpaid by reason of Nonpayment by the Issuer; and

(b) Avoided Payments; and

2.1.2 the AGE Proportion of:

(a) Guaranteed Amounts that are Due for Payment but are unpaid by reason of Nonpayment by the Issuer to the extent that AGE has not paid such amounts when due and payable by AGE under the terms of the AGE Financial Guarantee, and

(b) Avoided Payments to the extent that AGE has not paid such amounts when due and payable by AGE under the terms of the AGE Financial Guarantee;

Any payment by the Financial Guarantor under this Clause 2.1.2 shall constitute a discharge of AGE's obligation to make such payment under the AGE Financial Guarantee.

2.2 This Financial Guarantee does not guarantee any prepayment or other accelerated payment which at any time may become due in respect of any Guaranteed Amount, other than at the sole option of the Financial Guarantor as specified in Clause 4 (Acceleration) of this Financial Guarantee, nor against any risk other than Nonpayment by the Issuer, including failure of the Bond Trustee or any Agent to make any payment due to the Guaranteed Bondholders or any diminution in the market or fair value of the Guaranteed Bonds.

3. **Payments by the Financial Guarantor**

3.1 Following Receipt by the Financial Guarantor of a Notice of Demand in accordance with Clause 8 (Notice of Demand) from the Bond Trustee for any Defaulted Amount, the Financial Guarantor will, subject to Clause 7.5, pay:

3.1.1 the AGM Proportion of the Defaulted Amount to the Bond Trustee by no later than 10.00 a.m., London time, on the later of:

(a) the date such Defaulted Amount becomes Due for Payment; and

(b) the fourth Business Day following the day on which the Financial Guarantor Received such Notice of Demand; and

3.1.2 if (i) the Bond Trustee has made a claim against AGE under the AGE Financial Guarantee by delivering a Notice of Demand that has been Received (as defined in the AGE Financial Guarantee) by AGE, (ii) such claim has not been paid by AGE in accordance with the terms of the AGE Financial Guarantee, (iii) the AGE Financial Guarantee has not been terminated and (iv) the Financial Guarantor has Received notice from the Bond Trustee that AGE has failed to pay such claim, the AGE Proportion of the Defaulted Amount to the Bond Trustee no later than the Business Day following the day on which such amount was due and payable by AGE in accordance with the terms of the AGE Financial Guarantee.

3.2 In the event that any amount shall be received by the Bond Trustee or the Bond Trustee has actual notice that any Guaranteed Bondholder has received any amount in respect of a Defaulted Amount forming the basis of a claim specified in a Notice of Demand submitted hereunder, which amount had not been received by the Bond Trustee, or which the Bond Trustee did not have actual notice had been received by a Guaranteed Bondholder when the Notice of Demand was prepared but which is received by the Bond Trustee or the Bond Trustee has actual notice has been received by such Guaranteed Bondholder prior to the

receipt of payment from the Financial Guarantor as contemplated by this Financial Guarantee (each such amount, a "**Recovery**"), the Bond Trustee shall promptly so notify the Financial Guarantor (which notice shall include the amount of any such Recovery). The fact that a Recovery has been received by the Bond Trustee or the Bond Trustee has actual notice that a Recovery has been received by such Guaranteed Bondholder shall be deemed to be incorporated in the applicable Notice of Demand as of the date such Notice of Demand was originally prepared, without the need for any further action by any Person, and the Financial Guarantor shall pay the amount of the claim against the Financial Guarantor specified in paragraph (ii) of the Notice of Demand less the sum of the AGM Proportion of all such Recoveries or, in the case of any payment by the Financial Guarantor under Clause 2.1.2, the claim against AGE specified in paragraph (ii) of the Notice of Demand less the sum of the AGE Proportion of all such Recoveries.

3.3 The Financial Guarantor shall be entitled to elect, in its absolute discretion, to pay part or all of any Defaulted Amount to any such bank account as is specified by the Bond Trustee without the need for the Financial Guarantor to have Received, and irrespective of whether the Financial Guarantor shall have Received, a Notice of Demand therefor. Any such payment shall be considered a payment by the Financial Guarantor under this Financial Guarantee for all purposes. If requested by the Financial Guarantor, the Bond Trustee shall promptly deliver to the Financial Guarantor a properly completed and executed Notice of Demand in respect of any such payment made or to be made by the Financial Guarantor.

3.4 Payments due hereunder in respect of Guaranteed Amounts will be disbursed to or to the order of the Bond Trustee and credited (in immediately available funds) to the bank account (the "**Account**") specified by the Bond Trustee in the applicable Notice of Demand or pursuant to Clause 3.3 or Clause 4.2. Payment in full to the Account shall discharge the obligations of the Financial Guarantor under this Financial Guarantee to the extent of such payment, whether or not such payment is properly applied by or on behalf of the Bond Trustee or any Agent.

3.5 Once payment by or on behalf of the Financial Guarantor of an amount in respect of any Guaranteed Amount (whether on a Scheduled Payment Date or pursuant to Clause 3.3 or on an accelerated basis pursuant to Clause 4.2) has been made to the Account, the Financial Guarantor shall have no further obligations under this Financial Guarantee in respect of such Guaranteed Amount to the extent of such payment.

4. **Acceleration**

4.1 At any time or from time to time following Acceleration, the Financial Guarantor may decide, in its absolute discretion, to make an Accelerated Payment under this Financial Guarantee without the need for the Financial Guarantor to have Received, and irrespective of whether the Financial Guarantor shall have Received, a Notice of Demand.

4.2 The Financial Guarantor shall notify the Bond Trustee in writing of its intention to make an Accelerated Payment and the proposed date of such payment, no later than two Business Days prior to such proposed date of payment. Any such Accelerated Payment shall be considered a payment by the Financial Guarantor under this Financial Guarantee for all purposes. If so requested by the Financial Guarantor at the time the Financial Guarantor gives such written notice, the Bond Trustee shall deliver to the Financial Guarantor and AGE a corresponding Notice of Demand.

5. **Withholding Tax**

All payments by the Financial Guarantor to or to the order of the Bond Trustee under this Financial Guarantee shall be made without withholding or deduction for, or on account of, any taxes, duties, assessments or other governmental charges of whatever nature imposed, levied, collected, withheld or assessed by any sovereign state, or any political subdivision or governmental or taxing authority therein or thereof unless such withholding or deduction is required by law. If any withholding or deduction is so required by law, the Financial Guarantor shall pay such amounts net of such withholding or deduction and shall account to the appropriate tax authority for the amount required to be withheld or deducted. The

Financial Guarantor shall not be obliged to pay any amount to or to the order of the Bond Trustee in respect of the amount of such withholding or deduction.

6. **Subrogation**

6.1 The Financial Guarantor will be fully, immediately and automatically subrogated to the Guaranteed Bondholders' and the Bond Trustee's rights to payment of the Guaranteed Amounts, and to any rights relating thereto, to the fullest extent permitted by applicable law to the extent and at the time of any payments made by or on behalf of the Financial Guarantor under this Financial Guarantee, including, for the avoidance of doubt, any Accelerated Payment.

6.2 Any payment made by or on behalf of the Issuer to or for the benefit of the Bond Trustee or any Guaranteed Bondholder in respect of any Guaranteed Amount forming the basis of a claim hereunder (and a corresponding claim under this Financial Guarantee and/or the AGE Financial Guarantee, which claims shall have been paid in full by the Financial Guarantor and AGE respectively) shall be received and held on trust by the recipient for the benefit of the Financial Guarantor and AGE and shall be paid by the recipient over to the Financial Guarantor and AGE *pro rata* in proportion to the respective amounts paid (i) by the Financial Guarantor in respect of a claim made pursuant to this Financial Guarantee, and (ii) by AGE in respect of the related claim made pursuant to the AGE Financial Guarantee.

7. **Waiver of Defences**

7.1 The obligations of the Financial Guarantor under this Financial Guarantee will continue and will not be terminable other than in accordance with Clause 12 (Termination and Amendment) of this Financial Guarantee notwithstanding failure to receive payment of the Financial Guarantee Fee or any other amount due in respect of this Financial Guarantee. The Financial Guarantee Fee is not refundable for any reason.

7.2 The Financial Guarantor acknowledges that there is no duty of disclosure by the Bond Trustee under this Financial Guarantee but nonetheless, to the fullest extent permitted by applicable law, hereby waives for the benefit of the Bond Trustee and the Guaranteed Bondholders and agrees not to assert any and all rights (whether by counterclaim, rescission, set-off or otherwise) and any and all equities and defences howsoever arising (including, without limitation, any right, equity or defence based on: (a) any right to require the Bond Trustee or any Guaranteed Bondholder first to proceed against or to enforce any other rights or security against, or to claim payment from, any Person (except in the case only of the guarantee set out in Clause 2.1.2, to the extent of the conditions set out in Clause 3.1.2) before the Bond Trustee may claim from the Financial Guarantor under this Financial Guarantee; (b) fraud on the part of any Person (including fraud on the part of any agent for the Bond Trustee, but excluding fraud by the Bond Trustee itself); (c) misrepresentation, breach of warranty or non-disclosure of information by any Person; (d) any lack of validity or enforceability of the Guaranteed Bonds or the Bond Trust Deed; (e) any modification or any amendment to the Guaranteed Bonds or the Bond Trust Deed; (f) the granting of any time, indulgence or concession by any Person to the Issuer; (g) any insolvency or similar proceedings in respect of the Issuer or any other Person; (h) any lack of capacity, power or authority or any change in status of the Issuer or any other Person; or (i) the refusal or failure to take up, to hold, to perfect or to enforce by any Person any rights under or in connection with any guarantee (except in the case only of the guarantee set out in Clause 2.1.2, to the extent of the conditions set out in Clause 3.1.2), indemnity, security or other document) to the extent such rights, equities and defences may be available to the Financial Guarantor to avoid payment of its obligations under this Financial Guarantee in accordance with the express provisions hereof.

7.3 No warranties are given and nothing in this Financial Guarantee is intended to constitute a warranty or a condition precedent to payment under the Financial Guarantee other than Receipt of a Notice of Demand in accordance with Clause 8 (Notice of Demand) of this Financial Guarantee and, in the case only of the guarantee set out in Clause 2.1.2, the conditions set out in Clause 3.1.2.

7.4 Nothing in this Financial Guarantee shall be construed in any way to limit or otherwise affect the Financial Guarantor's right to pursue recovery or claims (based on contractual or other rights, including to the extent applicable such rights resulting from any Person's fraud, negligence or breach of any agreement to which it is a party) for reimbursement against any Persons for any liabilities, losses, damages, costs and expenses incurred by the Financial Guarantor or to exercise at any time any other remedies that may be available to the Financial Guarantor at law or in equity.

7.5 Nothing in this Financial Guarantee shall be construed to require payment by the Financial Guarantor so long as a Force Majeure Event is continuing, in which event the Financial Guarantor agrees to perform its obligations under this Financial Guarantee promptly following cessation of such Force Majeure Event.

8. **Notice of Demand**

8.1 Subject to Clauses 2.2, 3.3 and 4 (*Acceleration*) of this Financial Guarantee, payments of Guaranteed Amounts (including Avoided Payments) will only be made after presentation of a properly completed Notice of Demand signed by the Bond Trustee and Received by the Financial Guarantor.

8.2 Notices of Demand can only be given by the Bond Trustee in the manner set out in Clause 11 (Notices).

8.3 Without limitation to the Financial Guarantor's obligations under Clause 8.5, if any Notice of Demand is not in the proper form or is not properly completed, executed or delivered, the Financial Guarantor will not be deemed to have Received such Notice of Demand.

8.4 Any Notice of Demand in respect of an Avoided Payment will not be deemed properly completed unless it is accompanied by:

8.4.1 a copy of the Order; and

8.4.2 a certificate of the Bond Trustee that the Order has been entered and that, on the basis of legal advice received by the Bond Trustee, the Order is not subject to any stay and specifying (to the extent that the Bond Trustee has actual knowledge sufficient to do so) the Guaranteed Amounts that are Avoided Payments.

8.5 The Financial Guarantor will promptly advise the Bond Trustee if a Notice of Demand is not in the proper form or has not been properly completed, executed or delivered and the Bond Trustee may submit an amended Notice of Demand to the Financial Guarantor.

9. **Fiscal Agent**

9.1 At any time during the Term of the Financial Guarantee, the Financial Guarantor may appoint a fiscal agent (the "**Fiscal Agent**") for purposes of this Financial Guarantee by written notice to the Bond Trustee, specifying the name and notice address of such Fiscal Agent. From and after the date of receipt of such notice by the Bond Trustee:

9.1.1 copies of all notices (including Notices of Demand) and other documents required to be delivered to the Financial Guarantor pursuant to this Financial Guarantee shall be simultaneously delivered to the Fiscal Agent and to the Financial Guarantor; and

9.1.2 all payments required to be made by the Financial Guarantor under this Financial Guarantee may be made directly by the Financial Guarantor or by the Fiscal Agent on behalf of the Financial Guarantor.

9.2 The Fiscal Agent is the agent of the Financial Guarantor only, and the Fiscal Agent shall in no event be liable to the Bond Trustee for any acts of the Fiscal Agent or any failure of the Financial Guarantor to deposit, or cause to be deposited, sufficient funds to make payments due under this Financial Guarantee.

10. **Transfer**

10.1 The rights and obligations of the Financial Guarantor under this Financial Guarantee may be assigned or transferred to, or assumed by, any Affiliate of the Financial Guarantor provided that:

10.1.1 no Financial Guarantor Default has occurred and is continuing at the time of such assignment, transfer or assumption or would occur as a result of such assignment, transfer or assumption;

10.1.2 the Financial Guarantor or such assignee, transferee or party assuming such rights and obligations delivers to the Bond Trustee written confirmation from the Rating Agencies that, at the time of and immediately following any such assignment, transfer or assumption, the financial strength or claims paying ability of such affiliate will be rated at least equal to the financial strength or claims paying ability of the Financial Guarantor at that time; and

10.1.3 the Financial Guarantor or such assignee, transferee or party assuming such rights and obligations thereafter delivers to the Bond Trustee written notice of any such assignment, transfer or assumption.

10.1.4 such transferee assumes the obligations of the Financial Guarantor under this Financial Guarantee and accedes to the relevant Finance Documents to which the Financial Guarantor is party; and

10.1.5 the location of the transferee does not (a) result in any withholding or deduction for any taxes, duties, assessments, or other governmental charges of whatever nature in respect of any payment by such transferee hereunder, which withholding or deduction is not at the time of the relevant transfer applicable to any such payment by the Financial Guarantor hereunder, and (b) otherwise prevent payment being made in respect of any Guaranteed Amount where payment made by the Financial Guarantor hereunder is not prevented at the time of the relevant transfer.

10.2 The Bond Trustee may not transfer, assign, sub-participate, declare a trust over or otherwise dispose (other than in favour of the Guaranteed Bondholders) of any of its rights under this Financial Guarantee except to a Person as to whom the Financial Guarantor has given its prior written consent. However, if the Bond Trustee transfers or assigns its rights and obligations under the Bond Trust Deed to a new or additional trustee which has been appointed in accordance with the Bond Trust Deed, no such consent shall be required and such new or additional trustee will be able to enforce this Financial Guarantee and references in this Financial Guarantee to "**Bond Trustee**" shall be construed as including such new trustee or such additional trustee, as applicable.

11. Notices

11.1 All notices given under this Financial Guarantee shall be in writing (except as otherwise specifically provided herein) and shall be mailed by registered mail or personally delivered or faxed as follows:

To the Financial Guarantor:

Assured Guaranty Municipal Corp.
1633 Broadway
New York, NY 10019, USA

Re: University of Essex, Financial Guarantee No. 51929-N
Attention: Chief Surveillance Officer
Telephone: +1 212 974 0100
Fax: +1 212 581 3268

with a copy to the General Counsel at the above address and fax number. Each Notice of Demand shall be marked to indicate URGENT MATERIAL ENCLOSED.

To the Bond Trustee:

BNY Mellon Corporate Trustee Services Limited
1 Canada Square
London
E145AL

Attention: Trustee Administration Manager / Uliving@EssexIssuerco PLC
Fax: +44 0207 964 2509

If presentation to the Bond Trustee is made by fax transmission, the Financial Guarantor as soon as is reasonably practicable, shall deliver the original notice or other applicable documentation to the Bond Trustee's address for notices in accordance with this Clause 11 (*Notices*).

11.2 The Financial Guarantor or the Bond Trustee may designate an additional or different address, or telephone or fax number, by prior written notice. Each notice, presentation, delivery and communication to the Financial Guarantor or the Bond Trustee shall be effective only upon Receipt by the Financial Guarantor or actual receipt by the Bond Trustee, as the case may be.

12. **Termination and Amendment**

12.1 This Financial Guarantee is not cancellable by the Financial Guarantor for any reason, including, without limitation, the failure of the Financial Guarantor to receive payment of any Financial Guarantee Fee due in respect of this Financial Guarantee.

12.2 This Financial Guarantee and the obligations of the Financial Guarantor hereunder shall terminate upon the expiration of the Term of the Financial Guarantee.

12.3 This Financial Guarantee may not be amended, modified or supplemented without the prior written consent of the Bond Trustee.

13. **Miscellaneous**

No waiver of any rights or powers of the Financial Guarantor or the Bond Trustee, or any consent by either of them, shall be valid unless in writing and signed by an authorised officer or agent of the Financial Guarantor or the Bond Trustee, as applicable. The waiver of any right by the Financial Guarantor or the Bond Trustee, or the failure promptly to exercise any such right, shall not be construed as a waiver of any right to exercise the same or any other right at any time thereafter.

14. **Law and Jurisdiction**

14.1 This Financial Guarantee, and any non-contractual obligations arising out of or in connection with it, shall be governed by, and construed in accordance with, the laws of England and Wales.

14.2 With respect to any suit, action or proceedings relating to this Financial Guarantee ("**Proceedings**"), the Financial Guarantor irrevocably submits to the jurisdiction of the English courts and waives any objection which it may have at any time to the laying of venue of any Proceedings brought in any such court, waives any claim that such Proceedings have been brought in an inconvenient forum and further waives the right to object, with respect to such Proceedings that such court does not have any jurisdiction over such party.

15. **Entire Agreement**

This Financial Guarantee constitutes the entire agreement between the Financial Guarantor and the Bond Trustee in relation to the Financial Guarantor's obligation to make payments to the Bond Trustee for the benefit of the Guaranteed Bondholders in respect of the Guaranteed Amounts which become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer, and supersedes any previous agreement between the Financial Guarantor and the Bond Trustee in relation thereto.

16. **Third Party Rights**

No Person other than the Bond Trustee shall have rights under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Financial Guarantee but this shall not affect any such right any Person may have otherwise than by virtue of such Act.

17. **Property/Casualty Insurance Security Fund**

18. **THIS FINANCIAL GUARANTEE IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.**

19. **Surrender of Financial Guarantee**

The Bond Trustee shall deliver its original engrossment of this Financial Guarantee to the Financial Guarantor upon expiration of the Term of this Financial Guarantee.

In Witness Whereof, this Financial Guarantee has been executed as a deed and delivered on the date inserted above.

EXECUTED as a **DEED** for and on behalf of

ASSURED GUARANTY MUNICIPAL CORP. by:

Authorised signatory

in the presence of

Signature of Witness:
Name of Witness:
Address:
Occupation:

ANNEX

NOTICE OF DEMAND

Assured Guaranty (Europe) Ltd.
11th Floor
6 Bevis Marks
London, EC3A 7BA

Assured Guaranty Municipal Corp.
1633 Broadway
New York, NY 10019, USA

Attention:

Chief Surveillance Officer

and

General Counsel

The undersigned, BNY Mellon Corporate Trustee Services Limited as Bond Trustee (the "**Bond Trustee**"), hereby certifies to each of Assured Guaranty (Europe) Ltd. ("**AGE**") and Assured Guaranty Municipal Corp. ("**AGM**" and, together with AGE, the "**Financial Guarantors**") with reference to Financial Guarantee Number 80179-U (the "**AGE Financial Guarantee**") and Financial Guarantee Number 51929-N (the "**AGM Financial Guarantee**" and, together with the AGE Financial Guarantee, the "**Financial Guarantees**") that:

(i) [The Guaranteed Amount[s] that [is/are] due and payable on the Scheduled Payment Date falling on [insert applicable payment date] [is/are] [●][insert applicable amount]./The Guaranteed Amount[s] that [was/were] paid, credited, transferred or delivered to or to the order of the Bond Trustee or the Guaranteed Bondholders by or on behalf of the Issuer in accordance with the terms of the Bond Trust Deed and/or the Guaranteed Bonds on [insert applicable payment date] of [●][insert applicable amount] [was/were] recovered from, or was otherwise required to be returned or repaid by, the Bond Trustee or [a/the] Guaranteed Bondholder[s] as a result of Insolvency Proceedings by or against the Issuer on [insert applicable repayment date].]

(ii) [The deficiency with respect to the Guaranteed Amount Due for Payment and unpaid by reason of Nonpayment by the Issuer on the Scheduled Payment Date falling on [insert applicable payment date] is [●][insert applicable amount] (the "**Defaulted Amount**"), the AGE Proportion of such Defaulted Amount is [●] and the AGM Proportion of such Defaulted Amount is [●]]/[The Bond Trustee has been notified by the Account Bank that the deficiency in respect of the Guaranteed Amount[s] which [is/are] Due for Payment on the Scheduled Payment Date falling on [insert applicable payment date] will be [●] [insert applicable amount] (the "**Defaulted Amount**"). The AGE Proportion of such Defaulted Amount is [●] and the AGM Proportion of such Defaulted Amount is [●]].

(iii) The Bond Trustee is making (a) a claim against AGE under the AGE Financial Guarantee for the AGE Proportion of the Defaulted Amount, and (b) a claim against AGM under the AGM Financial Guarantee for the AGM Proportion of the Defaulted Amount, with each such amount to be applied to the payment of the above-described Guaranteed Amount[s].

(iv) To the extent that AGE does not pay the AGE Proportion of any Defaulted Amount when due and payable by AGE in accordance with the terms of the AGE Financial Guarantee, the Bond Trustee is making a claim against AGM under Clause 3.1.2 of the AGM Financial Guarantee for such amount. The Bond Trustee agrees that any payment by AGM of such amount shall

discharge AGE from any obligation to make such payment under the AGE Financial Guarantee.

(v) The Bond Trustee agrees that following any payment by the Financial Guarantors made with respect to the Defaulted Amount which is the subject of this Notice of Demand, it (a) will cause such amounts to be applied directly to the payment of the applicable Guaranteed Amount[s] in accordance with Clause 7.9 of the Bond Trust Deed; (b) will ensure that such funds are not applied for any other purpose; and (c) will cause an accurate record of such payment to be maintained with respect to the appropriate Guaranteed Amount(s), the corresponding claim on each Financial Guarantee, and the proceeds of such claim.

(vi) Payments should be made by credit to the following account:

[(insert details of bank account)] (the "**Account**").

Capitalised terms used in this Notice of Demand and not otherwise defined herein shall have the respective meanings ascribed thereto in or pursuant to the applicable Financial Guarantee.

This Notice of Demand may be revoked at any time by written notice of such revocation by the Bond Trustee to each Financial Guarantor, if and only to the extent that moneys are actually received by the Bond Trustee prior to any such revocation from a source other than the Financial Guarantors with respect to the Defaulted Amount set forth herein. The Bond Trustee will withdraw this Notice of Demand, or submit a restated Notice of Demand reducing the amount of the claim hereunder, if the required amount of the Defaulted Amount and accordingly each of the AGE Proportion and the AGM Proportion thereof has been reduced (including reduction to zero) on or prior to the date the Financial Guarantors are required to make payment under the Financial Guarantees.

If the Bond Trustee has received, or the Bond Trustee has actual notice that one or more Guaranteed Bondholders has received, from the Issuer or the Financial Guarantors an amount in excess of a Defaulted Amount, the Bond Trustee shall promptly return to each Financial Guarantor the lesser of (i) such Financial Guarantor's proportionate share in such excess amount (such share being calculated by a fraction equal to the amount of the Defaulted Amount paid by the relevant Financial Guarantor to or to the order of the Bond Trustee divided by the total Defaulted Amount paid by both Financial Guarantors to or to the order of the Bond Trustee) and (ii) the amount of the Defaulted Amount paid by the relevant Financial Guarantor to or to the order of the Bond Trustee and not previously distributed by the Bond Trustee to the Guaranteed Bondholders or to any insolvency official appointed in respect of the Issuer. For the avoidance of doubt the Bond Trustee shall only be required to repay any such amounts to the Financial Guarantors that are in the Bond Trustee's possession and under its control, at the time it becomes aware of the requirement to repay such amounts, and the Bond Trustee shall have no liability to any Person for any amounts received by the Bond Trustee from the Financial Guarantors but distributed by the Bond Trustee in accordance with the preceding sentence.

The Bond Trustee acknowledges that as of the date on which any payment by the relevant Financial Guarantor towards a Defaulted Amount is credited to the Account, the relevant Financial Guarantor shall be deemed fully, immediately and automatically subrogated, to the fullest extent permitted by applicable law, to the rights (including, without limitation, any rights and benefits attached thereto, and any security granted at law, by contract or otherwise) of the Guaranteed Bondholders to payment of the Guaranteed Amounts to the extent and at the time of such payment by the relevant Financial Guarantor towards the Defaulted Amount.

The Bond Trustee hereby (i) assigns to each Financial Guarantor its rights to receive any payment for the account of the Guaranteed Bondholders from the Issuer in respect of the Guaranteed Bonds to the extent of any payments made to (or to the order of) the Bond Trustee by the relevant Financial Guarantor under the applicable Financial Guarantee, including without limitation its right to receive payments of principal and interest on the Guaranteed Bonds (including Recoveries), and (ii) confirms that it has taken or will promptly take all steps reasonably required by, and at the expense of, the Financial Guarantors to effect and perfect such assignments to the Financial Guarantors. The foregoing assignments are in addition to, and not in limitation of, rights of subrogation otherwise available to each Financial Guarantor in respect of such payments. Payments to each Financial Guarantor in respect of the foregoing assignment shall in all cases be subject to and subordinate to the rights of the Bond Trustee to receive all Guaranteed Amounts in respect of the Guaranteed Bonds. The Bond Trustee shall

cooperate in all reasonable respects, and at the expense of the Financial Guarantors, with any request by either Financial Guarantor for action necessary to preserve or enforce such Financial Guarantor's rights and remedies, any related security arrangements or otherwise in relation to such subrogation. The Bond Trustee shall also, at the expense of the Financial Guarantors, deliver any such instruments as may be reasonably requested or required by the Financial Guarantors to effectuate the purpose or provisions of this paragraph.

Any payment made by or on behalf of the Issuer to or for the benefit of the Bond Trustee in respect of any Guaranteed Amount forming the basis of a claim hereunder (which claim shall have been paid in full by the Financial Guarantors) shall be received and held on trust for the benefit of the Financial Guarantors and shall be paid over to each Financial Guarantor *pro rata* in proportion to the respective amounts each Financial Guarantor paid in respect of the Defaulted Amount.

The Bond Trustee hereby agrees that so long as no Financial Guarantor Default shall have occurred and be continuing, each Financial Guarantor may at any time during the continuation of any Insolvency Proceeding by or against the Issuer under any applicable law direct all matters relating thereto, including without limitation, (a) all matters relating to any claim in connection with an Insolvency Proceeding by or against the Issuer seeking the avoidance as a preferential transfer of any payment made with respect to the Guaranteed Bonds (a "**Preference Claim**"), (b) the direction of any appeal of any order relating to any Preference Claim at the expense of the Financial Guarantors and (c) the posting of any surety or performance bond pending any such appeal.

[Pursuant to Clause 8.4 of the Financial Guarantee, the following documents are attached:

- a copy of the Order; and
- a certificate of the Bond Trustee that the Order has been entered and that, on the basis of legal advice received by the Bond Trustee, the Order is not subject to any stay and specifying (to the extent that the Bond Trustee has actual knowledge sufficient to do so), the Guaranteed Amounts that are Avoided Payments.*
- To be inserted if demand relates to Avoided Payments.]

This Notice of Demand, and any non-contractual obligations arising out of or in connection with it, shall be governed by, and construed in accordance with, the laws of England and Wales.

[With respect to any suit, action or proceedings relating to this Notice of Demand ("**Proceedings**"), the Bond Trustee irrevocably submits to the jurisdiction of the English courts and waives any objection which it may have at any time to the laying of venue of any Proceedings brought in any such court, waives any claim that such Proceedings have been brought in an inconvenient forum and further waives the right to object, with respect to such Proceedings that such court does not have any jurisdiction over it.**]

** For use when the Bond Trustee is not incorporated in England and Wales.

No Person, other than each Financial Guarantor, shall have any right under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Notice of Demand but this shall not affect any such right any Person may have otherwise than by virtue of such Act.

In Witness Whereof, the undersigned has executed and delivered this Notice of Demand as a deed on the __ day of _________ of 2__.

EXECUTED as a DEED for and on behalf of
BNY MELLON CORPORATE TRUSTEE SERVICES LIMITED

acting by two of its lawful Attorneys:

Attorney

Attorney

in the presence of

Signature of Witness:
Name of Witness:
Address:
Occupation:

For the Financial Guarantor or
Fiscal Agent Use Only
Wire transfer sent on By:
Confirmation Number:

DESCRIPTION OF THE FINANCIAL GUARANTORS

The information appearing in this section has been prepared by the Financial Guarantors and has not been independently verified by the Issuer or the Manager. Neither the Issuer nor the Manager assumes any responsibility for the accuracy, completeness or applicability of such information; except the Issuer assumes responsibility for the accurate reproduction herein of such information provided by the Financial Guarantors and confirms that such information has been accurately reproduced and that as far as the Issuer is aware and is able to ascertain from information published by the Financial Guarantors no facts have been omitted which would render the reproduced information inaccurate or misleading.

The information in this section contains statements regarding projections and expectations of the Financial Guarantors. These statements can be identified by the fact that they do not relate strictly to historical or current facts and relate to future operations or financial performance. All of the Financial Guarantors' forward looking statements in this Prospectus are based on current expectations and the current economic environment and may vary materially from what is stated herein if the performance of the related transactions is positively or negatively affected by economic, fiscal and financial market variability or for other reasons related to such transactions.

1. Assured Guaranty (Europe) Ltd.

1.1 General

Assured Guaranty (Europe) Ltd. ("**AGE**") is a direct wholly-owned subsidiary of Assured Guaranty Municipal Corp. ("**AGM**" and together with AGE, "**Assured Guaranty**"), an insurance company organised under the laws of the State of New York, U.S.A. AGM is an indirect wholly-owned subsidiary of Assured Guaranty Ltd. ("**AGL**"), a Bermuda based holding company that, through its operating subsidiaries, provides credit protection products to the public finance, infrastructure and structured finance markets. AGL's shares are publicly listed on the New York Stock Exchange under the symbol "AGO". AGL applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guarantee insurance that protects holders of debt instruments and other monetary obligations from defaults in scheduled payments due on an obligation, including scheduled principal or interest payments. AGL's operating subsidiaries market their credit protection products directly to issuers and underwriters of public finance, infrastructure and structured finance securities. as well as to investors in such obligations. AGL's operating subsidiaries guarantee debt obligations issued principally in the United States and the United Kingdom. They also guarantee obligations issued in other countries and regions, including Australia and Western Europe.

AGE was incorporated with limited liability in England on 8 June 1990 pursuant to the Companies Acts 1985 and 1989 with registered number 02510099. AGE was authorised from 29 April 1994, originally by the UK Department of Trade and Industry and subsequently by the UK Financial Services Authority (the "**FSA**"), to carry out and effect "credit", "suretyship" and "miscellaneous financial loss" insurance business in the United Kingdom (firm reference number 202896). From 1 April 2013, AGE is authorised by the Prudential Regulation Authority (the "**PRA**") and regulated by the PRA and the Financial Conduct Authority (the "**FCA**"). These permissions are sufficient for AGE to provide financial guarantees in the UK. In addition, pursuant to the EC third non-life insurance directive (No. 92/49/EEC), AGE is able to provide financial guarantees in twenty European countries, subject to certain conditions.

AGE's registered office is located at 11th Floor, 6 Bevis Marks, London EC3A 7BA, United Kingdom, Telephone: +44 (0)207 562 1900. AGE has no subsidiaries. AGE's legal and commercial name is Assured Guaranty (Europe) Ltd.

AGE is dependent on AGM in that AGM supports AGE through certain contractual arrangements (see "*Material Contracts*" below).

1.2 Ratings

Standard and Poor's Global Ratings Services ("**S&PGRS**") has assigned to AGE financial strength and financial enhancement ratings of "AA" (stable outlook) and Moody's Investors Service, Inc., ("**Moody's**") has assigned to AGE an insurance financial strength rating of "A2" (stable outlook).

On 27 July 2016, S&PGRS affirmed the AA (stable) financial strength and financial enhancement ratings of AGE. On 8 August 2016, Moody's affirmed the A2 (stable outlook) insurance financial strength rating of AGE.

AGE 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. AGE can give no assurance as to any further ratings action that either rating agency may take.

Each rating of AGE should be evaluated independently. An explanation of the significance of the above ratings may be obtained from the applicable rating agency. The above ratings are not recommendations to buy, sell or hold any bond or other security, and such ratings are subject to revision or withdrawal at any time by the Rating Agencies, including withdrawal initiated at the request of AGE in its sole discretion. In addition, the rating agencies may at any time change AGE's ratings outlooks or place AGE's ratings on a watch list for possible downgrade. Any downward revision or withdrawal of any of the above ratings, the assignment of a negative outlook to such ratings or the placement of such ratings on a negative watch list may have an adverse effect on the market price of any bond or other security guaranteed by AGE.

AGE only guarantees scheduled principal and scheduled interest payments payable by the issuer of bonds or other securities guaranteed by AGE on the date(s) when such amounts were initially scheduled to become due and payable (subject to and in accordance with the terms of the relevant financial guarantee), and does not guarantee the market price or liquidity of the bonds or other securities it insures, nor does it guarantee that the ratings on such bonds or other securities will not be revised or withdrawn.

1.3 **Overview of AGE's Business**

AGE provides financial guarantees in the United Kingdom and other European countries for public finance, structured finance and other project and infrastructure finance transactions.

Financial guarantees generally guarantee to the holder of the guaranteed obligation the timely payment of principal of and interest on such obligation in accordance with such obligation's original payment schedule. Accordingly, in the case of a default on the guaranteed obligation, payments under the financial guarantee may not be accelerated without AGE's consent.

Financial guarantees on public infrastructure finance transactions are typically issued in connection with transactions in which the bonds or other securities being issued are secured by or payable from cashflows coming either from a government or quasi-governmental entity or from users of the relevant asset (e.g., passengers on a light rail system or drivers on a toll road). Projects financed under the UK government's Public Private Partnership based model typically involve the construction of an asset (e.g., hospital, school, court buildings) and its ongoing management and maintenance for an agreed duration in return for which a performance-based fee is paid by the relevant public sector body; this fee is used to pay interest on and amortise the debt that is guaranteed by the relevant financial guarantor.

Financial guarantees on structured finance or asset-backed obligations are typically issued in connection with transactions in which the bonds or other securities being issued are secured by or payable from a specific pool of assets having an ascertainable cash flow or market value and held by a special purpose issuing entity.

New business written by AGE is guaranteed using a co-guarantee structure pursuant to which AGE co-guarantees municipal and infrastructure transactions with AGM and structured finance transactions with its affiliate Assured Guaranty Corp. ("**AGC**"). As described elsewhere in this Prospectus with respect to the Bonds and below under *Material Contracts*, AGE covers a proportionate share of the total exposure (expected to be between 3 and 10 per cent.), and AGM (or AGC for structured finance transactions) guarantees the remaining exposure under the transaction (subject to compliance with European Economic Area (the "**EEA**") licensing requirements). In its financial guarantee, AGM (or AGC for structured finance transactions) also will provide a second-to-pay guarantee to cover AGE's share of the total exposure.

1.4 **Information**

Copies of the annual financial statements filed with the Registrar of Companies in the United Kingdom are available upon request to AGE at its registered office.

1.5 **Recent Developments**

Since 31 December 2015, the date as at which its latest audited accounts were prepared, AGE has continued to conduct its financial guarantee business in the United Kingdom and the other European countries into which it is passported to provide financial guarantees.

There are no governmental, legal or arbitration proceedings (pending or threatened) of which AGE is aware during the previous 12 months which may have, or have had in the recent past, significant effects on AGE's financial position or profitability.

1.6 **Directors of AGE**

The following is a list of the members of the board of directors of AGE by name and function and sets forth any principal activities of such members outside of AGE:

Name	Function	Principal Activities Outside of AGE
Robert Bailenson	Executive	Chief Financial Officer, Assured Guaranty Ltd.
Charles Barrington	Non-Executive	Non-executive director of other U.K. companies, charitable organisations and trusts
Dominic Frederico	Executive	Chief Executive Officer and President, Assured Guaranty Ltd.
Simon Leathes (Chairman)	Non-Executive	Director of Assurance Guaranty Ltd., non-executive director of other financial institutions, U.K. companies, charitable organisations and trusts
James Michener	Executive	General Counsel and Secretary, Assured Guaranty Ltd.
Dominic Nathan	Executive	None
Nick Proud	Executive	None

The business address of Messrs. Nathan and Proud and of Messrs. Barrington and Leathes, in their capacity as non-executive directors, is 11th Floor, 6 Bevis Marks, London EC3A 7BA, United Kingdom. The business address of Mr. Bailenson is 1633 Broadway, New York, New York 10019, United States of America. The business address of Messrs. Frederico and Michener is 30 Woodbourne Avenue, Hamilton, Bermuda HM 08.

As at the date of this Prospectus, the above-mentioned board members of AGE do not have potential conflicts of interests between any duties to AGE and their private interests or other duties that are material to the Bonds.

1.7 **Insurance Regulation**

AGE is authorised by the PRA and regulated by the PRA for prudential regulation and by the FCA for conduct of business, in the conduct of its financial guarantee business in the United Kingdom.

The PRA has a general regulatory objective to promote the safety and soundness of the firms which it regulates, thereby supporting the stability of the UK financial system and a specific insurance objective to contribute to securing an appropriate degree of protection for those who are or may become policyholders. The PRA applies new threshold conditions (Threshold Conditions), which insurers must meet, and against which the PRA will assess them on a continuous basis. These conditions include that (a) an insurer, which is incorporated in the United Kingdom, should have its head office (and registered office, if different) in the United Kingdom; (b) an insurer's business must be conducted in a prudent manner — in particular that the insurer maintains appropriate financial and non-financial resources; (c) the insurer must be fit and proper, including that the individuals managing its business have adequate skills and experience; and (d) the insurer must be capable of being effectively supervised by reference to a number of matters including whether it is a member of a group which might prevent the PRA's effective supervision and the complexity of its business and products.

Solvency

Under the European Union's Solvency II Directive (Directive 2009/138/EC), as amended, including by the Omnibus II Directive together with implementing laws, rules and regulations (collectively, "**Solvency II**"), which took effect from 1 January 2016 as implemented in the United Kingdom, AGE is subject to certain limits and requirements, including the maintenance of a minimum solvency capital requirement (which depends on the type and amount of insurance business a company writes and the other risks to which it is exposed) and the establishment of technical provisions including loss and unearned premium reserves. Failure to maintain capital at least equal to the capital requirements under Solvency II is one of the grounds on which the wide powers of intervention conferred upon the PRA may be exercised.

Among other things, Solvency II introduced a revised risk-based prudential regime which includes the following features: (1) assets and liabilities are generally to be valued at their market value; (2) the amount of required economic capital is intended to ensure, with a probability of 99.5 per cent., that regulated insurance firms are able to meet their obligations to policyholders and beneficiaries over the following 12 months; and (3) reinsurance recoveries are treated as a separate asset (rather than being netted off the underlying insurance liabilities). AGE calculates its solvency capital requirements under Solvency II using the Standard Formula. Prior to the implementation of Solvency II, AGE was required to calculate its capital adequacy in accordance with a "benchmarker" capital adequacy model originally devised by the Financial Services Authority (the predecessor prudential regulator to the PRA). AGE was not required to maintain an increased amount of capital under Solvency II. Another feature of Solvency II (and indeed under the predecessor regulatory regime) insurers and reinsurers that are part of a group of insurance/reinsurance companies are required to calculate a group solvency capital requirement at the level of the EEA parent company. The PRA is responsible under Solvency II for the group supervision of the Assured group of companies and accordingly, AGE, would ordinarily be required to perform and submit to the PRA a group capital adequacy return in respect of its ultimate insurance parent. AGE does not have an EEA insurance parent and so does not need to comply with this requirement. However, it would ordinarily be required to provide the PRA with a report showing the calculation of the group capital requirement and the available capital resources of the whole of the Assured group of companies applying Solvency II principles. AGE has obtained a waiver from this particular requirement and obtained the agreement of the PRA to apply "other methods". These other methods include the requirement that AGE provides the PRA with copies of various financial reports the Assured group submits to the New York Department of Financial Services ("**NYSDFS**") and gives prior notice of certain intra-group transactions, including the payment of dividends, capital extractions and intra group reinsurance involving any company in the group that is headquartered in the EEA to or in with other members of the Assured group of companies. If the reports submitted to the PRA raise concerns, the PRA may take regulatory action.

Financial Services Compensation Scheme

The beneficiaries of AGE's Financial Guarantee are not protected by the Financial Services Compensation Scheme.

1.8 Financial Information

The audited accounts of AGE for the years ended 31 December 2015 and 31 December 2014 prepared in accordance with UK GAAP are included at Appendix 1 and Appendix 2 hereto. There has been no

material adverse change in the prospects of AGE since 31 December 2015 (being the date to which AGE's most recent audited financial statements have been prepared). There has been no significant change in the financial or trading position of AGE since 31 December 2015 (being the date to which AGE's most recent audited financial statements have been prepared).

1.9 Auditors

AGE's auditors are PricewaterhouseCoopers LLP ("**PwC**"), 7 More London Riverside, London SE1 2RT. PwC is a member of the Institute of Chartered Accountants in England and Wales.

PwC's report on the audited accounts of AGE for the years ended 31 December 2014 and 31 December 2015 is included with such accounts, which are included at Appendix 1 and Appendix 2 hereto, respectively.

1.10 Material Contracts

Except as discussed below, AGE has not entered into contracts outside the ordinary course of business that could result in AGE being under an obligation or entitlement that is material to AGE's ability to meet its obligations to the Bond Trustee under its Financial Guarantee.

AGM currently provides support to AGE through a second amended and restated quota share and stop loss reinsurance agreement (the "**Reinsurance Agreement**") and a second amended and restated net worth maintenance agreement (the "**Net Worth Agreement**" and together with the Reinsurance Agreement, the "**Assured Guaranty Agreements**"), which were first implemented in 1994. For transactions closed prior to 2011, AGE typically guarantees all of the guaranteed obligations directly and AGM, under the quota share cover of the Reinsurance Agreement, reinsures approximately 92 per cent. of AGE's retention after cessions to other reinsurers. In addition, AGM posts collateral for AGE's benefit securing AGM's quota share reinsurance obligations in respect of such pre-2011 business. In 2011, AGE implemented a co-guarantee structure pursuant to which (i) AGE directly guarantees a portion of the guaranteed obligations in an amount equal to what would have been AGE's *pro rata* retention percentage under the quota share cover; and (ii) AGM directly guarantees the balance of the guaranteed obligations and also provides a second-to-pay guarantee for AGE's portion of the guaranteed obligations.

The Reinsurance Agreement also provides an excess of loss cover under which AGM will pay AGE quarterly the amount (if any) by which AGE's incurred losses, calculated in accordance with UK GAAP as reported by AGE in its financial returns filed with the PRA, and AGE's paid losses and loss adjustment expenses, in both cases net of all other performing reinsurance (including the reinsurance provided by AGM under the quota share cover of the Reinsurance Agreement), exceeds an amount equal to (a) AGE's capital resources under UK law minus 110 per cent. of the greatest of the amounts as may be required by the PRA as a condition for maintaining AGE's authorisation to carry on a financial guarantee business in the UK. AGE may terminate the Reinsurance Agreement upon the occurrence of any of the following events: (i) AGM's ratings by Moody's fall below "Aa3" or its ratings by S&PGRS fall below "AA-" (and AGM fails to restore such rating(s) within a prescribed period of time); and (ii) AGM's insolvency, failure to maintain the minimum capital required under AGM's domiciliary jurisdiction, filing a petition in bankruptcy, going into liquidation or rehabilitation or having a receiver appointed.

The quota share and excess of loss covers each exclude transactions guaranteed by AGE on or after July 1, 2009 that are not municipal, utility, project finance or infrastructure risks or similar types of risks.

Under the Net Worth Agreement, AGM is obligated to cause AGE to maintain capital resources equal to 110 per cent. of the greatest of the amounts as may be required by the PRA as a condition for maintaining its authorisation to carry on a financial guarantee business in the U.K., provided that contributions (a) do not exceed 35 per cent. of AGM's policyholders' surplus as determined by the laws of the State of New York, and (b) are in compliance with a provision of the New York Insurance Law requiring notice to or approval by the NYSDFS for transactions between affiliates that exceed certain thresholds. The Net Worth Agreement clarifies that any amounts due thereunder will take into account all amounts paid or reasonably expected to be paid under the Reinsurance Agreement. The Net Worth Agreement also includes termination provisions substantially similar to those in the Reinsurance

Agreement. AGM has never been required to make any contributions to AGE's capital under the current Net Worth Agreement or its prior net worth maintenance agreements.

On the basis of the support provided by the Assured Guaranty Agreements, AGE has the same ratings as AGM. Holders of the Bonds should note that AGE's ability to perform its obligations under its Financial Guarantee and to maintain its current rating substantially depends on the ability of AGM to perform its obligations under the Assured Guaranty Agreements.

The holders of the Bonds should note that the "Assured Guaranty Agreements" are entered into for the benefit of AGE and are not, and should not be regarded as, guarantees by AGM of the payment of any indebtedness, liability or obligations of the Issuer or AGE, including the Bonds or the Financial Guarantee. The Assured Guaranty Agreements are not guarantees for the benefit of the holders of the Bonds. Neither the Bond Trustee nor holders of the Bonds have any recourse to AGM in respect of the Assured Guaranty Agreements.

Payment of Guaranteed Amounts that are Due for Payment on the Bonds and unpaid by reason of Nonpayment by the Issuer will be guaranteed by the Financial Guarantors pursuant to the Financial Guarantees but will not be additionally covered by the Assured Guaranty Agreements.

2. Assured Guaranty Municipal Corp.

2.1 General

AGM is an insurance company organised under the laws of the State of New York, U.S.A. AGM is an indirect wholly-owned subsidiary of AGL, a Bermuda based holding company that, through its operating subsidiaries, provides credit protection products to the public finance, infrastructure and structured finance markets. AGL's shares are publicly listed on the New York Stock Exchange under the symbol "AGO". AGL applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guaranty insurance that protects holders of debt instruments and other monetary obligations from defaults in scheduled payments due on such obligations, including scheduled principal or interest. AGL's operating subsidiaries market their credit protection products directly to issuers and underwriters of public finance, infrastructure and structured finance securities. as well as to investors in such obligations. AGL's operating subsidiaries guarantee debt obligations principally in the United States and the United Kingdom. They also guarantee obligations in other countries and regions, including, Western Europe and Australia.

AGM was organised in the State of New York, U.S.A. as an insurance company on 16 March 1984 and commenced operations in 1985.

AGM maintains its principal executive offices at 1633 Broadway, New York, New York 10019, U.S.A. The telephone number of AGM is +1 212 974 0100. AGM's legal and commercial name is Assured Guaranty Municipal Corp.

2.2 Ratings

S&PGRS has assigned to AGM financial strength and financial enhancement ratings of "AA" (stable outlook); Kroll Bond Rating Agency ("**KBRA**") has assigned to AGM an insurance financial strength rating of "AA+" (stable outlook); and Moody's has assigned to AGM an insurance financial strength rating of "A2" (stable).

On 27 July, 2016, S&PGRS affirmed the "AA" (stable) financial strength and financial enhancement ratings of AGM. On 14 December, 2016, KBRA affirmed the "AA+" (stable outlook) insurance financial strength rating of AGM. On 8 August 2016, Moody's affirmed the "A2" (stable outlook) insurance financial strength rating of AGM.

AGM 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. AGM can give no assurance as to any further ratings action that any rating agency may take.

Each rating of AGM should be evaluated independently. An explanation of the significance of the above ratings may be obtained from the applicable rating agency. The above ratings are not recommendations to buy, sell or hold any bond or other security, and such ratings are subject to

revision or withdrawal at any time by the Rating Agencies, including withdrawal initiated at the request of AGM in its sole discretion. In addition, the rating agencies may at any time change AGM's ratings outlooks or place AGM's ratings on a watch list for possible downgrade. Any downward revision or withdrawal of any of the above ratings, the assignment of a negative outlook to such ratings or the placement of such ratings on a negative watch list may have an adverse effect on the market price of any bond or other security guaranteed by AGM. AGM only guarantees scheduled principal and scheduled interest payments payable by the issuer of bonds or other securities guaranteed by AGM on the date(s) when such amounts were initially scheduled to become due and payable (subject to and in accordance with the terms of the relevant financial guarantee), and does not guarantee the market price or liquidity of the bonds or other securities it insures, nor does it guarantee that the ratings on such bonds or other securities will not be revised or withdrawn.

2.3 **Overview of AGM's business**

AGM provides financial guarantees to issuers both within and outside the U.S.A. In Europe, it provides co-insurance on public finance and other project and infrastructure finance transactions with AGE (see "*Description of the Financial Guarantors - Assured Guaranty (Europe) Ltd. – Overview of AGE's Business*" above). Since mid-2008, AGM has only provided insurance that protects against principal and interest payment defaults on debt obligations in the U.S. public finance and global infrastructure market. Previously, AGM also offered insurance and reinsurance in the global structured finance market. Like AGE, AGM's financial guarantees generally guarantee to the holder of the guaranteed obligation the timely payment of principal of and interest on such obligation in accordance with such obligation's original payment schedule. Accordingly, in the case of a default on the guaranteed obligation, payments under the financial guarantee may not be accelerated without AGM's consent.

Municipal obligations and municipal bonds include taxable and tax-exempt bonds, notes and other evidences of indebtedness issued by states, political subdivisions (cities, counties, towns and villages), water, sewer and other utility districts, higher educational institutions, hospitals, transportation and housing authorities and other similar agencies. Municipal obligations are supported by the taxing authority of the issuer or the issuer's or underlying obligor's ability to collect fees or assessments for certain projects or public services. References herein to "municipal bonds" and "municipal obligations" are to debt obligations of states and other political subdivisions in the U.S.A.

2.4 **Information**

The quarterly and annual statements filed by AGM in the U.S.A. are available in the "Investor Information" section of Assured Guaranty's website at assuredguaranty.com.

2.5 **Recent Developments**

On 19 December 2016, AGM repurchased 125 shares of its common stock from its parent for $300 million pursuant to the approval described under "Stock Redemption Plan" under "Note 10 – Insurance Company Regulatory Requirements" to its unaudited financial statements found in Appendix 5. On 31 January 2017, it was announced that the Restructuring Support Agreement with the Puerto Rico Electric Power Authority, which is described under "Exposure to Puerto Rico" under "Note 3 – Outstanding Exposure" to its unaudited financial statements found in Appendix 5, has been extended through March 31, 2017.

Since 31 December 2015, the date as at which its latest audited financial statements were prepared, AGM has continued to conduct its financial guarantee business in the U.S.A. and the other states and countries in which it is permitted to provide financial guarantees.

There are no governmental, legal or arbitration proceedings (pending or threatened) of which AGM is aware during the 12 months preceding the date of this Prospectus which may have, or have had in the recent past, significant effects on AGM's financial position or profitability other than as set forth in (a) AGM's audited financial statements as of 31 December 2015 and (b) AGM's unaudited financial statements as of 30 September 2016.

2.6 **Directors of AGM**

The following is a list of the members of the board of directors of AGM by name and function and sets forth any principal activities of such members outside of AGM:

Name	***Function***	***Principal Activities Outside of AGM***
Howard W. Albert	Executive	Chief Risk Officer, Assured Guaranty Ltd.
Robert A. Bailenson	Executive	Chief Financial Officer, Assured Guaranty Ltd.
Russell B. Brewer II	Executive	Chief Surveillance Officer, Assured Guaranty Ltd.
Ling Chow	Executive	U.S. General Counsel of AGC and Municipal Assurance Corp. ("MAC")
Stephen Donnarumma	Executive	Chief Credit Officer of AGC and MAC.
Dominic Frederico (Chairman)	Executive	Chief Executive Officer and President, Assured Guaranty Ltd.
James M. Michener	Executive	General Counsel and Secretary, Assured Guaranty Ltd.
Donald H. Paston	Executive	Treasurer of AGC and MAC
Benjamin Rosenblum	Executive	Chief Actuary of AGC and MAC
Bruce E. Stern	Executive	Executive Officer of AGC and MAC

The business address of Messrs. Albert, Bailenson, Brewer, Donnarumma, Paston, Rosenblum and Stern and of Ms. Chow is 1633 Broadway, New York, New York 10019, U.S.A. The business address of Messrs. Frederico and Michener is 30 Woodbourne Avenue, Hamilton, Bermuda HM 08.

As at the date of this Prospectus, the above-mentioned board members of AGM do not have potential conflicts of interests between any duties to AGM and their private interests or other duties that are material to the Bonds.

2.7 **Insurance Regulation**

AGM is licensed to do business as an insurance company in all fifty states of the United States, the District of Columbia, Guam, Puerto Rico and the U.S. Virgin Islands. It is subject to the insurance laws and regulations of the State of New York, its state of incorporation, which has a comprehensive financial guarantee insurance law, and the insurance laws and regulations of other jurisdictions in which it is licensed to transact business. These laws and regulations, as well as the level of supervisory authority that may be exercised by the various insurance departments, vary by jurisdiction, but generally require insurance companies to maintain minimum standards of business conduct and solvency, meet certain financial tests, including single risk limits and minimum policyholders' surplus

and reserve levels, file certain reports with regulatory authorities, including information concerning their capital structure, ownership and financial condition, and require prior approval of certain changes in control of domestic insurance companies and their direct and indirect parents and the payment of certain dividends and distributions. In addition, these laws and regulations require approval of certain intercorporate transfers of assets and certain transactions between insurance companies and their direct and indirect parents and affiliates, and generally require that all such transactions have terms no less favourable than terms that would result from transactions between parties negotiating at arm's length.

U.S. State insurance laws and regulations (as well as the rating agencies) impose minimum capital requirements on financial guarantee insurance companies, limiting the aggregate amount of insurance which may be written and the maximum size of any single risk exposure which may be assumed. Such companies can use reinsurance to diversify risk, increase underwriting capacity, reduce additional capital needs, stabilise shareholder returns and strengthen financial ratios.

AGM is a party to various reinsurance treaties and facultative reinsurance agreements with various third party, unaffiliated reinsurers and its affiliates, Assured Guaranty Re Ltd. ("**AGR**") and AGC. These treaties and agreements cover AGM's outstanding book of municipal bond and structured and international finance business, except that they generally do not apply to outstanding business that AGM has written since 2008. AGM entered into such treaties and agreements in order to reduce its large risks, to manage its portfolio of insurance by bond type and geographic distribution, and/or to obtain additional capacity for frequent municipal bond issuers. Under such agreements, portions of AGM's interests and liabilities have been ceded on an issue-by-issue basis and AGM has received ceding commissions from the reinsurers to defray its underwriting expenses.

AGM also has a quota share treaty with AGR, which provides for AGR to share a percentage of premiums and losses with AGM. This treaty applies to business written by AGM after 2008, including current business. AGM is also a party to an excess of loss reinsurance arrangement with certain 3rd party, unaffiliated reinsurers, which provides reinsurance for losses on a substantial portion of AGM's net book of U.S. municipal finance business outstanding as of 30 September 2015. This reinsurance facility excludes credits that were rated non-investment grade as of 31 December 2015 by Moody's or S&PGRS or internally by AGM. The reinsurance attaches when AGM's net losses (and those of its affiliates AGC and MAC in respect of credits also covered by the facility) exceed $1.25 billion in the aggregate. The facility covers a portion of the next $400 million of losses, with the third party reinsurers assuming $360 million of the $400 million of losses and AGM, AGC and MAC jointly retaining the remaining $40 million.

As a primary insurer, AGM is required to honour its obligations to its policyholders whether or not its reinsurers perform their obligations under the various reinsurance agreements with AGM detailed above.

AGM is required to file quarterly and annual statutory financial statements in the United States of America, and is subject to single and aggregate risk limits and other statutory restrictions concerning the types and quality of investments and the filing and use of policy forms and premium rates. In addition, AGM's accounts and operations are subject to periodic examination by the NYSDFS and its market conduct is subject to review by other state insurance regulatory authorities.

The beneficiaries of AGM's Financial Guarantee are not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the Insurance Law of the State of New York, U.S.A.

AGM is not authorised or regulated by the PRA or the FCA in the United Kingdom.

2.8 **Financial Information**

The consolidated balance sheets of AGM as of 31 December 2014 and 31 December 2015 and the related consolidated statements of operations and comprehensive income, of shareholder's equity and of cash flows for each of the two years in the period ended 31 December 2015, prepared in accordance with U.S. GAAP are included at Appendix 3 and 4 hereto.

The consolidated balance sheets of AGM as of 30 September 2016 and the related consolidated statements of operations (unaudited) and comprehensive income (unaudited) for the three and nine months ended 30 September 2016, of shareholder's equity (unaudited) for the nine months ended 30

September 2016 and of cash flows (unaudited) for the nine months ended 30 September 2015 and 30 September 2016, prepared in accordance with U.S. GAAP, are included at Appendix 5 hereto.

Other than as may be described in its unaudited financial statements for the period ended 30 September 2016 and under "*Description of the Financial Guarantors – Assured Guaranty Municipal Corp. – Recent Developments*" above, there has been no material adverse change in the prospects of AGM since 31 December 2015 (being the date to which AGM's most recent audited financial statements have been prepared). Other than as may be described in its unaudited financial statements for the period ended 30 September 2016 and under "*Description of the Financial Guarantors – Assured Guaranty Municipal Corp. – Recent Developments*" above, there has been no significant change in the financial or trading position of AGM since 30 September 2016 (being the date to which AGM's most recent unaudited financial statements have been prepared).

2.9 **Auditors**

AGM's auditors are PricewaterhouseCoopers LLP ("**PwC U.S.** "), 300 Madison Avenue, New York, New York 10017 U.S.A. PwC U.S. is a member of the American Institute of Certified Public Accountants.

PwC-U.S.'s report on the audited financial statements of AGM for the years ended 31 December 2015 and 31 December 2014 is included with such accounts, which are included at Appendix 3 and 4 hereto.

2.10 **Material Contracts**

AGM has not entered into contracts outside the ordinary course of business that could result in AGM being under an obligation or entitlement that is material to AGM's ability to meet its obligations to the Bond Trustee under its Financial Guarantee. See "*Description of the Financial Guarantors – Assured Guaranty (Europe) Ltd. – Material Contracts*" above.

DESCRIPTION OF THE ISSUER, HOLDCO AND PROJECTCO

The following is a summary Description of the Issuer, HoldCo and ProjectCo and should be read in conjunction with the rest of the Prospectus.

1. **The Issuer**

Uliving@Essex Issuerco PLC (the "Issuer") was incorporated in England on 4 January 2017 under the Companies Act 2006 as a public limited liability company with number 10546935 and obtained its certificate to commence business and borrow under section 761 of the Companies Act 2006 on 4 January 2017.

The Issuer has not, since its date of incorporation, carried on any business or activities other than those incidental to its registration and the financing, and other matters described or contemplated in this Prospectus. The Issuer has been incorporated as a special purpose company for the purpose of issuing the Bonds. The registered office of Issuer is 10-11 Charterhouse Square, London, United Kingdom, EC1M 6EH (telephone number 020 7250 7333). The Issuer has not published any audited financial accounts since its incorporation.

As at the date of this Prospectus, the Issuer is a wholly owned subsidiary of Holdco and its issued share capital is £50,000 divided into 50,000 ordinary shares of £1 each of which 50,000 ordinary shares have been issued.

The rights of the shareholders in the Issuer are contained in the articles of association of the Issuer and the Issuer will be managed by its directors in accordance with those articles and with the provisions of English Law.

Directors	**Function**	**Address**	**Principal Activities**
Mark Fowkes	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Commercial Director – Equitix Limited
Peter Sheldrake	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Portfolio Manager – Equitix Limited
Matthew Rickards	Director	No.1 Centro Place, Pride Park, Derby, DE24 8RF, United Kingdom	Group Accountant, Derwent Housing Association Limited
Samantha Veal	Director	No.1 Centro Place, Pride Park, Derby, DE24 8RF, United Kingdom	Development Director, Derwent Housing Association Limited

There are no actual or potential conflicts of interest between the duties to the Issuer of the persons listed above and their private interests or duties.

2. **ProjectCo**

Uliving@Essex Limited ("**ProjectCo**") was incorporated in England on 19 April 2012 under the Companies Act 2006 as a private limited company with registered number 08038090. The registered office of ProjectCo is at 10-11, Charterhouse Square, London, EC1M 6EH (telephone number 020 7250 7333).

ProjectCo has not, since its date of incorporation, carried on any business or activities other than those incidental to its registration, the original financing of the Project, the refinancing of the Project and other matters described or contemplated in this Prospectus and the Project Documents (See "*Summary*

of the Project Documents" below). ProjectCo is a special purpose company established to enter into the documentation to which it is expressed to be a party.

Copies of the annual report and financial statements of ProjectCo for the year ended 31 December 2015, as filed with the Registrar of Companies in the United Kingdom, are attached at Appendix 6 hereto and include the independent auditors' report to the shareholders of ProjectCo.

ProjectCo is wholly owned by HoldCo. The authorised share capital of ProjectCo is £15,000 divided into 15,000 Ordinary Shares of £1 each of which 15,000 Ordinary Shares have been issued. All shares issued are fully paid.

Directors	Function	Address	Principal Activities
Mark Fowkes	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Commercial Director – Equitix Limited
Peter Sheldrake	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Portfolio Manager – Equitix Limited
Matthew Rickards	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Group Accountant, Derwent Housing Association Limited
Samantha Veal	Director	Derwent Living, 1 Centro Place, Pride Park, Derby, United Kingdom, DE24 8RF	Development Director, Derwent Housing Association Limited

ProjectCo is not aware of any potential conflicts of interest between the duties to ProjectCo of the persons listed above and their private interests and or other duties.

3. **Hold Co**

Uliving@Essex Holdco Limited ("**HoldCo**") was incorporated in England on 19 April 2012 under the Companies Act 2006 as a private limited company with registered number 08037507. The registered office of HoldCo is at 10-11, Charterhouse Square, London, EC1M 6EH (telephone number 020 7250 7333).

HoldCo has not, since its date of incorporation, carried on any business or activities other than those incidental to its registration, the original financing of the Project, the refinancing of the Project and other matters described or contemplated in this Prospectus and the Project Documents (See "*Summary of the Project Documents*" below). HoldCo is a special purpose company established to enter into the documentation to which it is expressed to be a party.

Copies of the annual report and financial statements of HoldCo for the year ended 31 December 2015, as filed with the Registrar of Companies in the United Kingdom, are attached at Appendix 6 hereto and include the independent auditors' report to the shareholders of HoldCo.

Equitix Education owns 85% of HoldCo and Centro 15%. The authorised share capital of HoldCo is £15,000 divided into: 1,500 A Ordinary Shares of £1 each of which 1,500 A Ordinary Shares have been issued to Equitix Education; 2,250 B Ordinary Shares of £1 each of which 2,250 B Ordinary Shares have been issued to Centro; and 11,250 C Ordinary Shares of £1 each of which 11,250 C Ordinary Shares have been issued to Equitix Education. All shares issued are fully paid.

Directors	Function	Address	Principal Activities
Mark Fowkes	Director	Welken House, 10-11	Commercial Director –

		Charterhouse Square, London, EC1M 6EH	Equitix Limited
Peter Sheldrake	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Portfolio Manager – Equitix Limited
Matthew Rickards	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Group Accountant, Derwent Housing Association Limited
Samantha Veal	Director	Welken House, 10-11 Charterhouse Square, London, EC1M 6EH	Development Director, Derwent Housing Association Limited

HoldCo is not aware of any potential conflicts of interest between the duties to HoldCo of the persons listed above and their private interests and or other duties.

DESCRIPTION OF THE SHAREHOLDERS

The following is a summary Description of the Shareholders and should be read in conjunction with the rest of the Prospectus.

1. **Equitix Education 2 Limited**

The principal activity of Equitix Education 2 Limited (**"Equitix Education"**) relates to investment in long-term contracts with local authorities and universities in the UK to develop education related projects.

The ultimate parent of Equitix Education is a wholly owned subsidiary of Equitix Capital Eurobond 2 Limited, which is incorporated in England and Wales with company number 7449938 whose registered office is at Welken House, 10-11 Charterhouse Square, London EC1M 6EH and which was incorporated on 24 November 2010.

The most recent published audited accounts of Equitix Education show that its profit before tax from ordinary activities for the year ended 31 December 2015 was £11.326m. Its net assets as at 31 December 2015 were £12.954m.

2. **Centro Place Investments Limited**

The principal activity of Centro Place Investments Limited ("**Centro**") relates to accommodation, facilities management and investments operating within the student and facilities management sectors.

Centro is a wholly owned subsidiary of Derwent Housing Association Limited, which is incorporated in England and Wales with company number 18127 R whose registered office is at 80 Cheapside, London, EC2V 6EE and which was incorporated on 22nd May 1964.

The most recent published audited accounts of Centro show that its profit before tax from ordinary activities for the year ended 31 December 2015 was £86k. Its net assets as at 31 December 2015 were £2.472m.

SUMMARY OF THE PROJECT DOCUMENTS

The ability of the Bond Trustee to make a claim under the Financial Guarantees is not subject to the terms of the Project Documents.

1. The Project Agreement

1.1 General

This section describes the principal terms of the Project Agreement. It is not exhaustive, but focuses on issues of particular interest to prospective Bondholders.

1.2 Parties and Term

(a) Parties

The parties to the Project Agreement are the University and ProjectCo.

(b) Term

The Project Agreement came into force on 7 August 2012. The Project Agreement will expire at the end of the 50th consecutive Contract Year following the last Service Commencement Date (30 January 2014), being 31 August 2063, unless terminated earlier in accordance with its terms.

(c) Headleases and Underleases

The structure of the property interests in the Project is described in the section entitled "*Real Estate Documents – Project Leases*" below.

(d) Change in Control

The Project Agreement does not contain a restriction on changes in control.

1.3 Construction Defects and Associated Unavailability

(a) For twelve months after the practical completion of each section, the Building Contractor was liable to rectify any construction defects at the Meadows site. Thereafter, the Building Contractor is liable for a period of up to twelve years following practical completion of the Meadows development (after which ProjectCo takes the risk associated with latent defects).

(b) In the event of any unavailability of a room at the Meadows due to a construction defect, the FM Service Contractor is responsible for procuring alternative accommodation. Following twelve years after practical completion of the Meadows development, ProjectCo takes the risk associated with latent defects.

1.4 The Site

(a) Meadows Site Risks – Ground Conditions

ProjectCo bears substantially all risks relating to the Meadows site. This includes site conditions and the presence of contamination. ProjectCo is deemed to have inspected the construction site, its surrounding areas, and all relevant buildings and accommodation.

These risks were passed to the Building Contractor under the Building Contract in relation to the construction period.

(b) Planning and Other Consents

Detailed planning consent for the Project was obtained. ProjectCo passed its obligations to comply with such planning consent to the Building Contractor and to the FM Service Contractor as relevant.

(c) Contract Risks – Title Conditions

The Headleases are granted subject to the title conditions and reserved rights as disclosed to ProjectCo, and the FM Service Contractor is obliged to carry out its obligations subject to such conditions and reservations.

Certificates of title were produced at the Original Financial Close Date.

1.5 **Commercial Unit**

The commercial unit at the Meadows site, forming part (the ground floor) of block M5, is not sublet back to the University and is leased to Compass UK Limited. The permitted uses for the commercial unit within block M5 are as a small retail unit, launderette, plant room and student common room or outside the Initial Period, such other use as may be permitted under planning law whether or not specifically the subject of a planning permission.

ProjectCo may sub-let the commercial unit within block M5 provided that it serves notice and declaration of the proposed sub-let on the Landlord and the sub-lessor enters into direct covenants with the Landlord in respect of the rent and other underlease obligations.

The current sub-lease with Compass UK Limited is due to be terminated with effect from the summer of 2017.

Any income received from a sub-let arrangement for the commercial unit is retained by ProjectCo, but no revenue is included in the financial model.

1.6 **Services**

(a) Overview

ProjectCo commenced provision of the services from each relevant Service Commencement Date, being the date of the Meadows Underlease Completion (which occurred on 30 January 2014) and the Quays Underlease Completion (which occurred on 8 July 2013), as appropriate.

The services to be provided or procured by ProjectCo generally include planned and reactive maintenance, the renewal and replacement of fixtures and fittings, together with major plant and machinery lifecycle replacement of the premises (the "**Services**") . These obligations are passed down to the FM Service Contractor.

The FM Service Contractor performs all of the services required under the Project Agreement, including the provision of lifecycle works. The risk associated with the adequacy of the lifecycle fund is held by the FM Service Contractor.

ProjectCo jointly employs the Employees with the FM Service Contractor. The FM Service Contractor indemnifies ProjectCo against all costs, expenses and liabilities arising out of the joint employment provisions (including in respect to VAT). The "**Employees**" are those employees of the University who transferred to ProjectCo and the FM Provider and/or any sub-contractor pursuant to the Transfer of Undertakings (Protection of Employment) Regulation 2006 on the Quays Commencement Date (which occurred on 8 July 2013).

ProjectCo has the right to inspect the Accommodation at reasonable times, and the FM Service Contractor is obliged to permit such inspections on the giving of reasonable notice.

(b) Payment

The FM Service Contractor estimates the cost of performing the Services (the "**FM Fee**"). ProjectCo makes regular monthly payments in arrear to the FM Service Contractor, subject to certain adjustments. The FM Service Contractor bears the risk of any inadequacy of the FM Fee. Certain employment costs are paid in addition to the cost of performing the Services. The "**Total FM Sum**" is the aggregate of the FM Fee and the employment costs.

(c) Maximum Liability

The liabilities of the FM Service Contractor arising under the FM Service Contract are, with certain exclusions, limited to an agreed annual cap of an amount equal to 100% of the Total FM Sum in that contract year, and a cap on termination of: an amount equal to 200% of the Total FM Sum in the contract year or termination or expiry; and in relation to a lifecycle shortfall, £5,000,000 (indexed) provided that this shall be limited to the actual lifecycle shortfall at the time of termination or expiry. Limitations do not apply in certain circumstances, including:

(i) any liability of the FM Service Contractor arising out of any fraud, fraudulent misrepresentation, repudiatory breach, abandonment, wilful misconduct or wilful default of the FM Service Contractor or any FM Service Contractor Related Party;

(ii) any liability of the FM Service Contractor to the extent it recovers such liability under any insurances and/or in respect of any deductibles or excesses relating to claims made by the FM Service Contractor;

(iii) any claims brought against ProjectCo by third parties (save for the University, Senior Lender, the Sponsors and the Building Contractor), any losses recovered by the FM Service Contractor from a third party, where such claim or recovery is brought in connection with a failure of the FM Service Contractor;

(iv) any liability under the Transferring Employees provisions;

(v) any payment of default interest on any sum to be paid by the FM Service Contractor;

(vi) costs awarded in favour of ProjectCo against the FM Service Contractor by the Courts or an adjudicator.

1.7 **University Step-in**

In certain circumstances the University is entitled to take action in relation to the Services (including the lifecycle works). These circumstances are where:

(i) there is a serious risk to the health or safety of persons or property or to the environment; and/or

(ii) to discharge a statutory duty; and/or

(iii) because an emergency has arisen.

During the period in which the University is taking the required action and ProjectCo is prevented from providing any part of the Services, ProjectCo is relieved of its obligation to provide the relevant part of the Service. Where the required action results from a ProjectCo breach, ProjectCo shall pay the University's reasonable costs and expenses.

"**Services**" includes all the services which ProjectCo is required to provide under the Project Agreement.

No Service Default Points (see below *Performance Monitoring and Service Default – Service Default Points*) can be allocated to ProjectCo in respect of that part of the Services that is subject to the required action for the period of the required action.

The University step-in position is passed down to the FM Service Contractor, and ProjectCo also has its own step-in right under the FM Service Contract.

1.8 **Payment**

The University makes payments to ProjectCo in the form of Rent under each of the Underleases. Rent is paid in four equal instalments on 31 October, 31 January, 30 April and 31 July in each contract year. "**Rent**" is comprised of:

(i) One pound;

(ii) The Annual Rental Amount;

(iii) Less the Annual University Retention;

(iv) Less the sum due from ProjectCo to the University by way of service charge under the Headlease.

The "**Annual Rental Amount**" under the Underleases is comprised of the Aggregate Base Rent less 4% of that Aggregate Base Rent which is retained by the University. The "**Aggregate Base Rent**" is the annual rent for each type of room which is calculated by multiplying the revised Forecast Base Rent (calculated in accordance with the methodology in the Project Agreement) by the relevant letting period.

The "**Annual University Retention**" is calculated pursuant to the Project Agreement and is dependent on the circumstances applying in the relevant contract year, as follows:

(i) if the "Actual Net Rental Income" (being the sum received under the underleases for the relevant contract year is equal to or less than the Rental Floor then the Annual University Retention will be zero:

(ii) if the Actual Net Rental Income for the relevant Contract Year is more than the Rental Floor but less than the Modelled Rental Income then the Annual University Retention shall be the amount calculated in accordance with the following formula:

Annual University Retention
= Actual Net Rental Income — Rental Floor

(iii) subject to the Gainshare if the Actual Net Rental Income for the relevant Contract Year is equal to or exceeds the Modelled Rental Income then the Annual University Retention shall be an amount calculated in accordance with the following formula:

Annual University Retention = Modelled Rental Income — Rental Floor

"**Modelled Rental Income**" and "**Rental Floor**" are figures stated in the Project Agreement.

The "**Gainshare**" occurs where the IRR calculated by reference to the actual equity subscriptions, subordinated loan notes and distribution cash flows up to and including the relevant date. Where the IRR is above 14%. then ProjectCo is to pay the University 50% of any distributions to be made pursuant to the Facilities Agreement. This will exclude amounts available for distribution due to the Refinancing.

1.9 **Rent Setting**

Rents are set annually in accordance with the procedure in the Project Agreement. The "**Forecast Base Rent**" is calculated by indexing the Actual Base Rent for each type of room for the previous contract year. Indexation is subject to a cap of 6 per cent. and a floor of 0 per cent. annually. In the year 2016/17 the inflation factor includes a Z factor of 0.0075; and in 2017/18, 2018/19, 2019/2020, 2020/2021 the inflation factor includes a Z factor of 0.005.

The "**Total Rent**" is calculated by aggregating the Forecast Base Rents and adding adjustments to reflect changes in insurance costs, utilities consumption, any compulsory or voluntary changes and any increase in the cost of the FM provision where the University has required replacement of the FM Service Contractor due to service failures in accordance with the Project Agreement.

The "**Actual Base Rent**" is the weekly rent chargeable to each qualifying person, and is set at ProjectCo's discretion, provided that:

(i) The Actual; Base Rent chargeable for each room type is not less than for the previous year (except where the ADSCR is equal to or less than 1.15:1.00, then Actual Base Rents can be reduced to address occupancy levels);

(ii) The aggregate of the "**Annual Base Rents**" (being the Actual Base Rent multiplied by the letting period) for all student bedrooms in the accommodation intended to be let to an applicant ("**Rooms**") does not exceed the Total Rent; and

(iii) The aggregate increase in Total Rent for that year will be applied on a pro rata basis to the Actual Base Rent of each type of room.

In the fifth contract year, and every five years thereafter, the Actual Base Rents will be adjusted following ProjectCo exercising its option to prepare a Market Review Report. The "**Market Review Report** " will cover:

(i) the current mix of rooms and Actual Base Rents payable, and level of services provided;

(ii) sample room mix and rent levels for students at comparator universities;

(iii) levels of occupancy achieved since the last review date;

(iv) any proposals for changes in the letting period;

(v) levels of nominations by the University over the previous five years.

The University may give comments on the Market Review Report, and ProjectCo may set increased rents so that: rents can be increased in line with the comparator universities; the Actual Base Rents shall take account of the requirements of a reasonable investor to ProjectCo (including requirements as to anticipated internal rate of return); and demand for rooms is not adversely affected.

The University is restricted from setting rent levels in particular parts of its own accommodation at less than a specified percentage of the relevant University Base Rent. The University Base Rent is set out in the Project Agreement, and subject to indexation annually.

1.10 **Marketing, Allocation and Reservation of Rooms**

(a) Reservation Rights

The University is entitled to reserve up to 100% of the available rooms for the following Contract Year by issuing a "**Reservation Notice**", although the University is not obliged to reserve any or all of the rooms. When issuing the Reservation Notice, the University is required to provide the following information:

(i) the projected number of first year students allocated to come to the University;

(ii) the projected number of returning students to the University;

(iii) the projected number of overseas students;

(iv) the projected number of post graduates; and

(v) any other information that ProjectCo reasonably requires.

Where the reservation concerns rooms in a Townhouse or a Cluster, the University is obliged to reserve all rooms in such Townhouse or Cluster.

Where the University does not reserve all of the available rooms, then ProjectCo may market the remaining rooms as it chooses. Such rooms may be taken by "**Qualifying Persons** (full-time students at the University of other higher education institution, or part time students so long as it would not breach the planning consent) or "Alternative Occupiers" (those permitted by the planning consent who are not Qualifying Persons).

(b) Allocation of Rooms

The University must ensure that applicants for student accommodation offered by the University are able to identify their preferred choice of accommodation as part of the application process.

The University is required to allocate an available room to the first 655 Qualifying Persons requiring accommodation on a 50 week basis in any contract year.

(c) Licences

The University tenants occupy their rooms pursuant to a licence in an agreed form which is attached to the Project Agreement.

(d) Deposits

The terms of the student licence do not require deposits from occupiers.

(e) Student Damage

ProjectCo bears the risk of physical damage to the Accommodation and other property of ProjectCo. The University has certain obligations to pursue students for recovery where this damage is caused by students. Where the University has not recovered costs from students. ProjectCo will seek to recover from insurances. The University will reimburse ProjectCo for any insurance deductible and/or any repair costs not recovered by ProjectCo from insurances.

1.11 **Restrictive Covenant**

The University is restricted from disposing of certain land during the Term unless it obtains a covenant from the disposee that it will not be used for student accommodation.

The University is also prohibited from:

(i) entering into a "**Relevant Arrangement**" being an arrangement concerning the construction or other provision of residential accommodation to be let to Qualifying Persons (as defined in "Project Agreement - Marketing, Allocation and Reservation of Rooms" above) including any phase 2 arrangement without ProjectCo consent;

(ii) supporting the creation of student accommodation within the specified area; and/or

(iii) advertising or marketing student accommodation (other than the University’s accommodation on the Colchester Campus and ProjectCo’s Accommodation) within a specified area.

The University may however enter into a Relevant Arrangement without ProjectCo consent where the Applicable Tests have been met. The "**Applicable Tests**" are:

(i) for each of the previous 3 consecutive Contract Years the ratio of Total Student Demand to Total Bed Supply has not fallen below 1.5:1;

(ii) the number of proposed further rooms is such that when occupied the ratio of Total Student Demand to Total Bed Supply will not fall below 1.5:1 for the following 3 contract years assessed on the basis of the University’s projected student number returns to HEFCE;

(iii) for each of the previous 3 consecutive contract years at least 98 per cent of the rooms within the accommodation have been occupied for the whole of the relevant letting period.

"**Total Student Demand**" is the number of full time students at the University’s Colchester campus, less those students who live within Essex, Bedfordshire, Cambridgeshire, Hertfordshire, Norfolk or Suffolk who are not currently living in term time accommodation as

measured by HESA subject to the University reserving the right the revise the HESA data where they are reasonably able to demonstrate that such HESA data includes material factual inaccuracies in relation to the origin of Qualifying Students to the reasonable satisfaction of ProjectCo.

The "**Total Bed Supply**" means:

(i) existing University accommodation within the Colchester Campus; and

(ii) the accommodation under the Project Agreement; and

(iii) any Relevant Arrangements allowed (including approved or anticipated accommodation to be developed but not yet available); and

(iv) any accommodation which the University is at the relevant time proposing to become the subject of a Relevant Arrangement; and

(v) the Maltings.

ProjectCo has agreed that the University has demonstrated that the Applicable Tests have been met in relation to the development known as phase 2a.

1.12 **Supervening Events**

Relief Events apply during the operational phase. Relief Events are a specified set of events which are outside of the parties' control, and include:

(i) fire explosion, lightning, storm, tempest, flood, bursting or overflowing of water tanks, apparatus or pipes, ionising, radiation (to the extent it does not constitute a Force Majeure Event), earthquakes, riot and civil commotion;

(ii) any blockade or embargo which does not constitute a Force Majeure Event;

(iii) failure by a statutory undertaker utility company, local authority or other like body to carry out works or provide services; or

(iv) any: official or unofficial strike; lock out; go-slow; or other dispute generally affecting the construction and facilities, management industry or a significant sector of it.

None of the above will be treated as a Relief Event if the event arises (directly or indirectly) from any wilful default or act of ProjectCo.

Where either party to the Project Agreement is affected by a Relief Event, it must take all reasonable steps to mitigate the consequences of such event. If the Relief Event adversely affects the ability of either party to perform any of its obligations under the Project Agreement, then that party will be entitled to apply for relief. To obtain relief, the relevant party must give notice to the other party in accordance with the procedures and deadlines in the Project Agreement.

Where a Relief Event has arisen, no default, Default Event and Service Warning Notice (see below *Performance Monitoring and Service Default – Service Warning Notices*) shall arise. All other rights and obligations of the parties remain unaffected by the occurrence of the Relief Event. ProjectCo shall not be entitled to any compensation.

In relation to Force Majeure Events, see also the section entitled Summary of the Project Documents – The Project Agreement – Change Events – Compulsory Change Events below.

1.13 **Change Events**

(a) Compulsory Change Events

Compulsory Change Events apply during the operational phase as well as the works phase. Compulsory Change Events are a specified set of events which are either caused by the University's default or for which the University takes the risk, and include:

(i) a Change in Law which affects the Works or Services;

(ii) a Force Majeure Event;

(iii) an Uninsurable Risk Event; and/or

(iv) a change to the start date of an academic year which materially affects demand or shortens the Letting Period.

"**Change in Law**" is defined as the coming into effect or repeal of any law or any amendment, change in interpretation or variation to any law or any judgement of a relevant court of law which changes binding precedent (in each case after 7 August 2012) and includes any change in interpretation of any case law.

"**Force Majeure Events**" means the occurrence of one of the following (after 7 August 2012):

(i) war, civil war, armed conflict or terrorism (but excluding certain insured terrorist events); or

(ii) nuclear, chemical or biological contamination; or

(iii) pressure waves caused by devices travelling at supersonic speeds,

which directly causes ProjectCo to be unable to comply with any of its obligations under the Project Agreement.

An "**Uninsurable Risk Event**" arises where a risk against which ProjectCo or the University is required to insure under the Project Agreement for which (after 7 August 2012) either: insurance is not available within the European insurance market with reputable insurers of good standing in respect of that risk; or the terms and/or insurance premium offered in respect of that risk is at such a level that the risk is not generally being insured against in the European insurance market.

On the occurrence of a Compulsory Change Event, ProjectCo is to provide details of the impact to the University in accordance with the procedure in the Project Agreement. The parties are to agree how to deal with the Compulsory Change Event, which shall include:

(i) the variation of the Services and any consequential change in the cost of those Services;

(ii) any extension of the Term;

(iii) an increase or decrease in rental levels unless ProjectCo reasonably considers that any increase in rental levels would adversely affect demand for the Accommodation;

(iv) the obtaining by ProjectCo of any subsequent funding which is required in order to fund the Compulsory Change Event;

(v) the obtaining by the University of any subsequent funding which is required in order to fund the Compulsory Change Event.

Where the parties agree that subsequent funding should be obtained but this funding is insufficient to fund the costs of the Compulsory Change Event, or ProjectCo has not been able to obtain funding, then the University shall either provide ProjectCo with the full amount of the required funding, or terminate the Project Agreement.

(b) Voluntary Change Events

Either party may request a change to the Services or other obligations in the Project Agreement (a "**Voluntary Change Event**"). The parties are not obliged to consent to the proposed change unless both parties agree to give effect to the Voluntary Change Event and the method of financing it.

1.14 **Insurance**

(a) ProjectCo's Obligations

ProjectCo must ensure that certain required insurances (the "**Insurances**"), specified in the Project Agreement, have been taken out. The Insurances for the operations phase include material damage, business interruption and operational third party liability. ProjectCo, together with the FM Service Contractor, must also take out those insurances required by legislation.

(b) Application of Proceeds

All insurance proceeds that are paid as the result of a claim under the material damage policy are to be paid to the joint insurance account, or to another account if the Security Trustee as loss payee specifies.

All insurance proceeds received in relation to public risks shall be paid to the third party to satisfy the claim except where the insured has discharged its liability to the third party in which case the proceeds shall be paid to the project company insurance proceeds account (or such account as directed by the Security Trustee).

Proceeds from a claim under the business interruption insurance shall be paid to the joint insurance account, or to another account if the Security Trustee specifies.

(c) Uninsurable Risks

ProjectCo does not have to take out insurance where an insurable risk becomes Uninsurable. Accordingly, ProjectCo will not be held in breach of its insuring obligations under the Project Agreement.

For a risk to be "**Uninsurable**", then: insurance for the relevant risk must not be available within the European insurance market with reputable insurers of good standing in respect of that risk; or the terms and/or insurance premium offered in respect of that risk is at such a level that the risk is not generally being insured against in the European insurance market.

Where a risk becomes Uninsurable, the Compulsory Change Event provisions also apply, see "*Summary of the Project Documents – The Project Agreement – Change Events – Compulsory Change Events*" above.

(d) Damage to the Accommodation

Where rooms occupied by University tenants are damaged by an insured risk and are rendered uninhabitable:

(i) ProjectCo is to provide "**Suitable Alternative Equivalent Accommodation**", which means, in respect of each relevant University tenant, residential accommodation;

(A) (if practicable) within one mile of the University's Colchester campus;

(B) at a cost to the University tenant that is no higher than the rent payable in respect of the relevant Room until the Room becomes an available room or until the Project Agreement is terminated (whichever is earlier);

(C) if the accommodation does not include suitable self-catering facilities, ProjectCo (where appropriate) pays to the University tenant weekly in advance such sum as ProjectCo and University from time to time agree represents the cost to the University tenant of the lack of self-catering facilities; and

(D) if the accommodation is not within one mile of the University's Colchester campus ProjectCo pays (where appropriate) to the University tenant weekly in advance a reasonable travel allowance to reflect the cost to the University tenant of travelling by public transport from the alternative accommodation to the University's Colchester campus;

(ii) ProjectCo is to seek all necessary consents required to procure that the property is reinstated so that the rooms become available against (subject to the economic reinstatement test);

(iii) where it is not possible to rebuild or reinstate the property exactly as it was prior to the occurrence of the risk, then ProjectCo shall make the changes necessary to allow it to rebuild or reinstate in substantially the same form; and

(iv) in reinstating, ProjectCo shall pay due regard to the reasonable requests of the University.

If despite having used its reasonable endeavours ProjectCo has been unable to reinstate the property by a date three years after the occurrence of the risk, then ProjectCo may terminate the Project Agreement and compensation will be payable on the no fault basis.

(e) Insurance Premia

ProjectCo is responsible for the payment of insurance premia, subject to the application of the annual adjustment mechanism in setting the rents. See further "Summary of the Project Documents – The Project Agreement – Rent Setting" above.

1.15 **TUPE**

It was understood and intended by the parties that the commencement of the Services by ProjectCo and the commencement of the Services (and/or the LCM Works and/or the works at Quays site) by the FM Service Contractor on the Transfer Date (being the Quays Commencement Date, which occurred on 8 July 2013) constituted Relevant Transfers under the Transfer of Undertakings (Protection of Employment) Regulations 2006. The parties agreed that as a consequence of those Relevant Transfers and the arrangements entered into between ProjectCo and the FM Provider, the contracts of employment made between the University and the Employees had effect from and after the Transfer Date as if originally made between ProjectCo, the FM Provider or any of its or their subcontractors and the Employees. ProjectCo agreed with the FM Service Contractor that it or its subcontractor shall employ the Employees jointly with ProjectCo.

If the TUPE Regulations do not apply on the expiry or earlier termination of the Project Agreement, the University shall ensure that any new service provider of services equivalent to the Services offers employment to those employees of ProjectCo or any other person engaged by ProjectCo to procure the provision of the Services who provides the Services immediately before expiry or termination. The University will indemnify ProjectCo and its Sub-Contractors for any direct losses they suffer as a result of the University's failure to do so.

1.16 **Termination of the FM Service Contract at the University's Request**

The University may require ProjectCo to terminate the FM Service Contract due to certain service failures including:

(a) The FM Service Contractor has received six Service Warning Notices relating to an Individual Services Category (as identified in the Project Agreement) in any nine month period;

(b) The FM Service Contractor has received eighteen Service Warning Notices relating to All Services Categories in any nine month period; or

(c) Where there are two occurrences of the events in a) and b) above relating to the individual categories for certain specified services.

On substitution of the FM Service Contractor, any outstanding Service Warning Notices issued are cancelled. Where ProjectCo has tendered for a replacement FM provider and been unable to procure one for the price in the original financial model, then it is able to revise the price and adjust the rent accordingly. See further "*Summary of the Project Documents – The Project Agreement – Rent Setting*" above.

1.17 **Termination of the Project Agreement**

(a) ProjectCo Default Events

There are a number of specific events which, upon their occurrence or in certain cases if they are not remedied in accordance with the Project Agreement, entitle the University to terminate the Project Agreement.

The "**Default Events**" include:

(i) a breach by ProjectCo of the assignment provisions;

(ii) a breach by ProjectCo of its obligation to take out and maintain the Insurances;

(iii) the occurrence of more than two FM provider replacement events (see below *Performance Monitoring and Service Default – FM Service Contractor Replacement*) in any 5 year rolling period;

(iv) the abandonment of the Project Agreement by ProjectCo; or

(v) ProjectCo becoming insolvent;

(b) Compulsory Change Event

Compulsory Change Events include:

(i) a Change in Law which affects the Works or Services;

(ii) a Force Majeure Event;

(iii) an Uninsurable Risk Event; and/or

(iv) a change to the start date of an academic year which materially affects demand or shortens the Letting Period.

See further the section entitled "*Summary of the Project Documents – The Project Agreement – Change Events – Compulsory Change Events*" above.

(c) Corrupt Gifts and Fraud

A "**Prohibited Act**" can be summarised as meaning:

offering, giving or agreeing to give to the University or any other public body any gift or consideration as an inducement or reward for doing or not doing any act or showing or not showing favour or disfavour to any person in relation to the Project Agreement or any other agreement with the University or any other public body:

(i) entering into the Project Agreement or any other agreement with the University or any other public body in connection with which commission has been paid or has been agreed to be paid by ProjectCo without prior disclosure to the University;

(ii) committing any offence under the Bribery Act 2010, under any law creating offences in respect of fraudulent acts or at common law in respect of fraudulent acts in relation to the Project Agreement or any other agreement with the University or any other public body; or

(iii) defrauding or attempting to defraud the University or any other public body.

In the event that ProjectCo, any ProjectCo party or any of their employees commits a Prohibited Act, then the University may be entitled to terminate the Project Agreement. In certain cases, ProjectCo has the ability to prevent termination by "curing" the breach in specified ways. This may be achieved by terminating the employment of the relevant employee or terminating the contract of the relevant subcontractor (as the case may be) who committed the Prohibited Act.

(d) University Events of Default

"**University Events of Default**" are:

(i) the University and/or Universal Accommodation Group Limited ("**UAGL**") failing to pay any undisputed sum not exceeding £100,000 for more than 20 Business Days and/or any undisputed sum exceeding £100,000 for more than 20 Business Days);

(ii) a breach by the University which materially and adversely affects demand for the accommodation;

(iii) the University and/or UAGL committing a material breach of any of its obligations under the Project Agreement which frustrates and/or materially affects the performance of ProjectCo of its obligations under this Agreement;

(iv) a breach by the University of its financial covenants and/or restrictions and/or guidelines imposed on it by HEFCE provided such breach has a material adverse effect on the University's ability to perform its obligations under any Project Document and/or a material adverse effect on the then current income projections of ProjectCo;

(v) an order is made or other action is taken for the dissolution or winding up of the University;

(vi) an expropriation, sequestration or requisition of a material part of the accommodation;

(vii) any corporate or legal proceeding or other procedure or step (including the presentation of a petition (other than a winding up petition presented on frivolous or vexatious grounds contested in good faith and by appropriate proceedings which is discharged within 14 days of its presentation and before being advertised)) is taken prior to the grant of the Quays Lease in relation to UAGL;

(viii) h) the suspension of payments, a moratorium of any indebtedness, winding-up, dissolution, administration or reorganisation (by way of voluntary arrangement, scheme of arrangement or otherwise) of UAGL;

(ix) a composition, compromise, assignment or arrangement with any creditor of UAGL;

(x) the appointment of a liquidator, receiver, administrator, administrative receiver, compulsory manager or other similar officer in respect of UAGL or any of its assets;

(xi) a material breach by the University of clause 13 (Restrictive Covenant) of the Project Agreement;

(xii) a material breach by the University of clause 22.1 (Compulsory Change Event) of the Project Agreement;

(xiii) a material breach by the University of clause 21 (Assignment) of the Project Agreement;

(xiv) a failure by the University and/or UAGL to grant the leases in accordance with the Agreement for Lease;

(xv) the transfer of all or a substantial part of the University's undertaking, property, rights, or liabilities to any other person in each case otherwise than with the prior written consent of the Service Provider (which shall not be unreasonably withheld or delayed;

(xvi) relocation of any significant academic, sports and/or leisure facilities which materially and adversely affects demand for the Accommodation;

(xvii) any merger, amalgamation, and/or consolidation of the University with another body without the prior written consent of the Service Provider (which shall not be unreasonably withheld or delayed);

(xviii) a material breach by the University of clause 25A (Early Termination by the University and Substitution Rights) of the Project Agreement.

Where a University Event of Default occurs, ProjectCo may terminate the Project Agreement if the default is not remedied with a specified period following notice.

(e) Automatic Termination

The Project Agreement terminates automatically on termination of the Agreement for Lease.

(f) Bridge Closure

Where the bridge crossing that part of Network Rails Hythe Quays – Colchester to Walton-on-the-Naze line of railway at Colchester (the "**Bridge**") is closed for more than six months, ProjectCo can demonstrate an adverse impact on occupancy of the Quays premises and the University has failed to procure an alternative bridge, ProjectCo may terminate the Project Agreement.

1.18 **Compensation on Termination**

(a) Compensation in the Event of Termination for ProjectCo Default and Corrupt Gifts and Fraud

On termination of the Project Agreement for ProjectCo default and for corrupt gifts and fraud, the University will pay the "**Service Provider Default Sum**", which is the greater of:

(i) the Base Senior Debt Termination Amount; and

(ii) the Adjusted Estimated Fair Value of the Agreement.

If the amounts in calculating the Service Provider Default Sum are less than zero, they shall be deemed to be zero for the purposes of the calculation.

The "**Base Senior Debt Termination Amount**" consists of all amounts outstanding at the termination date (including indexation and interest in accordance with the relevant condition of the Bonds) payable by ProjectCo or the Issuer under the senior funding agreements and breakage costs relating to early termination including any interest rate hedging arrangements, less: credit balances on bank accounts; breakage costs payable by senior funders to ProjectCo; and all other amounts received by the senior funders between the termination date and the date on which compensation is payable.

The "**Adjusted Estimated Fair Value of the Agreement"** is the amount that would be paid to the University by a third party as calculated in accordance with the Project Agreement (see below) (the "**Estimated Fair Value of the Agreement**"), less an amount equal to the aggregate of the amounts that the University is entitled to set off or deduct under the Project Agreement plus credit balances on bank accounts and insurance proceeds and other amounts owing to ProjectCo.

The Estimated Fair Value of the Agreement is agreed in accordance with the principles set out in the Project Agreement, including:

(i) all forecast amounts should be calculated in nominal terms at current prices, recognising inflation adjustments;

(ii) the total of all future Annual net rental income and other forecast income to be received by ProjectCo to the Expiry Date, and discounted to the Termination Date;

(iii) the total of all costs forecast to be incurred by the University as a result of termination shall be calculated and discounted and deducted from the payment calculated above.

The Service Provider Default Sum is payable either: as a lump sum within 10 business days of agreement of the sum, with interest at the no default interest rate from the termination date until the date 40 business days after the termination date and thereafter at the default interest rate; or by request from the University and at the controlling creditor's discretion, by instalments on agreed payment dates.

(b) Compensation in the Event of Termination for University Default, Bridge Closure and Corrupt Gifts and Fraud (where ProjectCo has terminated)

On termination of the Project Agreement for University Default, Bridge closure and corrupt gifts and fraud (where ProjectCo has terminated), the University will pay the "**University Default Termination Sum**", which is:

(i) the Base Senior Debt Termination Amount;

(ii) the UD Junior Debt;

(iii) the Sub-Contractor Breakage Costs; and

(iv) redundancy payments of employees of ProjectCo and the FM Service Contractor.

If the amounts in calculating the University Default Termination Sum are less than zero, they shall be deemed to be zero for the purposes of the calculation.

The "**UD Junior Debt**" is the aggregate amount for which the share capital of ProjectCo and the amounts outstanding at the Termination Date due to be paid to the Sponsor ProjectCo under the Subordinated Finance Documents could have been sold on an open market basis based on the Relevant Assumptions which are that:

(i) there is no default by the University;

(ii) the sale is on a going concern basis;

(iii) no restrictions exist on the transfer of share capital; and

(iv) rental income is forecast to be at least the Modelled Aggregate Base Rents in the financial close model but that otherwise the actual state of affairs of the Service Provider and the Project is taken into account.

"**Sub-Contractor Breakage Costs**" are certain direct losses incurred by ProjectCo and/or the FM Service Contractor as a result of the termination.

If the Base Senior Debt Termination Amount (as defined in paragraph "*1.18(a) Compensation in the Event of Termination for ProjectCo Default and Corrupt Gifts and Fraud*" above) plus the UD Junior Debt is less than the Revised Senior Debt Termination Amount then the compensation payable shall be increased to the aggregate of the Revised Senior Debt Termination Amount plus redundancy and Sub-Contractor Breakage Costs. The amount comprising redundancy and Sub-Contractor Breakage Costs shall only be paid to the extent ProjectCo has demonstrated that it will not be applied in payment of a distribution. If at the time of termination there are Additional Permitted Borrowings (as defined below) outstanding, no Sub-Contractor Breakage Costs shall be paid in circumstances where there is an event of default under such sub-contract which would entitle ProjectCo to terminate that sub-contract.

The "**Revised Senior Debt Termination Amount**" consists of all amounts outstanding at the termination date (including Early Redemption Amount (as defined in Condition 6 (*Redemption and Purchase*) of the Terms and Conditions of the Bonds) indexation and interest in accordance with the relevant condition of the Bonds) payable by ProjectCo or the Issuer under the senior funding agreements and Breakage Costs) (to be made in accordance with the provisions headed "Payments on Dates of Early Redemption or Acceleration" in the Financial

Guarantee Fee Letters) relating to early termination and costs of early termination of any interest rate hedging arrangements, less: credit balances on bank accounts; breakage costs payable by senior funders to ProjectCo; and all other amounts received by the senior funders between the termination date and the date on which compensation is payable; and all APB Distributions (being, for the period during which additional permitted borrowing subsists, an amount equal to all distributions made during the period up to an amount equal to the principal of the Additional Permitted Borrowing on the first day of that period).

ProjectCo is entitled under the Project Agreement to raise further borrowing (Additional Permitted Borrowings) without the consent of the University, subject to a limit (the "**Additional Permitted Borrowings Limit**"). "**Additional Permitted Borrowings**" is that amount of principal that exceeds the amount scheduled at financial close to be outstanding at any time, and the Additional Permitted Borrowings Limit is initially 10 per cent. of the original senior debt commitments at the Issue Date until outstanding principal is 50 per cent. or less of those commitments, when the limit reduces to 5 per cent. of those commitments (or the then outstanding Additional Permitted Borrowings if higher).

Additional borrowing invested in a Compulsory Change Event or Voluntary Change Event is not treated as Additional Permitted Borrowings.

Where an APB Distribution (as defined in paragraph 1.18(b) *Compensation in the Event of Termination for University Default, Bridge Closure and Corrupt Gifts and Fraud (where ProjectCo has terminated)*) has been made and ProjectCo has failed to comply with certain obligations under the Funder Direct Agreement, then the University can set off the value of that APB Distribution against the University Default Termination Sum (notwithstanding that the APB Distribution has also been taken into account when calculating the Revised Senior Debt Termination Amount), provided that the amount of the University Default Termination Sum shall not be less than the Revised Senior Debt Termination Sum.

Where ProjectCo has failed to comply with certain obligations under the Funder Direct Agreement and overstated the cash balances which has caused the University to believe that it would be required to pay a lesser sum at termination than is actually due, then the University can set off the value of that overstatement against the University Default Termination Sum, provided that the amount of the University Default Termination Sum shall not be less than the Revised Senior Debt Termination Sum.

The University Default Termination Sum is payable either: as a lump sum within 10 business days of agreement of the sum, with interest at the no default interest rate from the termination date until the date 40 business days after the termination date and thereafter at the default interest rate

(c) Compensation in the Event of Termination for Compulsory Change Events including Force Majeure

On termination of the Project Agreement in the event of Compulsory Change Events including Force Majeure, the University shall pay the No Fault Termination Sum, which is:

(i) the Base Senior Debt Termination Amount;

(ii) the NF Junior Debt;

(iii) all amounts paid to ProjectCo by way of share subscriptions, less distributions paid to the shareholders;

(iv) the Sub-Contractor Breakage Costs; and

(v) redundancy payments of employees of ProjectCo and the FM Service Contractor.

If the amounts in calculating the No Fault Termination Sum are less than zero, they shall be deemed to be zero for the purposes of the calculation.

The "**NF Junior Debt**" comprises all amounts outstanding at the Termination Date under the Subordinated Finance Documents due to be paid to the Sponsors from ProjectCo, less an amount equal to the aggregate of payments of interest made by ProjectCo under the Subordinated Finance Documents (and where such amount is less than zero the amount shall be deemed to be zero).

If the aggregate of Base Senior Debt Termination Amount (as defined in paragraph 1.18(a) *Compensation in the Event of Termination for ProjectCo Default and Corrupt Gifts and Fraud* above), the NF Junior Debt and all amounts paid to ProjectCo by way of share subscriptions, less distributions paid to the shareholders is less than the Revised Senior Debt Termination Amount (as defined in paragraph 1.18(b) *Compensation in the Event of Termination for University Default, Bridge Closure and Corrupt Gifts and Fraud (where ProjectCo has terminated)* above) then the compensation payable shall be increased to the aggregate of the Revised Senior Debt Termination Amount plus redundancy and Sub-Contractor Breakage Costs. The amount comprising redundancy and Sub-Contractor Breakage Costs shall only be paid to the extent ProjectCo has demonstrated that it will not be applied in payment of a distribution. If at the time of termination there are Additional Permitted Borrowings (as defined below) outstanding, no Sub-Contractor Breakage Costs shall be paid in circumstances where there is an event of default under such sub-contract which would entitle ProjectCo to terminate that sub-contract.

ProjectCo is entitled under the Project Agreement to raise Additional Permitted Borrowings without the consent of the University, subject to a limit Additional Permitted Borrowings Limit.

Additional borrowing invested in a Compulsory Change Event or Voluntary Change Event is not treated as Additional Permitted Borrowings.

Where an APB Distribution (as defined in paragraph 1.18(b) *Compensation in the Event of Termination for University Default, Bridge Closure and Corrupt Gifts and Fraud (where ProjectCo has terminated)*) has been made and ProjectCo has failed to comply with certain obligations under the Funder Direct Agreement, then the University can set off the value of that APB Distribution against the University Default Termination Sum (notwithstanding that the APB Distribution has also been taken into account when calculating the Revised Senior Debt Termination Amount), provided that the amount of the University Default Termination Sum shall not be less than the Revised Senior Debt Termination Sum.

Where ProjectCo has failed to comply with certain obligations under the Funder Direct Agreement and overstated the cash balances which has caused the University to believe that it would be required to pay a lesser sum at termination than is actually due, then the University can set off the value of that overstatement against the University Default Termination Sum, provided that the amount of the University Default Termination Sum shall not be less than the Revised Senior Debt Termination Sum.

The No Fault Termination Sum is payable either: as a lump sum within 10 business days of agreement of the sum, with interest at the no default interest rate from the termination date until the date 40 business days after the termination date and thereafter at the default interest rate

(d) Tax Gross-up

This is payable by the University in case of compensation payments for all circumstances leading to termination.

2. **Agreement for Lease**

2.1 **General**

The agreement for lease, dated 7 August 2012, was entered into between University, Universal Accommodation Group Limited (the "**Quays Head Landlord**"), University of Essex

Knowledge Gateway Holdings Limited (the "**Adjoining Owner**") and Project Co (the "**Agreement for Lease**").

2.2 **The Works**

(a) Meadows Overview

ProjectCo was required to design and construct the Developer's Works at the Meadows site comprising student residences, service areas, landscape areas and means of access and egress.

These obligations were passed to the Building Contractor under the Building Contract as further described in the section entitled "The Building Contract" below.

(b) Quays Overview

ProjectCo was required to undertake certain "Catch-up Works" at the Quays site as identified in the first condition survey.

Project Co was required to commission a further condition survey, and to complete any "Further Works" identified as being required in such second condition survey. The cost of any Further Works was deductible from the Quays premium otherwise payable to the Quays Head Landlord.

ProjectCo was required to undertake the Quays Works which consisted of the conversion of a café area into thirteen additional rooms.

(c) Design and Carrying Out

ProjectCo was required to complete the Developer's Works in accordance with the Agreement for Lease including the Developer's Works Specification as set out therein.

ProjectCo was required to complete the Catch-up Works in accordance with a condition survey dated August/September 2011 undertaken by Davis Langdon LLP (the "**Condition Survey Consultant**").

ProjectCo was required to complete the Further Works in accordance with a further condition survey undertaken by the Condition Survey Consultant.

ProjectCo was required to complete the Quays Works in accordance with the Agreement for Lease including the Quays Works Specification as set out therein.

2.3 **Works Completion**

The Works required pursuant to the Agreement for Lease have been certified as complete in accordance with the relevant requirements.

2.4 **The Leases**

The leases granted pursuant to the Agreement for Lease are described in the section entitled "*Real Estate Documents – Leases"* below.

2.5 **Adjoining Owner**

The Adjoining Owner is party to the "Agreement for Lease" in order to grant certain specified rights over its adjoining land.

3. **The Building Contract**

3.1 **General**

The Building Contract is between ProjectCo and Bouygues (U.K.) Limited. The Works-related obligations of ProjectCo in the section entitled Agreement for Lease above were passed down to the Building Contractor.

The Project is in the operational phase, so the Building Contract is in many aspects historic.

3.2 **Supporting Documents**

The Building Contractor’s obligations under the Building Contract were guaranteed by Bouygues Batiment International (the "**Guarantor**") under the Parent Company Guarantee. This limited the liability of the Guarantor to the Building Contractor’s liability to ProjectCo under the Building Contract.

4. **The FM Service Contract**

4.1 **General**

The FM Service Contract is between ProjectCo and Derwent Housing Association Limited. The FM Service Contractor’s obligations have been described in detail by reference to the pass down of ProjectCo’s Services-related obligations (including IT services and the provision of lifecycle works) in the section entitled "Project Agreement" above, but included immediately below is a summary of the works obligation which are passed down, along with a description of the circumstances in which termination of the FM Service Contract can occur and supporting FM Service Contract document information.

4.2 **Works – Quays Site**

The FM Service Contractor was obliged to undertake the Catch-up Works identified in the first condition survey; any Further Works identified in the second condition survey; and the Quays Works to convert an existing café to thirteen additional rooms, in accordance with the specification set out in the FM Service Contract.

4.3 **Termination**

(a) FM Service Contractor Default

Events of default entitling ProjectCo to terminate the FM Service Contract include:

(i) A material breach by the FM Service Contractor of its obligations under the FM Service Contract;

(ii) The FM Service Contractor has received five Service Warning Notices relating to an Individual Services Category in any nine month period;

(iii) The FM Service Contractor has received sixteen Service Warning Notices relating to an All Services Categories in any nine month period;

(iv) The occurrence of certain insolvency events;

(v) A breach of the FM Service Contractor’s insurance obligations;

(vi) A breach of the restriction on assignment;

(vii) A breach of the FM Service Contract by the FM Service Contractor which causes ProjectCo to be in material breach of the Project Agreement;

(viii) ProjectCo incurs costs due to the FM Service Contractor breaching its Annual Cap on Liability.

Under the Project Agreement, the University may require ProjectCo to terminate the FM Service Contract due to certain service failures including:

(i) The FM Service Contractor has received six Service Warning Notices relating to an Individual Services Category in any nine month period;

(ii) The FM Service Contractor has received eighteen Service Warning Notices relating to an All Services Categories in any nine month period; or

(iii) Where there are two occurrences of the events in a) and b) above relating to the individual categories for certain specified services.

(b) ProjectCo Default

Events of default entitling the FM Service Contractor to terminate the FM Service Contract include:

(i) ProjectCo becoming insolvent;

(ii) Failure to pay by ProjectCo of a sum equal to two months' Total FM Sum;

(iii) Material breach by ProjectCo which prevents the FM Service Contractor from performing its obligations.

4.4 **Liability Caps**

(a) The FM Service Contractor's annual cap on liability is an amount equal to 100% of the Total FM Sum in that contract year.

(b) The FM Service Contractor's cap on liability in the case of termination or expiry is:

(i) an amount equal to 200% of the Total FM Sum in the contract year or termination or expiry; and

(ii) in relation to a lifecycle shortfall, £5,000,000 (indexed) provided that this shall be limited to the actual lifecycle shortfall at the time of termination or expiry.

4.5 **Tangible Net Worth**

If the FM Service Contractor's tangible net worth falls below £10,000,000 then it is obliged to give ProjectCo a notice setting out the details of such occurrence. ProjectCo may require the FM Service Contract to be novated or assigned to a subsidiary or associate of the FM Service Contractor if it considers that the reduced net worth is insufficient for the FM Service Contractor to meet its obligations under the FM Contact.

4.6 **Supporting Documents**

The FM Service Contractor has no parent company and as such has not provided a parent company guarantee. ProjectCo and the FM Service Contractor entered into a Parallel Loan Agreement at the Original Financial Close Date.

ProjectCo, the FM Service Contractor, the Security Trustee will, by the Issue Date, enter into a direct agreement which acknowledges the security granted over the FM Service Contract and regulates step-in rights under the FM Service Contract.

5. **Funders' Direct Agreement**

On or before the Issue Date, the University, Security Trustee and ProjectCo will enter into a direct agreement (the "**Funders' Direct Agreement**"), providing for rights of step-in and step-out in default situations that might otherwise cause termination of the Project Agreement.

6. **Performance Monitoring and Service Default**

6.1 **General**

ProjectCo is to provide the University and the liaison group established pursuant to the Project Agreement with the performance monitoring report on a monthly basis, in accordance with the requirements of the performance management schedule. The performance monitoring report is to show for each service category, the performance level against the performance target for each performance standard, for the relevant service requirement.

The "**Service Categories**" are Services measured by the performance monitoring schedule relating to:

(i) General Compliance;

(ii) Building and Maintenance;

(iii) Grounds Maintenance;

(iv) Cleaning and Housekeeping;

(v) Security;

(vi) Pastoral Welfare & Student Management;

(vii) Utilities;

(viii) IT Service;

(ix) Car Park; and

(x) External Facilities.

During the operational phase these risks are passed to the FM Service Contractor.

6.2 **Service Defaults**

A service default is, subject to the terms of the Project Agreement, any failure to carry out the Service Requirements in accordance with the relevant performance standard.

If there is a service default, ProjectCo shall notify in the performance monitoring report any service default identified, including reasonable details of the service default and the number of service default points (if any) attributable. ProjectCo is to rectify any service default within the relevant temporary rectification period (if any) and the permanent rectification period for that Service Requirement. If ProjectCo has not so rectified the service default, the University may award the relevant service default points. Service default points are calculated in accordance with the default points methodology.

Where a service default occurs due to a defect caused by the Building Contractor, The University may not award service default points for a period of eighteen months to enable ProjectCo to rectify any such defect. Where ProjectCo takes the specified steps including taking action against the Building Contractor and uses reasonable endeavours to rectify or procure rectification of the service defaults, then the eighteen month period referred to shall be extended by a reasonable amount, up to a maximum of six further months. During this time, the University may still categorise a room as Unavailable, and require ProjectCo to provide alternative accommodation and use its other rights under the Project Agreement.

6.3 **Service Default Points**

Where the service default points for any service category in any measurement period exceeds the increased monitoring default threshold, then ProjectCo shall implement increased monitoring. If such monitoring is not implemented within ten business days, then ProjectCo shall implement a remediation plan.

If within two payment dates for any service requirement, the increased monitoring default threshold has been exceeded twice, then ProjectCo shall implement a remediation plan.

ProjectCo shall also implement a remediation plan where the service default points for any service category in any measurement period exceeds the remediation plan default threshold.

Where there has been an all service category default and: 100 or more but less than 200 service default points have been awarded in any one month; or 50 service default points have

been awarded per month for three months, then ProjectCo shall implement increased monitoring.

Where there has been an all service category default and: 200 or more have been awarded in three consecutive months but less than 300 service default points, then ProjectCo shall implement a remediation plan.

6.4 **Service Warning Notices**

The University may serve a service warning notice:

(i) if a remediation plan is not in the process of implementation within twenty business days of the requirement being triggered;

(ii) if within three consecutive payment dates for any service requirement three or more increased monitoring defaults have been incurred;

(iii) where the number of service default points for any service category in any measurement period exceeds the service warning notice threshold;

(iv) where there has been an all service category default and the number of service default points is equal to 300 or more service default points in three consecutive months or equals 600 service default points in any one month;

(v) where there is a health and safety breach which has not been rectified within the relevant rectification period,

a "**Service Warning Notice**".)

The obligations of ProjectCo described in this section are passed to the FM Service Contractor.

6.5 **FM Service Contractor Replacement**

Should the FM Service Contractor seriously fail in the performance of the Services, ProjectCo may terminate the FM Service Contract. The University is entitled to require ProjectCo to terminate the FM Service Contract if it issues 6 Service Warning Notices relating to an individual service category in any three consecutive payment dates, or 18 Service Warning Notices relating to all service categories in any three consecutive payment dates. An all service category FM provider replacement event can also arise if there are two individual category FM provider replacement events in any three payment periods relating to building maintenance, cleaning and housekeeping, security or IT services. These triggers for requiring termination are lower than the FM Service Contractor events of default.

7. **Real Estate Documents – Project Leases**

The project is situated across two distinct locations: the Meadows, and Quays sites.

7.1 **Headleases – Meadows**

(a) The Meadows site, at the University of Essex Research Park, Elmstead Road, Colchester, Essex, is divided into five blocks, a separate headlease, each dated 7 August 2012, was entered into between the University (as landlord) and ProjectCo (as tenant) in relation to each block (known as M1-M5) (the "**Meadows Headleases**").

(b) Each Meadows Headlease contains the following terms:

(i) It runs for a period from 7 August 2012 until and including 4 July 2063 (the "**Meadows Contractual Term**"). The Meadows Headleases also contain an option to renew at any time during the Meadows Contractual Term.

(ii) Early termination upon the early termination of the Project Agreement.

(iii) Registered in the Land Register of England.

(iv) Rent is a peppercorn.

(v) As each Meadows Headlease is subject to the terms of the Project Agreement, the occupational obligations on ProjectCo are not extensive. The occupational obligations include:

(A) to keep the Meadows Premises in good and substantial repair during the Meadows Initial Period;

(B) to decorate the exterior of the Meadows Premises at least once every 10 years;

(C) not to make any alterations or additions to the Meadows Premises without the Landlord's permission by way of licence;

(D) not to use the Meadows Premises otherwise than for the use as stated in the Meadows Headleases;

(E) not to assign the whole of the Meadows Premises during the Meadows Initial Period unless in accordance with the Project Agreement and not to assign part only of the Meadows Premises;

(F) not to underlet part or whole of the Meadows Premises during the Meadows Initial Period except for the Meadows Underleases and the granting of licences or tenancies on an assured shorthold basis of less than 12 months;

(G) not to charge part only of the Meadows Premises during the Meadows Initial Period and not to charge the whole of the Premises without the Landlord's permission;

(H) to respect terms relating to rights of light and encroachment during the Meadows Initial Period; and

(I) pay all rents and charges for rates, taxes, duties, charges, assessments and outgoings and indemnify ProjectCo for any amenities used which are not separately assessed.

Furthermore, some of these occupational obligations have been transferred on to the University in the Meadows Underleases and to Compass in the Compass Lease.

(c) In the Meadows Headleases, several of the occupational obligations no longer apply and instead are replaced with less restrictive obligations on ProjectCo once the period ends which runs from the date of the Meadows Headleases until the earlier of:

(i) the date from and including 50 years from the date of the Meadows Headleases;

(ii) the date upon which ProjectCo exercises its rights to assign the Meadows Headlease as a result of the University not making the capital sum contribution notified to it by ProjectCo in respect of the Annual Debt Service Cover Ratio in accordance with the Project Agreement; or

(iii) the date of termination (if any) of the Project Agreement (the "**Meadows Initial Period**").

(d) The reduced occupational obligations on ProjectCo from the end of the Initial Period in respect of the Meadows Headleases include the following:

(i) the restrictions on alterations no longer apply and the restrictions on permitted use are reduced. Instead, ProjectCo may use the Meadows Premises for such other use as may be permitted under planning law whether or not specifically the subject of a planning permission;

(ii) the restrictions on underlettings in the Meadows Headleases no longer apply and the restrictions on assigning and charging the whole of the Meadows Premises in the Meadows Headleases no longer apply; and

(iii) the repair obligation is amended to an obligation on the Tenant to maintain the external appearance of the Premises in reasonable state of repair and in a clean and tidy condition free of rubbish.

(e) The University is obliged under the Meadows Headleases to provide services relating to the operation and maintenance of common areas, i.e. footpaths, car parks, service roads, made available to ProjectCo from time to time, for which ProjectCo pays a service charge, during the Initial Period and after it has ended.

7.2 **Headleases – Quays**

(a) The Quays site, at Hythe Riverside Park, Colchester, is divided into three sections, as separate headlease, each dated 8 July 2013, was entered into between Universal Accommodation Group Limited (as landlord) and ProjectCo (as tenant) in relation to each block (known as Q1-Q3).

(b) Each Quays Headlease contained the following terms:

(i) It runs for a period from 8 July 2013 until and including 4 July 2063 (the "Quays Contractual Term"). The Quays Headleases also contain an option to renew at any time during the Quays Contractual Term.

(ii) Early termination upon the early termination of the Project Agreement.

(iii) Registered in the Land Register of England.

(iv) Rent is a peppercorn.

(v) As each Quays Headlease is subject to the terms of the Project Agreement, the occupational obligations on ProjectCo are not extensive. The occupational obligations include:

(A) to keep the Quays Premises in good and substantial repair during the Quays Initial Period;

(B) to decorate the exterior of the Quays Premises at least once every 10 years;

(C) not to use the Quays Premises otherwise than for the use as stated in the Quays Headleases.

(D) not to assign the whole of the Quays Premises during the Quays Initial Period unless in accordance with the Project Agreement and not to assign part only of the Meadows Premises;

(E) not to underlet part or whole of the Quays Premises during the Quays Initial Period except for the Quays Underleases and the granting of licences or tenancies on an assured shorthold basis of less than 12 months;

(F) not to charge part only of the Quays Premises during the Quays Initial Period and to charge the whole of the Quays Premises without the Landlord's permission;

(G) to respect terms relating to rights of light and encroachment during the Quays Initial Period; and

(H) pay all rents and charges for rates, taxes, duties, charges, assessments and outgoings and indemnify ProjectCo for any amenities used which are not separately assessed.

Furthermore, some of these occupational obligations have been transferred on to the University in the Quays Underleases.

(c) In the Quays Headleases, several of the occupational obligations no longer apply and instead are replaced with less restrictive obligations on ProjectCo once the period ends which runs from the date of the Quays Headleases until the earlier of:

(i) the date from and including 50 years from the date of the Quays Headleases;

(ii) the date upon which ProjectCo exercises its rights to assign Quays Headlease as a result of the University not making the contribution notified it by ProjectCo to in respect of the Annual Debt Service Cover Ratio in accordance with the Project Agreement; or

(iii) the date of termination (if any) of the Project Agreement (the "**Quays Initial Period**").

(d) The reduced occupational obligations on ProjectCo from the end of the Initial Period in respect of the Quays Headleases include the following:

(i) the restrictions on permitted use are reduced. Instead, ProjectCo may use the Quays Premises for such other use as may be permitted under planning law whether or not specifically the subject of a planning permission;

(ii) the restrictions on underlettings in the Quays Headleases no longer apply and the restrictions on assigning and charging the whole of the Quays Premises in the Quays Headleases no longer apply; and

(iii) the repair obligation is amended to an obligation on the Tenant to maintain the external appearance of the Premises in reasonable state of repair and in a clean and tidy condition free of rubbish.

(e) The University is obliged under the Quays Headleases to provide services relating to the operation and maintenance of common areas, i.e. the areas and amenities within the Quays Premises including any roads, footpaths, car parks, loading bays and similar.

(f) Railtrack Deed of Covenant

In the event of a disposal of any part of the Quays Premises for value, ProjectCo is under an obligation in the Quays Headleases to ensure that any successor tenant must enter into a deed of covenant with Network Rail to observe the University's obligations in respect of the railway track on the Quays Premises, which include payment obligations.

(g) Tenant and Landlord Deeds of Covenants

In the event that the one or more of the Quays Headleases falls away and is transferred or merged with the freehold, ProjectCo is under an obligation to enter into a deed of covenant with the freehold owner of that transferred land to maintain certain positive obligations relating to the common areas between Blocks Q1-Q3, such as to keep those parts of the Quays Premises in a reasonable state of repair and condition and to pay costs relating to their maintenance. In such circumstances, the Universal Accommodation Group Limited, as landlord, is also obliged to enter into direct covenants with the tenants of the transferred or merged land to ensure that it will also carry forward its maintenance obligations in respect of the common parts of the Quays Premises.

7.3 **Underleases – Meadow and Quays**

(a) Separate undeleases, each dated 30 January 2014, were entered into between ProjectCo (as landlord) and the University (as tenant) in relation to blocks M1-M4 and part of block M5 following practical completion of ProjectCo's works. Part of block M5 was granted by underlease from ProjectCo to Compass Contract Services (UK) Limited, see further below.

(b) Separate underleases, each dated 8 July 2013, were entered into between ProjectCo (as landlord) and the University (as tenant) in relation to each block (Q1-Q3) of the Quays site.

(c) The occupational obligations on ProjectCo under the Meadows Headleases are transferred down as occupational obligations on the University under the Meadows Underleases and to Compass under the Compass Lease and in respect of the Quays Premises, the same applies to the Quays Headleases and the Quays Underleases. Points to note include:

(i) the University is not obliged to pay the cost of rates or the cost of providing services (i.e. these remain the responsibility of ProjectCo under the Meadows Headleases and the Quays Headleases).

(ii) the permitted use in all the Meadows and Quays Underleases is as defined in the relevant Meadows and Quays Headleases.

(iii) the University is not permitted to assign or sub-let part only of the Meadows Premises or the Quays Premises and is not permitted to assign or sub-let the whole of either the Meadows Premises or the Quays Premises otherwise than in accordance with the Project Agreement. The University is, however, entitled to grant student leases for less than 12 months.

(iv) The term expires on 1 July 2063.

7.4 **Underlease – Meadows – Pavilion**

(a) Part of block M5, known as the Pavilion, was subject to an underlease (the "**Compass Lease**"), dated 30 January 2014, between Project Co (as landlord) and Compass Contract Services (UK) Limited ("**Compass**").

(b) The occupational obligations on ProjectCo under the Meadows Headlease (M5) are transferred down as occupational obligations to Compass under the Compass Lease. The Compass Lease runs for a term of 10 years from 30 January 2014:

(i) Compass is obliged to pay and fully indemnify ProjectCo against all rates, taxes, levies, costs, charges, outgoings, assessments and impositions of any kind payable to any authority in respect of the Compass Premises.

(ii) the permitted use in the Compass Lease is for a high quality coffee shop within use class A1 and/or A3 of the Town and Country Planning (Use Classes) Order 1987.

(iii) Compass is not permitted to assign any part of the Compass Premises without ProjectCo's written consent as Landlord and not to share possession of the Compass Premises but it may share occupation with concessionaires and/or franchisees and/or a group company subject to ProjectCo consent as Landlord.

(iv) Compass is not permitted to underlet the Compass Premises unless it complies with certain conditions set out by ProjectCo which include a requirement for the future undertenant to enter into direct covenants with ProjectCo and to serve notices on ProjectCo.

(v) Compass is obliged to achieve a minimum turnover of £175,000 per annum and to reach a turnover threshold of £250,000 per annum (to increase annually).

The current sub-lease with Compass UK Limited is due to be terminated with effect from the summer of 2017.

8. **Insurance Arrangements**

8.1 **Summary of Insurance**

ProjectCo will place cover for the operational phase in accordance with the Project Documents and Senior Finance Documents. Policies will name the respective interested parties as Insured

Parties. The principal areas of cover, values at risk, limits of indemnity and deductibles will be as required in the Project Documents and Senior Finance Documents.

8.2 **Risk Areas Covered**

(a) Material Damage Insurance

All Risks protection has been effected by ProjectCo from the commencement of the operational phase for ProjectCo, the University, the FM Service Contractor and the Senior Lender and Security Trustee. They are included as insured parties. The insured property is the project assets for which ProjectCo is responsible.

(b) Business Interruption Insurance

Business interruption protection has been arranged for the operational phase for loss of revenue streams (to cover, among other things, revenue and anticipated third party income that would have been applied to debt servicing and fixed overheads). The business interruption insurance responds following loss or damage insured under the material damage insurance noted above.

The insured parties are ProjectCo, and the Senior Lender and Security Trustee. Extensions include failure of utilities, denial of access and terrorism.

Additional increased cost of working cover has also been arranged for additional costs incurred from having to procure alternative accommodation following loss or damage insured under the material damage insurance noted above.

(c) Third Party Liability

Cover for ProjectCo's legal liability for third party death or injury, and property damage has been affected to a limited of indemnity specified in the Project Documents and Senior Finance Documents for any one occurrence (but limited to an overall limit in aggregate for pollution and products liability claims).

(d) Others

Other insurances require by legislation, including employers' liability and motor vehicle insurances, have been effected by ProjectCo as required.

THE UNIVERSITY OF ESSEX

University Background / History

The University of Essex is a research-intensive university founded in 1963 which received its Royal Charter in 1965. The University has three campuses with the majority of both students and accommodation located at the main campus in Colchester. The Colchester campus is a self-contained true campus environment at the outskirts of the town.

The University is among the leading UK institutions in social sciences and describes itself as an academic community, which encourages its members to challenge the status quo and have a positive impact on society both, during and after their time at University. The institution prides itself for its international outlook; reflected in its diverse student base as well as internationally focused research and teaching.

Rankings and Collaborations

The University scored highly in the 2013 Research Excellence Framework (**REF**) submitting world-leading research ratings in a range of humanities based subjects. The institution is ranked among the top 20 research universities overall, with a top 5 position in social science and a first place in political research. The University also features within the top half of newspaper league table rankings and achieved, with a rank of 30th in The Times 2017 league table, its highest rank to date.

Governance

The University is a body incorporated by Royal Charter. The University's governing body is the Council, which is committed to achieving high standards of corporate governance in line with accepted best practice.

The University Governing Body

Members of the Council are the trustees of the University which is an exempt charity. The University's Council comprises ex officio external members, a student member, ex officio appointed employees, employees elected by Senate (the supreme academic authority of the University which is accountable to the Council). The roles of Chancellor and Pro-Chancellors (including the Chair of the Council) are separated from the role of the University's Chief Executive and Vice-Chancellor.

The Council

The Council of the University has adopted a Statement of Primary Responsibilities which is published on the University website. The statement sets out the Council's responsibilities in respect of powers of appointment and employment, financial and legal powers, planning, monitoring, control and student welfare.

The University complies with the Committee of University Chairs (**CUC**) Higher Education Code of Governance issued in December 2014.

The Council normally meets four times during the year and hold one full and two half away days. Of its 25 members, a majority are external members drawn from outside the University.

Officers of the University

Chancellor
The Right Honourable Baroness Chakrabarti, CBE
Pro-Chancellor
David Currie BSc MSocSci PhD (Chair of the Council) (external)
Judith Judd (external member of Council)
Maria Stanford (external member of the Council)
Vice-Chancellor
Professor Anthony Forster, FHEA FLF FRSA FAcSS
Treasurer
Tim Porter, MA FCA (external member of Council)

Deputy Vice-Chancellor
Professor Jules Pretty, OBE FRSA FIBiol
Pro-Vice-Chancellor (Education)
Professor Aletta Norval, BA BA MA PhD
Pro-Vice-Chancellor (Research)
Professor Heather Laurie BA PhD
Executive Deans
Professor Lorna Fox O'Mahony LLB PhD PGCHET; (Humanities)
Professor Graham Underwood BSc DPhil; (Science and Health)
Professor Sasha Roseneil BSc (Econ) PhD PGDip FAcSS MInstGA; (Social Sciences)

Dean of Partnerships
Professor Dominic Micklewright, PhD CPsychol MSc BSc PGCertHE FHEA
Deputy Dean of Partnerships
Allan Hildon, BHealthSc (Nursing)
Deputy Dean (Education) (Humanities)
Dr Peter Luther, MA MA PhD
Deputy Dean (Education) (Science and Health)
Dr David Penman, MA MMath MSc PhD
Deputy Dean (Education) (Social Sciences)
Professor Jackie Turton, SRN SCM:HV BA PhD
Dean of Postgraduate Research and Education
Professor David Pevalin, MA MA PhD (until 31 December 2016)
Professor Martyna Sliwa BA MA MSc PhD (from 1 October 2016)
Deputy Dean (Postgraduate Research and Education) (Humanities)
Dr Matthew Grant, PhD FRHistS
Deputy Dean (Postgraduate Research and Education) (Science and Health)
Professor Ian Colbeck, MSc PhD FInstP CPhys FRMets
Deputy Dean (Postgraduate Research and Education) (Social Sciences)
Dr Magda Abou-Seada, BComm MPhil PhD
Dean of Health
Professor Joanna Jackson, CertED BA MSc EdD MCSP
Registrar and Secretary
Bryn Morris BA
Student Conduct Officer
Penny Brearey-Horne, LLM LLB

University Funding

The University's three main revenue streams relate to teaching, research and commercial income.

Teaching income is derived from a mixture of public and private sources through fees payable by home, EU and overseas students at undergraduate and postgraduate taught levels. Regarding home undergraduate students, block grants from government have reduced significantly since the introduction of the higher-rate fee in 2012. Research is funded via the 'dual support' mechanism, with a significant block grant based on quality and volume of research, and a competitive approach for the funding of short-term research projects, sponsored by Research Councils, government, the EU, charities and industry. Postgraduate research students are funded from a public and private sources. Commercial income includes rent from accommodation, catering, conference business, sports and other trading activities.

The University receives a small amount of capital grant from government sources, with the balance of capital spending funded out of retained cash or external financing. In recent years the University has consciously managed both income and expenditure to increase the cash surplus of the University and this has been used to finance the current capital projects.

University Estate Developments

The University has invested in several estate developments across its Colchester and Southend campuses over recent years. The key developments at the Colchester campus are presented in the following.

- The £21 million Silberrad Student Centre for student services opened in summer 2015. It provides all services regarding accommodation, payments, registration and student welfare under one roof. Further facilities include an integrated learning centre for creative and group working; new IT facilities; a state-of-the-art media centre; a 24-hour postgraduate study area; and further study and library spaces

- A £26 million extension to the Albert Sloman Library also opened in summer 2015 providing 388 new study spaces, a new 24/7 postgraduate reading room as well as a collection of 1.4 million books.

- Essex Business School has relocated to a new £21m eco-friendly building, which is located next to the Knowledge Gateway research park. The building features contemporary facilities including a lecture theatre, dedicated space for MBA students as well as flexible group learning and ICT spaces.

- The Knowledge Gateway is a science and learning park which will be developed at the northern end of the campus. The development is expected to create circa 2,000 jobs and co-locate businesses and learning in an advanced science park intrinsically linked to the academic life of the University, building on the existing R&D work taking place at Parkside.

University Residences Strategy

As a campus based University, adequate provision of student residential accommodation on campus is fundamental in supporting the academic mission. Research shows that the accommodation offer is one of the most important decision influencers outside of academic choice, for prospective students choosing which University to study at.

As a growing University, it is of paramount importance that the number of bed spaces available on campus is in keeping with the pace of growth in student numbers. The current University strategic plan 2014-2019 aims to grow student numbers by 50% to 15,000, which will be achieved / exceeded by the end of the period. There is an emerging aspiration to further grow student numbers from 15,000 to 20,000 between the period 2019-2025. An additional 642 bed spaces were created by ProjectCo pursuant to the Project Agreement to satisfy part of the growth in demand within the current strategic plan period, with the remainder of supply coming from the proposed development of 643 bed spaces planned for completion by September 2018. This will increase stock to a total of 4,750 bed spaces at Colchester campus. It is anticipated that up to 2,000 further additional spaces will be required by 2025, to satisfy demand from growth in student numbers.

The strategy on total bed spaces is based around meeting the demand from 'priority' student groups. Providing on campus accommodation for all students in their first year of study is critical to recruitment and retention. In order to retain a competitive advantage for international student recruitment, the University also aims to provide on campus accommodation for international students throughout all years of study. It is not a specific aim of the University to generate on campus provision to satisfy demand from returning students (other than international students). Although there is large scale demand for on campus accommodation from returning student groups, it is deemed too risky a strategy to generate provision, based on demand from both new and returning students, with no guarantee of future demand.

Providing a range of accommodation to meet the varying student needs is a key area of focus. A steady range of price points is the most important factor, in line with demand for different accommodation types. Demand analysis is undertaken annually, in order to shape price point and room type requirements for the future. Research and benchmarking is undertaken annually to assess needs and demand for accommodation types that are not currently provided.

Design led refurbishments are key to enhancing existing accommodation stock, in order to provide a competitive advantage and keep pace with student expectation, and enhance the student experience.

Service provision is of paramount importance, in order to retain and improve the position as one of the leading Universities for student accommodation, through the national student housing survey.

Value for money brings together all elements of the strategy. The University aims to optimise the perception of value for money from student residents, via location, accommodation type, accommodation quality, service provision and price point.

TAXATION

United Kingdom Taxation

The following is a summary of the Issuer's understanding of the United Kingdom withholding taxation treatment at the date hereof in relation to payments of principal and interest in respect of the Bonds. The comments also summarise the Issuer's understanding of certain other United Kingdom tax aspects of acquiring, holding or disposing of Bonds. The comments relate only to the position of investors who are absolute beneficial owners of the Bonds and do not apply to the Issuer if it holds any Bonds. The following is a general guide and is based on current UK law and what is understood to be current H.M. Revenue & Customs practice (which may not be binding), both of which are subject to change (potentially with retrospective effect), should be treated with appropriate caution and may not apply to certain classes of Bondholders who are subject to special rules. Bondholders, Receiptholders or Couponholders who are in any doubt as to their tax position should consult their professional advisers.

Bondholders, Receiptholders or Couponholders who may be liable to taxation in jurisdictions other than the United Kingdom in respect of their acquisition, holding or disposal of the Bonds are particularly advised to consult their professional advisers as to whether they might be so liable (and if so under the laws of which jurisdictions), since the following comments relate only to certain United Kingdom taxation aspects of payments in respect of the Bonds. In particular, Bondholders, Receiptholders and Couponholders should be aware that they may be liable to taxation under the laws of other jurisdictions in relation to payments in respect of the Bonds even if such payments may be made without withholding or deduction for or on account of taxation under the laws of the United Kingdom.

1. UK Withholding Tax on UK Source Interest

The Bonds issued by the Issuer will constitute "quoted Eurobonds" provided they are and continue to be listed on a recognised stock exchange within the meaning of section 1005 of the Income Tax Act 2007. The Irish Stock Exchange is a recognised stock exchange for these purposes and this condition should be satisfied so long as the Bonds are and remain both: (i) officially listed in accordance with provisions applicable to the Irish Stock Exchange; and (ii) admitted to trading on the Irish Stock Exchange. Whilst the Bonds are and continue to be quoted Eurobonds, payments of interest on the Bonds may be made without withholding or deduction for or on account of United Kingdom income tax.

Interest on the Bonds may also be paid without withholding or deduction on account of United Kingdom tax where interest on the Bonds is paid by a company and, at the time the payment is made, the Issuer reasonably believes (and any person by or through whom interest on the Bonds is paid reasonably believes) that the beneficial owner is a company within the charge to United Kingdom corporation tax as regards the payment of interest (the "**Excepted Payments Exemption**"), provided that H.M. Revenue & Customs has not given a direction (in circumstances where it has reasonable grounds to believe that it is likely that the above exemption is not available in respect of such payment of interest at the time the payment is made) that the interest should be paid subject to a deduction of tax.

In other cases, interest on the Bonds may fall to be paid under deduction of United Kingdom income tax at the basic rate (currently 20 per cent.) subject to such relief as may be available under the provisions of any applicable double taxation treaty.

Interest on the Bonds will have a United Kingdom source and accordingly may be chargeable to United Kingdom tax by direct assessment on the Bondholder, Receiptholder or Couponholder. Where the interest is paid without withholding or deduction in respect of tax, the interest will not be subject to United Kingdom tax in the hands of Bondholders, Receiptholders or Couponholders who are not resident in the United Kingdom, except where such persons carry on a trade, profession or vocation in the United Kingdom through a United Kingdom branch or agency (or, in the case of corporate Bondholders, Receiptholders or Couponholders, through a United Kingdom permanent establishment) in connection with which the interest is received or to which the Bonds are attributable, in which case (subject to exemptions for interest received by certain categories of agent) United Kingdom tax may be levied on the United Kingdom branch or agency or permanent establishment.

2. **Payments by AGE and AGM under the Financial Guarantees**

If AGE and/or AGM make any payments in respect of interest on the Bonds (or other amounts due under the Bonds other than the repayment of amounts subscribed for the Bonds) such payments may be subject to United Kingdom withholding tax subject to any available exemptions and such relief as may be available under the provisions of any applicable double taxation treaty. Such payments by AGE and AGM may not be eligible for the quoted Eurobond exemption or the Excepted Payments Exemption described above.

3. **Provision of Information**

Certain persons (including persons in the United Kingdom paying interest to, or receiving interest on behalf of, another person) may be required to provide certain information to H.M. Revenue & Customs regarding the identity of the payee or the person entitled to the interest. In certain circumstances, such information may be exchanged with tax authorities in other countries

4. **Other Rules Relating to United Kingdom Withholding Tax**

Where interest has been paid under deduction of United Kingdom income tax, Bondholders, Receiptholders or Couponholders who are not resident in the United Kingdom may be able to recover all or part of the tax deducted if there is an appropriate provision in any applicable double taxation treaty.

The references to "interest" in this withholding tax summary mean "interest" as understood in United Kingdom tax law. The statements above do not take any account of any different definitions of "interest" or "principal" which may prevail under any other law or which may be created by the terms and conditions of the Bonds or any related documentation.

The above description of the United Kingdom withholding tax position assumes that there will be no substitution of the Issuer as principal obligor under the Bonds and does not consider the tax consequences of any such substitution.

5. **Stamp Duty and Stamp Duty Reserve Tax**

No United Kingdom stamp duty or stamp duty reserve tax should be payable on the issue or transfer of a Bond.

Republic of Ireland Taxation

The following is a summary of the Irish withholding tax treatment of the Bonds. The summary does not purport to be a comprehensive description of all of the Irish tax considerations that may be relevant to a decision to purchase, own or dispose of the Bonds.

The summary is based upon the laws of Ireland and the published practices of the Revenue Commissioners of Ireland as in effect on the date hereof. Prospective investors in the Bonds should consult their own advisers as to the Irish or other tax consequences of the purchase, beneficial ownership and disposition of the Bonds including, in particular, the effect of any state or local law taxes, if applicable.

1. **Irish Withholding Tax**

Irish withholding tax applies to certain payments including payments of:

(a) Irish source yearly interest (yearly interest is interest that is capable of arising for a period in excess of one year);

(b) Irish source annual payments (annual payments are payments that are capable of being made for a period in excess of one year and are pure income-profit in the hands of the recipient); and

(c) Distributions (including interest that is treated as a distribution under Irish law) made by companies that are resident in Ireland for the purposes of Irish tax;

at the standard rate of income tax (currently 20 per cent).

On the basis that the Issuer is not resident in Ireland for the purposes of Irish tax, nor does the Issuer operate in Ireland through a branch or agency with which the issue of the Bonds is connected, nor are the Bonds held in Ireland through a depository or otherwise located in Ireland, then to the extent that payments of interest or annual payments arise on the Bonds, such payments should not be regarded as payments having an Irish source for the purposes of Irish taxation.

Accordingly, the Issuer or any paying agent acting on behalf of the Issuer should not be obliged to deduct any amount on account of these Irish withholding taxes from payments made in connection with the Bonds.

Separately, for as long as the Bonds are quoted on a stock exchange, a purchaser of the Bonds should not be obliged to deduct any amount on account of Irish tax from a payment made by it in connection with the purchase of the Bonds.

2. **Irish Encashment Tax**

Payments on any Bonds paid by a paying agent in Ireland or collected or realised by an agent in Ireland acting on behalf of the beneficial owner of Bonds will be subject to Irish encashment tax at the standard rate of Irish tax (currently 20 per cent), unless it is proved, on a claim made in the required manner to the Revenue Commissioners of Ireland, that the beneficial owner of the Bonds entitled to the interest or distribution is not resident in Ireland for the purposes of Irish tax and such interest or distribution is not deemed, under the provisions of Irish tax legislation, to be income of another person that is resident in Ireland.

SUBSCRIPTION AND SALE

Subscription

TradeRisks Limited (the "**Manager**") has, in a subscription agreement dated the date of this Prospectus (the "**Subscription Agreement**") between it, the Issuer, HoldCo, ProjectCo, AGE and AGM upon the terms and subject to the conditions contained therein, agreed to subscribe and pay for the Bonds at the issue price of 100 per cent. of their principal amount less an arrangement fee. In addition, such amount as may be agreed in writing between the Issuer and the Manager in respect of guarantee fees payable to the Financial Guarantors may be deducted by the Manager from the issue price and paid by the Manager, on behalf of the Issuer, to AGE and AGM. The Issuer has also agreed to reimburse the Manager for certain of its expenses incurred in connection with the management of the issue of the Bonds. The Manager is entitled in certain circumstances to be released and discharged from its obligations under the Subscription Agreement prior to the closing of the issue of the Bonds.

Except for the fees payable to the Manager and to the Financial Guarantors and save as otherwise disclosed in this Propectus, no person has any interest, including conflicting interests, that are material to the issue of the Bonds.

Selling Restrictions — United States

The Bonds, the Obligor Guarantees and the Financial Guarantees have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act. Terms used in this paragraph have the meanings given to them by Regulation S of the Securities Act ("**Regulation S**").

The Bonds are subject to U.S. tax law requirements and may not be offered, sold or delivered within the United States or its possessions or to a United States person, except in certain transactions permitted by U.S. tax regulations. Terms used in this paragraph have the meanings given to them by the United States Internal Revenue Code of 1986 and regulations thereunder.

The Manager has agreed that, except as permitted by the Subscription Agreement, it will not offer, sell or deliver the Bonds, the Obligor Guarantees and the Financial Guarantees (a) as part of their distribution at any time or (b) otherwise, until 40 days after the later of the commencement of the offering and the issue date of the Bonds, within the United States or to, or for the account or benefit of, a U.S. person, and that it will have sent to each dealer to which it sells Bonds, the Obligor Guarantees and the Financial Guarantees during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Bonds, the Obligor Guarantees and the Financial Guarantees within the United States or to, or for the account or benefit of, U.S. persons. Terms used in this paragraph have the meanings given to them by Regulation S.

In addition, until 40 days after commencement of the offering of the Bonds, the Obligor Guarantees and the Financial Guarantees, an offer or sale of Bonds, the Obligor Guarantees or the Financial Guarantees within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with an available exemption from registration under the Securities Act.

Selling Restrictions — United Kingdom

The Manager has represented and agreed that:

(i) it has only communicated or caused to be communicated, and will only communicate or cause to be communicated, any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act ("**FSMA**") received by it in connection with the issue or sale of any Bonds in circumstances in which section 21(1) of the FSMA does not apply to the Issuer or the Financial Guarantors; and

(ii) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Bonds in, from or otherwise involving the United Kingdom.

Selling Restrictions — General

No action has been or will be taken in any jurisdiction by the Issuer or the Manager that would, or is intended to, permit a public offering of the Bonds, or possession or distribution of this Prospectus or any other offering material, in any country or jurisdiction where action for that purpose is required. The Manager has undertaken that it will comply (to the extent of its knowledge and belief) with all applicable securities, laws and regulations in each country or jurisdiction in which it purchases, offers, sells or delivers Bonds or has in its possession or distributes the Prospectus. Persons into whose hands this Prospectus comes are required by the Issuer and the Manager to comply with all applicable laws and regulations in each country or jurisdiction in which they purchase, offer, sell or deliver Bonds or have in their possession, distribute or publish this Prospectus or any other offering material relating to the Bonds, in all cases at their own expense.

Attention is also drawn to the information set out in the section entitled "*Important Notice*" above.

GENERAL INFORMATION

1. The creation and issue of the Bonds has been authorised by a resolution of the Board of Directors of the Issuer dated 17 February 2017.

2. AGE has obtained all necessary consents, approvals and authorisations in connection with the issue and performance of the AGE Financial Guarantee.

3. AGM has obtained all necessary consents, approvals and authorisations in connection with the issue and performance of the AGM Financial Guarantee.

4. There has been no significant change in the financial or trading position of the Issuer and no material adverse change in the prospects of the Issuer since its date of incorporation.

5. There has been no significant change in the financial or trading position of ProjectCo, and no material adverse change in the prospects of ProjectCo since the date of its incorporation.

6. There has been no significant change in the financial or trading position of HoldCo and its subsidiaries and no material adverse change in the prospects of HoldCo and its subsidiaries since the date of its incorporation.

7. The Issuer is not, and has not been, involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which it is aware) which may have, or have had during the 12 months prior to the date of this Prospectus, a significant effect on its financial position or profitability.

8. HoldCo and its subsidiaries are not, and have not been, involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which it is aware) which may have, or have had during the 12 months prior to the date of this Prospectus, a significant effect on its financial position or profitability.

9. ProjectCo is not, and has not been, involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which it is aware) which may have, or have had during the 12 months prior to the date of this Prospectus, a significant effect on its financial position or profitability.

10. The auditors of the Issuer, HoldCo and ProjectCo are Grant Thornton UK LLP, a member firm of the Institute of Chartered Accountants in England and Wales. No audited accounts have been prepared in relation to the Issuer or ProjectCo.

11. For as long as the Prospectus remains in effect or any Bonds shall be outstanding, copies of the following documents may be inspected in physical and/or electronic form during normal business hours at the offices of the Principal Paying Agent at its specified office, currently at One Canada Square, London E14 5AL:

    (i) articles of association of each of the Issuer, Holdco and ProjectCo;

    (ii) articles of association of AGE;

    (iii) by-laws of AGM;

    (iv) prior to the Issue Date, drafts (subject to notification) of and after the Issue Date:

        (A) the Finance Documents;

        (B) the AGE Financial Guarantee;

        (C) the AGM Financial Guarantee;

        (D) the Collateral Deed; and

        (E) The Bond Trust Deed;

(v) audited financial statements of AGE for the financial years ended 31 December 2014 and 31 December 2015;

(vi) audited financial statements of AGM for the financial years ended 31 December 2014 and 31 December 2015 and the unaudited interim financial statements dated 30 September 2016;

(vii) the Demand Report.

12. The Bonds and any Receipts, Coupons and Talons appertaining thereto will bear a legend to the following effect: "Any United States person (as defined in the Internal Revenue Code) who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in section 165(j) and 1287(a) of the Internal Revenue Code".

13. The Bonds have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The ISIN of the Bonds is XS1558478597 and the common code of the Bonds is 155847859.

14. It is expected that the Bonds will be admitted to the Official List and admitted to trading on the Irish Stock Exchange on or about 24 February 2017, subject only to the issue of each Temporary Global Bond and to the execution by AGE of the AGE Financial Guarantee and AGM of the AGM Financial Guarantee.

15. The total estimated expenses to be paid by the Issuer in relation to the admission to trading are approximately €6,641.20 exclusive of VAT.

16. Past and further performance information of the Index can be found at http://www.ons.gov.uk/ons/guide-method/user-guidance/prices/index.html.

17. Save for the Bondholder Report, the Issuer does not intend to provide any post-issuance information.

18. C&W, global commercial property consultants of 125 Old Broad Street, London, England, EC2N 1AR, has given and not withdrawn its written consent to the inclusion in this document of its demand report which is set out in Appendix 8 in the form and context in which it is included. C&W was engaged to produce that report under an appointment which obliged C&W to exercise all reasonable professional skill, care and diligence in its production. C&W's consent to the disclosure of the report is not, however, intended to create, and C&W does not accept, any duty of care to any recipient of this Prospectus. C&W has no material interest in the Issuer.

19. Any websites referred to herein do not form part of this Prospectus.

APPENDIX 1

2015 FINANCIAL STATEMENTS OF ASSURED GUARANTY (EUROPE) LTD.

Assured Guaranty (Europe) Ltd.
(an indirect wholly-owned subsidiary of
Assured Guaranty Ltd.)
Consolidated Financial Statements
December 31, 2015 and 2014

(Expressed in U.S. Dollars)

FINANCIAL STATEMENTS
ASSURED GUARANTY (EUROPE) LTD.

Independent Auditor's Report

To the Board of Directors of Assured Guaranty (Europe) Ltd.:

We have audited the accompanying consolidated financial statements of Assured Guaranty (Europe) Ltd. (the "Company"), which comprise the consolidated balance sheets as of December 31, 2015 and December 31, 2014, and the related consolidated statements of operations and comprehensive income, 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.

Auditor's 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 (Europe) Ltd. at December 31, 2015 and December 31, 2014, 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
July 21, 2016

Assured Guaranty (Europe) Ltd.

Consolidated Balance Sheets

(dollars in thousands except per share and share amounts)

	As of December 31,	
	2015	**2014**
Assets		
Investment portfolio:		
Fixed maturity securities, available-for-sale, at fair value (amortized cost of $288,483 and $277,224)	$ 269,714	$ 274,500
Short term investments, at fair value	112	14,675
Total investment portfolio	269,826	289,175
Cash	15,091	16,790
Premiums receivable	298,361	306,336
Ceded unearned premium reserve	680,834	746,620
Reinsurance recoverable on unpaid losses	36,040	47,219
Credit derivative assets	5,834	6,869
Deferred tax asset, net	38,997	36,220
Current income tax receivable	2,002	1,396
Other assets	4,151	4,341
Total assets	**$ 1,351,136**	**$ 1,454,966**
Liabilities and shareholder's equity		
Unearned premium reserve	$ 660,763	$ 726,672
Loss and loss adjustment expense reserve	36,569	47,909
Ceded reinsurance balances payable	205,265	210,637
Credit derivative liabilities	5,998	7,479
Deferred ceding commissions, net	170,868	180,382
Other liabilities	9,727	10,055
Total liabilities	**1,089,190**	**1,183,134**
Commitments and contingencies (See Note 14)		
Common stock (500,000,000 shares authorized; 55,000,000 issued and outstanding; par value of £1 each)	81,206	81,206
Additional paid-in capital	118,634	118,634
Retained earnings	74,305	73,762
Accumulated other comprehensive income (loss), net of tax of $(6,569) and $(953)	(12,199)	(1,770)
Total shareholder's equity	**261,946**	**271,832**
Total liabilities and shareholder's equity	**$ 1,351,136**	**$ 1,454,966**

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

Assured Guaranty (Europe) Ltd.

Consolidated Statements of Operations and Comprehensive Income

(in thousands)

	Year Ended December 31,	
	2015	2014
Revenues		
Net earned premiums	$ 1,258	$ (352)
Net investment income	6,597	7,395
Net realized investment gains (losses):		
Other-than-temporary impairment losses	(3,489)	(3,317)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	—	—
Net impairment loss	(3,489)	(3,317)
Other net realized investment gains (losses)	(203)	2,558
Net realized investment gains (losses)	(3,692)	(759)
Net change in fair value of credit derivatives:		
Realized gains (losses) and other settlements	188	362
Net unrealized gains (losses)	597	580
Net change in fair value of credit derivatives	785	942
Other income (loss)	(6,329)	13,529
Total revenues	(1,381)	20,755
Expenses		
Loss and loss adjustment expenses	(161)	(76)
Amortization of deferred ceding commissions	(19,362)	(13,020)
Other operating expenses	15,912	15,192
Total expenses	(3,611)	2,096
Income (loss) before income taxes	2,230	18,659
Provision (benefit) for income taxes:		
Current	(1,153)	(15,620)
Deferred	2,840	22,166
Total provision (benefit) for income taxes	1,687	6,546
Net income (loss)	**543**	**12,113**
Unrealized holding gains (losses) arising during the period on:		
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $(5,665) and $(1,458)	(10,522)	(2,707)
Investments with other-than-temporary impairment, net of tax provision (benefit) of $(1,243) and $(1,335)	(2,307)	(2,478)
Unrealized holding gains (losses) arising during the period, net of tax	(12,829)	(5,185)
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $(1,292) and $(266)	(2,400)	(493)
Other comprehensive income (loss)	(10,429)	(4,692)
Comprehensive income (loss)	**$ (9,886)**	**$ 7,421**

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

Assured Guaranty (Europe) Ltd.

Consolidated Statements of Shareholder's Equity

Years Ended December 31, 2015 and 2014

(dollars in thousands, except shares)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholder's Equity
	Shares	Amount				
Balance at December 31, 2013	55,000,000	$ 81,206	$ 118,634	$ 61,649	$ 2,922	$ 264,411
Net income	—	—	—	12,113	—	12,113
Other comprehensive loss	—	—	—	—	(4,692)	(4,692)
Balance at December 31, 2014	**55,000,000**	**$ 81,206**	**$ 118,634**	**$ 73,762**	**$ (1,770)**	**$ 271,832**
Net income	—	—	—	543	—	543
Other comprehensive loss	—	—	—	—	(10,429)	(10,429)
Balance at December 31, 2015	**55,000,000**	**$ 81,206**	**$ 118,634**	**$ 74,305**	**$ (12,199)**	**$ 261,946**

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

Assured Guaranty (Europe) Ltd.

Consolidated Statements of Cash Flows

(in thousands)

	Year Ended December 31,	
	2015	2014
Operating Activities:		
Net Income	$ 543	$ 12,113
Adjustments to reconcile net income to net cash flows provided by (used in) operating activities:		
Net amortization of premium (discount) on investments	3,014	2,524
Net realized investment losses (gains)	3,692	759
Provision (benefit) for deferred income taxes	2,840	22,166
Net unrealized losses (gains) on credit derivatives	(597)	(580)
Change in premiums receivable, net of premiums payable and commissions	2,603	12,123
Change in deferred ceding commissions, net	(9,514)	(2,681)
Change in ceded unearned premium reserve	65,786	18,976
Change in loss and loss adjustment expense reserve, net	(161)	(77)
Change in unearned premium reserve	(65,909)	(40,355)
Other changes in credit derivative assets and liabilities, net	151	(3,844)
Change in current income tax	(606)	1,067
Other	168	1,444
Net cash flows provided by (used in) operating activities	**2,010**	**23,635**
Investing activities		
Fixed-maturity securities:		
Purchases	(41,255)	(79,605)
Sales	12,204	28,348
Maturities	11,656	21,713
Net sales (purchases) of short-term investments	13,990	(8,254)
Net cash flows provided by (used in) investing activities	**(3,405)**	**(37,798)**
Net cash flows provided by (used in) financing activities	—	—
Effect of foreign exchange rate changes	(304)	(1,532)
Increase (decrease) in cash	(1,699)	(15,695)
Cash at beginning of period	16,790	32,485
Cash at end of period	**$ 15,091**	**$ 16,790**
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$ (547)	$ (16,688)

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

1. Business and Basis of Presentation

Business

Assured Guaranty (Europe) Ltd. ("AGE" or the "Company") is an insurance company organized in the United Kingdom ("U.K.") and authorized by the U.K. Prudential Regulation Authority (the "U.K. PRA") to transact the following classes of insurance: 14 (credit), 15 (suretyship) and 16 (miscellaneous financial loss). AGE is also currently permitted on a passport basis to conduct insurance business in certain member countries of the European Economic Area ("EEA") from its home office in the U.K., although this may change in the future as a result of the referendum held in the U.K. on June 23, 2016, in which a majority voted to exit the European Union ("EU"), known as "Brexit". The principal activity of AGE is providing financial guarantees for the international public finance (including infrastructure) market and, with the approval of the U.K. PRA, the asset-backed and other structured finance market.

For transactions closed prior to 2011, the Company typically guaranteed obligations directly and reinsured to its parent company, Assured Guaranty Municipal Corp. ("AGM"), approximately 92% of the Company's retention, after cessions to other reinsurers, under a quota share agreement (for additional details, refer to Note 13, Related Party Transactions). In 2011, the Company implemented a co-guarantee structure pursuant to which the Company directly guarantees a portion of the guaranteed obligations in an amount equal to what would have been the Company's pro rata retention percentage under the quota share agreement. AGM directly guarantees the remaining balance of the guaranteed obligations and also provides a second-to-pay guarantee for the Company's portion of the guaranteed obligations.

More specifically, management and the U.K. PRA have agreed that any new business written by AGE will be guaranteed using a co-insurance structure pursuant to which AGE will co-insure public finance transactions with AGM and structured finance transactions with its affiliate Assured Guaranty Corp. ("AGC"). AGE must obtain the approval of the U.K. PRA before it can guarantee any new structured finance transaction. AGE's financial guarantee will cover a proportionate share (expected to be approximately 3 to 10%) of the total exposure, and AGM or AGC, as the case may be, will guarantee the remaining exposure under the transaction (subject to compliance with EEA licensing requirements). AGM or AGC, as the case may be, will also issue a second-to-pay guarantee to cover AGE's financial guarantee.

AGE applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guarantees that protect holders of debt instruments and other monetary obligations from defaults in scheduled payments, including scheduled interest and principal payments ("Debt Service"). AGE markets its financial guarantees directly to issuers and underwriters of securities as well as to investors in such obligations. Financial guarantees provide an unconditional and irrevocable guaranty that protects the holder of a financial obligation against non-payment of Debt Service when due. Upon an obligor's default on scheduled Debt Service payments due on the obligation, AGE is required under the financial guarantee to pay the principal or interest shortfall.

In the past, AGE had sold credit protection by issuing financial guarantees that guaranteed payment obligations of Assured Guaranty Credit Protection Ltd. ("AGCPL") and former affiliates under credit derivatives, primarily credit default swaps ("CDS"). Financial guaranty contracts accounted for as credit derivatives are generally structured such that the circumstances giving rise to AGE's obligation to make loss payments are similar to those for financial guaranty insurance contracts. AGE's credit derivative transactions are governed by International Swaps and Derivative Association, Inc. ("ISDA") documentation.

AGE has not guaranteed any new CDS under which credit protection has been sold since 2008. AGE actively pursues opportunities to terminate existing CDS, which have the effect of reducing future fair value volatility in income and/or reducing rating agency capital charges.

The Company is evaluating the impact on its business of Brexit. Negotiations are expected to commence soon to determine the future terms of the U.K.'s relationship with the EU, including the terms of trade between the U.K. and the EU. Brexit may impact laws, rules and regulations applicable to the Company and its U.K. operations. Depending on the terms of Brexit, the Company may lose the ability to insure new transactions from London in non-U.K. EU and EEA countries without obtaining additional licenses, which may require a presence in another EU country. Brexit-related changes in laws and

regulations may also adversely affect the Company's surveillance and loss mitigation activities with respect to existing insured transactions in non-U.K. EU and EEA countries, especially to the extent Brexit inhibits the issuance of new guaranties in distressed situations. Brexit may also impact laws, rules and regulations applicable to U.K. entities with obligations insured by the Company and could adversely impact the ability of non-U.K. EU or EEA citizens to continue to be employed at the Company in London. The Company cannot predict the direction Brexit-related developments will take or the impact of those developments on the economies of the markets the Company serves, and Brexit-related developments may materially adversely affect the Company's business, results of operations and financial condition.

Corporate Structure

The ultimate parent of AGE is Assured Guaranty Ltd. ("AGL" and, together with its subsidiaries, "Assured Guaranty"). AGL is a Bermuda-based holding company that provides, through its operating subsidiaries, credit protection products to the public finance, infrastructure and structured finance markets in the EEA, the United States ("U.S."), and in other jurisdictions around the world.

In July 2013, as part of a series of transactions that AGL completed to increase the capitalization of one of the Company's affiliates, Municipal Assurance Corp. ("MAC"), to $800 million on a statutory basis, Assured Guaranty Municipal Insurance Company ("AGMIC") was merged into AGM, with AGM as the surviving company. Up to that point, AGMIC was the immediate parent company of AGE.

Solvency II Directive

The Company has invested significant financial and management resources into complying with the requirements established by the European Union's "Solvency II" directive (Directive 2009/138/EC). The Company intends to use the Standard Formula, which was developed by the European Insurance and Occupational Pensions Authority under the direction of the European Commission, for the calculation of its Solvency Capital Requirement. Solvency II was adopted on January 1, 2016.

Prior to the adoption of Solvency II, the Company was required to assess and manage the risks to which it is exposed and to make an assessment of its capital needs - referred to as an individual capital assessment or "ICA" - and to supplement that ICA model with a level of capital determined by reference to a "financial guarantee benchmark" capital adequacy model ("Benchmark Model"). Beginning 1 January 2016, with the approval of the Prudential Regulation Authority (the "U.K. PRA"), the Company no longer uses the Benchmark Model and instead uses only the ICA model. Should the level of capital at the Company fall below the capital requirement as indicated by the ICA model, the U.K. PRA may issue individual capital guidance setting out the level of capital the U.K. PRA believes the Company should maintain, which may be in excess of that required by the ICA model.

Basis of Presentation

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") and, in the opinion of management, reflect all adjustments that are of a normal recurring nature necessary for a fair statement of the financial condition, results of operations and cash flows of the Company for the periods presented. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The consolidated financial statements include the accounts of AGE and its affiliate, AGCPL. Intercompany accounts and transactions between the consolidated entities have been eliminated. Certain prior year balances have been reclassified to conform to the current year's presentation.

Significant Accounting Policies

The Company's functional currency is the U.S. dollar. The Company revalues assets, liabilities, revenue and expenses denominated in non-U.S. currencies into U.S. dollars using applicable exchange rates and reports related gains and losses in the consolidated statement of operations. Monetary assets and liabilities denominated in foreign currencies are translated at the spot rate at the balance sheet date. Non-monetary assets and liabilities are recorded at historical rates. Revenues and expenses denominated in foreign currencies are translated at average rates prevailing during the year.

The chief operating decision maker manages the operations of the Company at a consolidated level. Therefore, all results of operations are reported as one segment.

Other significant accounting policies are included in the following notes.

Significant Accounting Policies

Expected loss to be paid (insurance and credit derivatives)	Note 4
Financial guaranty insurance (premium revenue recognition, loss and loss adjustment expense and policy acquisition cost)	Note 5
Fair value measurement	Note 6
Credit derivatives (at fair value)	Note 7
Variable interest entities	Note 8
Investments and cash	Note 9
Income taxes	Note 11

Future Application of Accounting Standards

Credit Losses on Financial Instruments

In June 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The amendments in this ASU are intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The ASU requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions will use forward-looking information to better inform their credit loss estimates as a result of the ASU. While many of the loss estimation techniques applied today will still be permitted, the inputs to those techniques will change to reflect the full amount of expected credit losses. The ASU requires enhanced disclosures to help investors and other financial statement users to better understand significant estimates and judgments used in estimating credit losses, as well as credit quality and underwriting standards of an organization’s portfolio.

In addition, the ASU amends the accounting for credit losses on available-for-sale securities and purchased financial assets with credit deterioration. The ASU makes targeted improvements eliminates the concept of “other than temporary” impairment model for certain available-for-sale debt securities to eliminate the concept of “other than temporary” from that model. Accordingly, the ASU states that an entity must use an allowance approach, must limit the allowance to an amount at which the security’s fair value is less than its amortized cost basis, may not consider the length of time fair value has been less than amortized cost, and may not consider recoveries in fair value after the balance sheet date when assessing whether a credit loss exists. For purchased financial assets with credit deterioration, the ASU requires an entity’s method for measuring credit losses to be consistent with its method for measuring expected losses for originated and purchased non-credit-deteriorated assets.

The ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. For most debt instruments, 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 and changes to purchased financial assets with credit deterioration are to be applied prospectively. For the Company, this would be as of January 1, 2020. Early adoption is permitted for fiscal years, and interim periods with those fiscal years, beginning after December 15, 2018. The Company is currently evaluating the effect of adopting this ASU on its Consolidated Financial Statements.

Leases

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-02, *Leases (Topic 842)*. This ASU requires lessees to present right-of-use assets and lease liabilities on the balance sheet. ASU 2016-02 is to be applied using a modified retrospective approach at the beginning of the earliest comparative period in the financial statements. The ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The Company is evaluating the impact that this ASU will have on its Consolidated Financial Statements.

Financial Instruments

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments - Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities*. The amendments in this ASU are intended to make targeted improvements to GAAP by addressing certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. One of the amendments pertains to liabilities that an entity has elected to measure at fair value in accordance with the fair value option for financial instruments. For these liabilities, the portion of fair value change related to credit risk will be separately presented in other comprehensive income ("OCI"). Currently, the entire change in the fair value of these liabilities is reflected in the income statement.

The ASU is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Entities will be required to record a cumulative-effect adjustment to the statement of financial position as of the beginning of the fiscal year in which the guidance is adopted. For the Company, this would be as of January 1, 2018. Early adoption is permitted only for the amendment related to the change in presentation of financial liabilities that are fair valued using the fair value option. The Company is currently evaluating the effect of adopting this ASU on its Consolidated Financial Statements.

Short Duration Insurance Contracts

In May 2015, the FASB issued ASU 2015-09, *Financial Services - Insurance (Topic 944) - Disclosures about Short-Duration Contracts.* The primary objective of this ASU is to improve disclosures for insurance entities which issue short-duration contracts. The ASU 2015-09 will have no impact on the Company's financial statement disclosures. The ASU is effective for annual periods beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016.

Consolidation

In February 2015, the FASB issued ASU No. 2015-02, Consolidation *(Topic 810): Amendments to the Consolidation Analysis*, which is intended to improve certain areas of consolidation guidance for legal entities such as limited partnerships, limited liability companies, and securitization structures. The ASU will be effective on January 1, 2016. Early adoption is permitted, including adoption in an interim period. The Company does not expect that ASU 2015-02 will have an effect on its Consolidated Financial Statements.

2. Rating Actions

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

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 drop its rating of the Company or that another rating agency add a rating of the Company.

In the last several years, S&P Global Ratings ("S&P") and Moody's Investors Service, Inc. ("Moody's") have changed, multiple times, their financial strength rating of AGE, or changed the outlook on such rating. The rating agencies' most recent actions related to AGE are:

- On June 29, 2015, S&P affirmed the AA (stable) financial strength rating of AGE.

- On December 8, 2015, Moody's published its credit opinions maintaining its existing insurance financial strength ratings of A2 (stable outlook) on AGE.

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

3. Outstanding Exposure

The Company's financial guaranty contracts are written in either insurance or credit derivative form, but collectively are considered financial guaranty contracts. The Company seeks to limit its exposure to losses by underwriting obligations that it views as investment grade at inception, diversifying its insured portfolio and maintaining rigorous subordination or collateralization requirements on structured finance obligations. The Company also has utilized reinsurance by ceding business to third-party and affiliated reinsurers.

Significant Risk Management Activities

Assured Guaranty's Portfolio Risk Management Committee, which includes members of senior management and senior credit and surveillance officers of the Company, sets specific risk policies and limits and is responsible for enterprise risk management, establishing the Company's risk appetite, credit underwriting of new business, surveillance and work-out.

As part of the surveillance process, the Company monitors trends and changes in transaction credit quality, detects any deterioration in credit quality, and recommends such remedial actions as may be necessary or appropriate. All transactions in the insured portfolio are assigned internal credit ratings, which are updated based on changes in transaction credit quality. The Company also develops strategies to enforce its contractual rights and remedies and to mitigate its losses, engage in negotiation discussions with transaction participants and, when necessary, manage the Company's litigation proceedings.

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 investment grade credits to determine whether any need to be internally downgraded to BIG and refreshes its internal credit ratings on individual credits in quarterly, semi-annual or annual cycles based on the Company's view of the credit's quality, loss potential, volatility and sector. Ratings on credits in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter.

Credits identified as BIG are subjected to further review to determine the probability of a loss. See Note 4, Expected Loss to be Paid for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. For surveillance purposes, the Company calculates present value using a discount rate of 5%. (A risk-free rate is used for calculating the expected loss for financial statement measurement purposes.)

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

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

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

- BIG Category 3: Below-investment-grade transactions for which future losses are expected and on which claims (other than liquidity claims) have been paid.

Components of Outstanding Exposure

Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding	
	December 31, 2015	December 31, 2014	December 31, 2015	December 31, 2014
	(in thousands)			
Public finance	$ 43,596,571	$ 49,944,212	$ 807,460	$ 943,568
Structured finance	658,607	1,322,887	14,753	30,549
Total financial guaranty	$ 44,255,178	$ 51,267,099	$ 822,213	$ 974,117

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

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2015

	Public Finance		Structured Finance		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
			(dollars in thousands)			
AAA	$ 50	0.0%	$ 3,315	24.8%	$ 3,365	0.8%
AA	—	—	1,295	9.7	1,295	0.3
A	90,559	23.0	2,028	15.2	92,587	22.8
BBB	288,824	73.5	5,584	41.8	294,408	72.4
BIG	13,726	3.5	1,132	8.5	14,858	3.7
Total net par outstanding	$ 393,159	100.0%	$ 13,354	100.0%	$ 406,513	100.0%

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2014

	Public Finance		Structured Finance		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
			(dollars in thousands)			
AAA	$ 68	0.0%	$ 10,913	39.1%	$ 10,981	2.4%
AA	7,958	1.8	8,743	31.3	16,701	3.6
A	100,509	23.1	2,432	8.7	102,941	22.2
BBB	311,932	71.6	4,564	16.4	316,496	68.3
BIG	15,034	3.5	1,256	4.5	16,290	3.5
Total net par outstanding	$ 435,501	100.0%	$ 27,908	100.0%	$ 463,409	100.0%

Financial Guaranty Portfolio
by Sector

Sector	As of December 31, 2015	As of December 31, 2014
	(in thousands)	
Public finance:		
Non-U.S. Public infrastructure finance	$ 210,156	$ 227,705
Non-U.S. Utility finance	132,989	153,019
Non-U.S. Municipal and other public finance	50,014	54,777
Total public finance	393,159	435,501
Structured finance:		
Non-U.S. Residential mortgage-backed security ("RMBS")	10,234	19,222
U.S. and non-U.S. Pooled corporate obligations	3,120	8,686
Total structured finance	13,354	27,908
Total net par outstanding	$ 406,513	$ 463,409

Actual maturities of insured obligations could differ from contractual maturities because borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties. The expected maturities of structured finance obligations are, in general, considerably shorter than the contractual maturities for such obligations.

Expected Amortization of
Net Par Outstanding
As of December 31, 2015

	(in thousands)
0 to 5 years	$ 34,653
5 to 10 years	54,427
10 to 15 years	36,433
15 to 20 years	56,705
20 years and above	224,295
Total net par outstanding	$ 406,513

Geographic Distribution of Net Par Outstanding

The Company seeks to maintain a diversified portfolio of insured obligations designed to spread its risk across a number of geographic areas.

Geographic Distribution of
Net Par Outstanding
As of December 31, 2015

	Number of Risks	Net Par Outstanding	Percent of Total Net Par Outstanding
		(dollars in thousands)	
Country			
United Kingdom	63	$ 272,705	67.1%
France	7	55,072	13.5
Italy	8	34,906	8.6
Japan	8	14,051	3.5
Spain	2	7,682	1.9
Hungary	2	6,544	1.6
Poland	1	6,255	1.5
Scotland	1	5,117	1.3
Germany	1	1,722	0.4
Mexico	1	928	0.2
Other	2	1,531	0.4
Total	96	$ 406,513	100.0%

Exposure to the Selected European Countries

Several European countries continue to experience significant economic, fiscal and/or political strains such that the likelihood of default on obligations with a nexus to those countries may be higher than the Company anticipated when such factors did not exist. The European countries where the Company has exposure and believes heightened uncertainties exist are: Hungary, Italy, Portugal and Spain (collectively, the “Selected European Countries”). The Company is closely monitoring its exposures in the Selected European Countries where it believes heightened uncertainties exist. The Company’s direct economic exposure to the Selected European Countries (based on par for financial guaranty contracts and notional amount for financial guaranty contracts accounted for as derivatives) is shown in the following table, net of ceded reinsurance.

Net Direct Economic Exposure to Selected European Countries(1)
As of December 31, 2015

	Hungary	Italy	Spain	Total
		(in thousands)		
Sub-sovereign exposure (2)	$ 5,412	$ 26,968	$ 7,393	$ 39,773
Non-sovereign exposure (3)	1,132	7,878	—	9,010
Total	$ 6,544	$ 34,846	$ 7,393	$ 48,783
Total BIG (See Note 4)	$ 6,544	$ —	$ 7,393	$ 13,937

(1) While the Company's exposures are shown in U.S. dollars, the obligations the Company insures are in various currencies, primarily Euros. One of the RMBS included in the table above includes residential mortgages in both Italy and Germany, and only the portion of the transaction equal to the portion of the original mortgage pool in Italian mortgages is shown in the table.

(2) Sub-sovereign exposure in Selected European Countries includes transactions backed by receivables from or supported by sub-sovereigns, which are governmental or government-backed entities other than the ultimate governing body of the country.

(3) Non-sovereign exposure in Selected European Countries includes debt of regulated utilities and RMBS.

When the Company directly insures an obligation, it assigns the obligation to a geographic location or locations based on its view of the geographic location of the risk.

The Company has excluded from the exposure tables above its indirect economic exposure to the Selected European Countries through policies it provides on pooled corporate transactions. The Company calculates indirect exposure to a country by multiplying the par amount of a transaction insured by the Company times the percent of the relevant collateral pool reported as having a nexus to the country. On that basis, the Company has calculated exposure of $0.4 million to Selected European Countries in transactions with $3 million of net par outstanding.

4. Expected Loss to be Paid

The insured portfolio includes policies accounted for under two separate accounting models depending on the characteristics of the contract. The Company has paid and expects to pay future losses on policies which fall under either of the two accounting models. The following provides a summarized description of the two accounting models prescribed by GAAP with a reference to the notes that describe the accounting policies and required disclosures throughout this report. The two models are insurance and derivatives.

In order to effectively evaluate and manage the economics and liquidity of the entire insured portfolio, management compiles and analyzes loss information for all policies on a consistent basis. The Company monitors and assigns ratings and calculates expected losses in the same manner for all its exposures regardless of form or differing accounting models.

This note provides information regarding expected claim payments to be made under all contracts in the insured portfolio. Net expected loss to be paid in the tables below consists of the present value of future: expected claim and loss adjustment expense ("LAE") payments, expected recoveries in the transaction structures, cessions to reinsurers, and other loss mitigation strategies. 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, regardless of the accounting model. Expected loss to be paid is an important measure used by management to analyze the net economic loss on all contracts.

Accounting Policy

Insurance Accounting

For contracts accounted for as financial guaranty insurance, loss and LAE reserve is recorded only to the extent and for the amount that expected losses to be paid exceed unearned premium reserve. As a result, the Company has expected loss to be paid that have not yet been expensed. Such amounts will be recognized in future periods as unearned premium reserve amortizes into income. Expected loss to be expensed is important because it presents the Company's projection of incurred losses that will be recognized in future periods (excluding accretion of discount). See "Financial Guaranty Insurance Losses" in Note 5, Financial Guaranty Insurance.

There were no expected loss to be paid for credit derivative contracts for 2015 and 2014. The expected loss to be paid in this note relates only to contracts accounted for as financial guaranty insurance.

Expected Loss to be Paid

The expected loss to be paid is equal to the present value of expected future cash outflows for claim and LAE payments, net of inflows for expected salvage and subrogation, using current risk-free rates. Net expected loss to be paid is defined as expected loss to be paid, net of amounts ceded to reinsurers.

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

Economic Loss Development

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

Loss Estimation Process

The Company’s loss reserve committees estimate expected loss to be paid for all contracts by reviewing analyses that consider various scenarios with corresponding probabilities assigned to them. Depending upon the nature of the risk, the Company's view of the potential size of any loss and the information available to the Company, that analysis may be based upon individually developed cash flow models, internal credit rating assessments and sector-driven loss severity assumptions or judgmental assessments. The Company monitors the performance of its transactions with expected losses and each quarter the Company’s loss reserve committees review and refresh their loss projection assumptions and scenarios and the probabilities they assign to those scenarios based on actual developments during the quarter and their view of future performance. The Company's estimate of ultimate losses on a policy is subject to significant uncertainty over the life of the insured transaction due to the potential for significant variability in credit performance as a result of economic, fiscal and financial market variability over the long duration of most contracts. The determination of expected loss to be paid is an inherently subjective process involving numerous estimates, assumptions and judgments.

The following tables present a roll forward of the present value of net expected loss to be paid for financial guaranty contracts by sector. The Company used weighted average risk-free rates that ranged from 0.0% to 1.48% as of December 31, 2015 and 0.0% to 1.50% as of December 31, 2014.

Net Expected Loss to be Paid
Roll Forward

	Year Ended December 31, 2015
	(in thousands)
Net expected loss to be paid, beginning of period	$ 912
Economic loss development due to:	
Accretion of discount	0
Changes in discount rates	(6)
Changes in timing and assumptions	(200)
Total economic loss development	(206)
Paid losses	—
Net expected loss to be paid, end of period	$ 706

Net Expected Loss to be Paid
Roll Forward by Sector
Year Ended December 31, 2015

	Net Expected Loss to be Paid as of December 31, 2014	Economic Loss Development	(Paid) Recovered Losses	Net Expected Loss to be Paid as of December 31, 2015
		(in thousands)		
Non-U.S. public finance	$ 878	$ (209)	$ —	$ 669
Other structured finance	34	3	—	37
Total	$ 912	$ (206)	$ —	$ 706

Net Expected Loss to be Paid,
Roll Forward by Sector
Year Ended December 31, 2014

	Net Expected Loss to be Paid as of December 31, 2013	Economic Loss Development	(Paid) Recovered Losses	Net Expected Loss to be Paid as of December 31, 2014
		(in thousands)		
Non-U.S. public finance	$ 997	$ (119)	$ —	$ 878
Other structured finance	19	15	—	34
Total	$ 1,016	$ (104)	$ —	$ 912

Certain Selected European Country Transactions

The Company guarantees credits with sub-sovereign exposure to various Spanish issuers where a Spanish sovereign default may cause the sub-sovereigns also to default. The Company's gross exposure to these credits is $445 million and its exposure net of reinsurance is $7 million. The Company rates all of these issuers in the BB category due to the financial condition of Spain and their dependence on the sovereign. The Company's Hungary exposure is to infrastructure bonds dependent on payments from Hungarian governmental entities, and covered mortgage bonds. The Company's gross exposure to these Hungarian credits is $331 million and its exposure net of reinsurance is $7 million, all of which is rated BIG. The Company estimated net expected losses of $0.7 million related to these Spanish and Hungarian credits. The economic benefit of approximately $0.2 million during 2015 was primarily related to changes in the exchange rate between the Euro and US Dollar and certain assumption updates.

5. Financial Guaranty Insurance

Financial Guaranty Insurance Premiums

The portfolio of outstanding exposures discussed in Note 3, Outstanding Exposure, includes financial guaranty contracts that meet the definition of insurance contracts as well as those that meet the definition of a derivative under GAAP. Amounts presented in this note relate only to financial guaranty insurance contracts. See Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives for amounts that relate to CDS.

Accounting Policies

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 the contract was written on a direct basis, assumed from another financial guarantor under a reinsurance treaty, ceded to another insurer under a reinsurance treaty, or acquired in a business combination.

Premium receivables comprise the present value of contractual or expected future premium collections discounted using the risk-free rate.

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

- For premiums received upfront on financial guaranty insurance contracts that were originally underwritten by the Company, 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 that were originally underwritten by the Company unearned premium reserve is the present value of either (1) contractual premiums due or (2) in cases where the underlying collateral is comprised of homogeneous pools of assets, the expected premiums to be collected over the life of the contract. To be considered a homogeneous pool of assets prepayments must be contractually prepayable, the amount of prepayments must be probable, and the timing and amount of prepayments must be reasonably estimable. 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 and prospective changes are recognized in premium reserves. 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. 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.

The Company recognizes unearned premium reserve as earned premium over the contractual period or expected 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 principal 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 principal amounts outstanding in the reporting period compared with the sum of each of the

insured principal 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.

Financial Guaranty Insurance Premiums

Unearned premium reserve ceded to reinsurers (ceded unearned premium reserve) is recorded as an asset. Direct, assumed and ceded earned premium revenue are presented together as net earned premiums in the statement of operations. Net earned premiums comprise the following:

Net Earned Premiums

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Scheduled net earned premiums	$ 291	$ (119)
Acceleration of net earned premiums(1)	718	(48)
Accretion of discount on net premiums receivable	249	(185)
Net earned premiums	$ 1,258	$ (352)

(1) Reflects the unscheduled refunding or termination of the insurance on an insured obligation as well as changes in scheduled earnings due to changes in the expected lives of the insured obligations.

(2) Negative net earned premiums are due to cessions of commutation premiums.

Gross Premium Receivable
Roll Forward

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Beginning of period, December 31	$ 306,336	$ 350,436
Gross premium written, new business	29,733	478
Gross premiums received	(24,505)	(27,810)
Adjustments:		
Changes in the expected term	(2,239)	(2,267)
Accretion of discount	9,631	11,405
Foreign exchange translation	(20,595)	(25,906)
End of period, December 31	$ 298,361	$ 306,336

Foreign exchange translation relates to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 99.4%, and 99.4% of installment premiums at December 31, 2015 and 2014, respectively, are denominated in currencies other than the U.S. dollar, primarily the Euro and British Pound Sterling.

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

Expected Collections of
Financial Guaranty Gross Premiums Receivable
(Undiscounted)

	As of December 31, 2015
	(in thousands)
2016 (January 1 - March 31)	$ 13,823
2016 (April 1 - June 30)	10,511
2016 (July 1 - September 30)	5,397
2016 (October 1 - December 31)	6,248
2017	22,393
2018	20,842
2019	20,687
2020	20,402
2021-2025	96,538
2026-2030	77,661
2031-2035	57,824
After 2035	58,318
Total	$ 410,644

Scheduled Financial Guaranty Net Earned Premiums

	As of December 31, 2015
	(in thousands)
2016 (January 1 - March 31)	$ (194)
2016 (April 1 - June 30)	(196)
2016 (July 1 - September 30)	(198)
2016 (October 1 - December 31)	(199)
Subtotal 2016	(787)
2017	(802)
2018	(768)
2019	(737)
2020	(754)
2021-2025	(3,469)
2026-2030	(3,184)
2031-2035	(2,525)
After 2035	(7,045)
Net unearned premium reserve	(20,071)
Future accretion	4,033
Total future net earned premiums	$ (16,038)

Selected Information for Financial Guaranty Policies Paid in Installments

	As of December 31, 2015	As of December 31, 2014
	(dollars in thousands)	
Premiums receivable	$ 298,361	$ 306,336
Gross unearned premium reserve	353,761	383,636
Weighted-average risk-free rate used to discount premiums	3.3%	3.8%
Weighted-average period of premiums receivable (in years)	11.2	11.4

Financial Guaranty Insurance Acquisition Costs

Accounting Policy

Policy acquisition costs that are directly related and essential to successful insurance contract acquisition and ceding commission income on ceded reinsurance contracts are deferred for contracts accounted for as insurance and reported net. Amortization of deferred ceding commissions includes the accretion of discount on ceding commission income and expense.

Capitalized policy acquisition costs include expenses such as the cost of underwriting personnel attributable to successful underwriting efforts. 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 deferred acquisition costs ("DAC"), with a corresponding offset to net premiums receivable or reinsurance balances payable. Management uses its judgment in determining the type and amount of costs to be deferred. The Company conducts an annual study to determine which operating costs qualify for deferral. 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. DAC, net of deferred ceding commission income, is amortized in proportion to net earned premiums. When an insured obligation is retired early, the remaining related DAC, net of ceding commission income is recognized at that time.

Expected losses, which include 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 Ceding Commissions,
Net of DAC

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Beginning of period	$ 180,382	$ 183,063
Costs deferred during the period:		
Commissions on ceded business	7,600	6,957
Overhead and premium taxes	(483)	3
Total	7,117	6,960
Costs amortized during the period	(16,631)	(9,641)
End of period	$ 170,868	$ 180,382

Financial Guaranty Insurance Losses

Accounting Policies

Loss and LAE Reserve

Loss and LAE reserve reported on the balance sheet relates only to direct contracts that are accounted for as insurance, all of which are financial guaranty insurance contracts. The corresponding reserve ceded to reinsurers is reported as reinsurance recoverable on unpaid losses. As discussed in Note 6, Fair Value Measurement, contracts that meet the definition of a derivative, are recorded separately at fair value. Any expected losses on credit derivatives are not recorded as loss and LAE reserve on the consolidated balance sheet.

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 an insurance 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.

Expected Loss to be Expensed

Expected loss to be expensed represents past or expected future 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.

Insurance Contracts' Loss Information

The following table provides information on loss and LAE reserves, net of reinsurance. The Company used weighted average risk-free rates for financial guaranty insurance obligations that ranged from 0.0% to 1.48% as of December 31, 2015 and 0.0% to 1.50% as of December 31, 2014. The Company had no financial guaranty insurance expected LAE reserve as of December 31, 2015 and December 31, 2014.

Loss and LAE Reserve
Net of Reinsurance
Insurance Contracts

	As of December 31, 2015	As of December 31, 2014
	(in thousands)	
Non-U.S. public finance	$ 493	$ 658
Other structured finance	36	32
Total	$ 529	$ 690

Components of Net Reserves

	As of December 31, 2015	As of December 31, 2014
	(in thousands)	
Loss and LAE reserve	$ 36,569	$ 47,909
Reinsurance recoverable on unpaid losses	(36,040)	(47,219)
Net reserves	$ 529	$ 690

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

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

	As of December 31, 2015
	(in thousands)
Net expected loss to be paid	$ 706
Loss and LAE reserve, net of reinsurance	(529)
Net expected loss to be expensed (present value)	$ 177

The following table provides a schedule of the expected timing of net expected losses to be expensed. The amount and timing of actual loss and LAE may differ from the estimates shown below due to factors such as accelerations, commutations, changes in expected lives and updates to loss estimates.

Net Expected Loss to be Expensed
Financial Guaranty Insurance Contracts

	As of December 31, 2015
	(in thousands)
2016 (January 1 - March 31)	$ 6
2016 (April 1 - June 30)	6
2016 (July 1 - September 30)	5
2016 (October 1 - December 31)	5
Subtotal 2016	22
2017	20
2018	19
2019	17
2020	16
2021 - 2025	58
2026 - 2030	23
2031 - 2033	2
Net expected loss to be expensed	177
Discount	8
Total expected future loss and LAE	$ 185

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

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Non-U.S. public finance	$ (165)	$ (108)
Other structured finance	4	32
Total loss and LAE	$ (161)	$ (76)

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

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

	BIG Categories						
	BIG 1		BIG 2		BIG 3		Total BIG, Net
	Gross	Ceded	Gross	Ceded	Gross	Ceded	
	(dollars in thousands)						
Number of risks(1)	5	(5)	—	—	—	—	5
Remaining weighted-average contract period (in years)	7.2	7.2	—	—	—	—	7.3
Outstanding exposure:							
Principal	$ 889,053	$ (874,195)	$ —	$ —	$ —	$ —	$ 14,858
Interest	344,549	(339,268)	—	—	—	—	5,281
Total	$1,233,602	$ (1,213,463)	$ —	$ —	$ —	$ —	$ 20,139
Expected cash outflows (inflows)	$ 43,155	$ (42,441)	$ —	$ —	$ —	$ —	$ 714
Potential recoveries	—	—	—	—	—	—	—
Subtotal	43,155	(42,441)	—	—	—	—	714
Discount	(413)	405	—	—	—	—	(8)
Present value of expected cash flows	$ 42,742	$ (42,036)	$ —	$ —	$ —	$ —	$ 706
Unearned premium reserve	$ 6,173	$ (5,996)	$ —	$ —	$ —	$ —	$ 177
Reserves(2)	$ 36,569	$ (36,040)	$ —	$ —	$ —	$ —	$ 529

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of December 31, 2014

	BIG Categories						
	BIG 1		BIG 2		BIG 3		Total BIG, Net
	Gross	Ceded	Gross	Ceded	Gross	Ceded	
	(dollars in thousands)						
Number of risks(1)	4	(4)	—	—	—	—	4
Remaining weighted-average contract period (in years)	8.0	8.0	—	—	—	—	7.9
Outstanding exposure:							
Principal	$ 901,502	$ (885,212)	$ —	$ —	$ —	$ —	$ 16,290
Interest	377,450	(371,262)	—	—	—	—	6,188
Total	$1,278,952	$(1,256,474)	$ —	$ —	$ —	$ —	$ 22,478
Expected cash outflows (inflows)	$ 56,110	$ (55,187)	$ —	$ —	$ —	$ —	$ 923
Potential recoveries	—	—	—	—	—	—	—
Subtotal	56,110	(55,187)	—	—	—	—	923
Discount	(649)	638	—	—	—	—	(11)
Present value of expected cash flows	$ 55,461	$ (54,549)	$ —	$ —	$ —	$ —	$ 912
Unearned premium reserve	$ 7,553	$ (7,331)	$ —	$ —	$ —	$ —	$ 222
Reserves(2)	$ 47,909	$ (47,219)	$ —	$ —	$ —	$ —	$ 690

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

(2) See table "Components of net reserves."

6. Fair Value Measurement

The Company carries its investment portfolio and credit derivative contracts 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 2015, 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 fair value hierarchy is determined based on whether the inputs to valuation techniques used to measure fair value are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Company estimates of market assumptions. The fair value hierarchy prioritizes model inputs into three broad levels as follows, with Level 1 being the highest and Level 3 the lowest. An asset or liability's categorization is based on the lowest level of significant input to its valuation.

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

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

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

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

Measured and Carried at Fair Value

Fixed-Maturity Securities and Short-Term Investments

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

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

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

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

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

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

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

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

Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company's credit derivatives consist of insured CDS contracts that fall under derivative accounting standards requiring fair value accounting through the statement of operations. The Company did not enter into CDS with the intent to trade these contracts and the Company may not unilaterally terminate a CDS contract absent an event of default or termination event that entitles the Company to terminate such contracts; however, the Company has mutually agreed with various counterparties to terminate certain CDS transactions. Such terminations generally are not completed at fair value but instead for an amount that approximates the present value of future premiums or for a negotiated amount.

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

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

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

The fair value of the Company's credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay and the estimated present value of premiums that a financial guarantor of comparable credit-worthiness would hypothetically charge or pay at the reporting date for the same protection. The fair value of the Company's credit derivatives depends on a number of factors, including notional amount of the contract, expected term, credit spreads, changes in interest rates, the credit ratings of referenced entities, the Company's own credit risk and remaining contractual cash flows. The expected remaining contractual premium cash flows are the most readily observable inputs since they are based on the CDS contractual terms. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. Consistent with previous years, market conditions at December 31, 2015 were such that market prices of the Company's CDS contracts were not available.

Management considers factors such as current prices charged for similar agreements, when available, performance of underlying assets, life of the instrument, and the nature and extent of activity in the financial guaranty credit derivative marketplace. The assumptions that management uses to determine the fair value may change in the future due to market conditions. Due to the inherent uncertainties of the assumptions used in the valuation models, actual experience may differ from the estimates reflected in the Company's consolidated financial statements and the differences may be material.

Assumptions and Inputs

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

- Gross spread.

- The allocation of gross spread among:

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

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

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

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

- The rates used to discount future expected premium cash flows ranged from 0.62% to 1.81% at December 31, 2015 and 0.30% to 2.15% at December 31, 2014.

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

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

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

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

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

- Credit spreads interpolated based upon market indices.

- Credit spreads provided by the counterparty of the CDS.

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

As of December 31, 2015, and December 31, 2014, all of the Company's CDS contracts were fair valued utilizing credit spreads interpolated based upon market indices.

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

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

The premium the Company receives is referred to as the "net spread." The Company's pricing model takes into account not only how credit spreads on risks that it assumes affect pricing, but also how the Company's own credit spread affects the pricing of its deals. The Company's own credit risk is factored into the determination of net spread based on the impact of changes in the quoted market price for credit protection bought on the Company, as reflected by quoted market prices on CDS referencing AGM, which the Company uses as a proxy for the Company's credit cost. For credit spreads on the Company's name, the Company obtains the quoted price of CDS contracts traded on AGM from market data sources published by third parties. The cost to acquire CDS protection referencing AGM affects the amount of spread on CDS deals that the Company retains and, hence, their fair value. As the cost to acquire CDS protection referencing AGM increases, the amount of premium the Company retains on a deal generally decreases. As the cost to acquire CDS protection referencing AGM decreases, the amount of premium the Company retains on a deal generally increases. In the Company's valuation model, the premium the Company captures is not permitted to go below the minimum rate that the Company would currently charge to assume similar risks. This assumption can have the effect of mitigating the amount of unrealized gains that are recognized on certain CDS contracts. Given the current market conditions and the Company's own credit spreads, approximately 25% and 20%, based on number of deals, of the Company's CDS contracts are fair valued using this minimum premium as of December 31, 2015 and December 31, 2014, respectively. The percentage of deals that price using the minimum premiums fluctuates due to changes in AGM's credit spreads. In general when AGM's credit spreads narrow, the cost to hedge AGM's name declines and more transactions price above previously established floor levels. Meanwhile, when AGM's credit spreads widen, the cost to hedge AGM's name increases causing more transactions to price at previously established floor levels. The Company corroborates the assumptions in its fair value model, including the portion of exposure to the Company hedged by its counterparties, with independent third parties each reporting period. The current level of the Company's own credit spread has resulted in the bank or deal originator hedging a significant portion of its exposure to the Company. This reduces the amount of contractual cash flows the Company can capture as premium for selling its protection. For the portion of risk on each credit derivative that is ceded to AGM, no adjustment is made to the fair value for additional credit risk as the credit rating of the Company and AGM are the same. For the portion of risk on each credit derivative that is ceded to external reinsurers or affiliated reinsurers with a lower credit rating, the Company makes an adjustment to the fair value for any additional credit risk associated with external reinsurers or affiliated reinsurers as applicable.

The amount of premium a financial guaranty insurance market participant can demand is inversely related to the cost of credit protection on the insurance company as measured by market credit spreads assuming all other assumptions remain constant. This is because the buyers of credit protection typically hedge a portion of their risk to the financial guarantor, due to the fact that the contractual terms of the Company's contracts typically do not require the posting of collateral by the guarantor. The extent of the hedge depends on the types of instruments insured and the current market conditions.

A fair value resulting in a credit derivative asset on protection sold is the result of contractual cash inflows on in-force deals in excess of what a hypothetical financial guarantor could receive if it sold protection on the same risk as of the reporting date. If the Company were able to freely exchange these contracts (i.e., assuming its contracts did not contain proscriptions on transfer and there was a viable exchange market), it would be able to realize a gain representing the difference between the higher contractual premiums to which it is entitled and the current market premiums for a similar contract. The Company

determines the fair value of its CDS contracts by applying the difference between the current net spread and the contractual net spread for the remaining duration of each contract to the notional value of its CDS contracts and taking the present value of such amounts discounted at the corresponding London Interbank Offered Rate over the weighted average remaining life of the contract.

Example

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

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

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

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

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

Strengths and Weaknesses of Model

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

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

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

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

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

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

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

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

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

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

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

Not Carried at Fair Value

Financial Guaranty Insurance Contracts

The fair value of the Company's financial guaranty contracts accounted for as insurance is based on management's estimate of what a similarly rated financial guaranty insurance company would demand to acquire the Company's in-force book of financial guaranty insurance business. It is based on a variety of factors that may include pricing assumptions management has observed for portfolio transfers, commutations, and acquisitions that have occurred in the financial guaranty market, as well as prices observed in the credit derivative market with an adjustment for illiquidity so that the terms would be similar to a financial guaranty insurance contract, and includes adjustments to the carrying value of unearned premium reserve for stressed losses, ceding commissions and return on capital. The significant inputs were not readily observable. The Company accordingly classified this fair value measurement as Level 3.

Other Assets

The Company's other assets consist predominantly of accrued interest, the carrying values of which approximate fair value.

Financial Instruments Carried at Fair Value

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

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2015

		Fair Value Hierarchy		
	Fair Value	Level 1	Level 2	Level 3
		(in thousands)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Corporate securities	$ 88,449	$ —	$ 88,449	$ —
Non-U.S. government securities	181,265	—	181,265	—
Total fixed-maturity securities	269,714	—	269,714	—
Short-term investments	112	112	—	—
Credit derivative assets	5,834	—	—	5,834
Total assets carried at fair value	$ 275,660	$ 112	$ 269,714	$ 5,834
Liabilities:				
Credit derivative liabilities	$ 5,998	$ —	$ —	$ 5,998
Total liabilities carried at fair value	$ 5,998	$ —	$ —	$ 5,998

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2014

	Fair Value	Fair Value Hierarchy Level 1	Level 2	Level 3
		(in thousands)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Corporate securities	$ 87,178	$ —	$ 87,178	$ —
Non-U.S. government securities	187,322	—	187,322	—
Total fixed-maturity securities	274,500	—	274,500	—
Short-term investments	14,675	112	14,563	—
Credit derivative assets	6,869	—	—	6,869
Total assets carried at fair value	$ 296,044	$ 112	$ 289,063	$ 6,869
Liabilities:				
Credit derivative liabilities	$ 7,479	$ —	$ —	$ 7,479
Total liabilities carried at fair value	$ 7,479	$ —	$ —	$ 7,479

Changes in Level 3 Fair Value Measurements

The table below presents a roll forward of the Company's Level 3 financial instruments carried at fair value on a recurring basis during the years ended December 31, 2015 and 2014.

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2015

	Credit Derivative Asset (Liability), net(2)
	(in thousands)
Fair value as of December 31, 2014	$ (610)
Total pretax realized and unrealized gains/(losses) recorded in: (1)	
Net income (loss)	785
Settlements	(339)
Fair value as of December 31, 2015	$ (164)
Change in unrealized gains/(losses) related to financial instruments held as of December 31, 2015	$ 597

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2014

	Credit Derivative Asset (Liability), net(2)
	(in thousands)
Fair value as of December 31, 2013	$ (5,034)
Total pretax realized and unrealized gains/(losses) recorded in: (1)	
Net income (loss)	942
Settlements	3,482
Fair value as of December 31, 2014	$ (610)
Change in unrealized gains/(losses) related to financial instruments held as of December 31, 2014	$ 580

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

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

Level 3 Fair Value Disclosures

Quantitative Information About Level 3 Fair Value Inputs
As of December 31, 2015

Financial Instrument Description (1)	Fair Value at December 31, 2015 (in thousands)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Liabilities:				
Credit derivative liabilities, net	$ (164)	Hedge cost (in bps)	32.8 - 91.5	74.8
		Bank profit (in bps)	49.5 - 254.1	200.4
		Internal floor (in bps)	12.5 - 30.0	25.0
		Internal credit rating	AAA - BBB	A+

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

Quantitative Information About Level 3 Fair Value Inputs
As of December 31, 2014

Financial Instrument Description (1)	Fair Value at December 31, 2014 (in thousands)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Liabilities:				
Credit derivative liabilities, net	$ (610)	Hedge cost (in bps)	21.3 - 81.3	53.8
		Bank profit (in bps)	38.5 - 229.4	146.6
		Internal floor (in bps)	12.5 - 30.0	25.0
		Internal credit rating	AAA - BBB	AA

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

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

Fair Value of Financial Instruments

	As of December 31, 2015		As of December 31, 2014	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in thousands)			
Assets:				
Fixed-maturity securities	$ 269,714	$ 269,714	$ 274,500	$ 274,500
Short-term investments	112	112	14,675	14,675
Credit derivative assets	5,834	5,834	6,869	6,869
Financial guaranty insurance contracts(1)	112,638	118,234	114,957	120,003
Other assets	4,128	4,128	4,319	4,319
Liabilities:				
Credit derivative liabilities	5,998	5,998	7,479	7,479

____

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

7. Financial Guaranty Contracts Accounted for as Credit Derivatives

Accounting Policy

Credit derivatives are recorded at fair value. Changes in fair value are recorded in "net change in fair value of credit derivatives" on the consolidated statement of operations. Realized gains and other settlements on credit derivatives include credit derivative premiums received and receivable for credit protection the Company has sold under its insured CDS contracts, premiums paid and payable for credit protection the Company has purchased, claims paid and payable and received and receivable related to insured credit events under these contracts, ceding commission expense or income and realized gains or losses related to their early termination. Fair value of credit derivatives is reflected as either net assets or net liabilities determined on a contract by contract basis in the Company's consolidated balance sheets. See Note 6, Fair Value Measurement, for a discussion on the fair value methodology for credit derivatives.

Credit Derivative Net Par Outstanding by Sector

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

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

Fair Value of Credit Derivatives

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

	Year Ended December 31, 2015	Year Ended December 31, 2014
	(in thousands)	
Realized gains on credit derivatives	$ 188	$ 362
Net change in unrealized gains (losses) on credit derivatives		
Funded collateralized loan obligations (“CLOs”)	12	20
Other(1)	585	560
Net change in unrealized gains (losses) on credit derivatives	597	580
Net change in fair value of credit derivatives	$ 785	$ 942

____

(1) “Other” includes all other international asset classes, such as commercial receivables and international infrastructure.

In 2015 and 2014, unrealized fair value gains were generated primarily by the run-off of par outstanding, terminations, and the lapse of time in the other category as these transactions approach maturity.

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

The following table presents the net par outstanding and fair value for contracts accounted for as derivatives. There were no expected claim payments or recoveries as of December 31, 2015 and 2014.

Net Par Outstanding and Net Fair Value of Credit Derivatives by Sector

	Net Par Outstanding		Fair Value of Credit Derivative Asset (Liability), net	
Asset Type	As of December 31, 2015	As of December 31, 2014	As of December 31, 2015	As of December 31, 2014
	(in thousands)			
CLOs	$ 3,120	$ 8,171	$ 37	$ 132
Other	11,165	11,689	(201)	(742)
Total	$ 14,285	$ 19,860	$ (164)	$ (610)

8. Variable Interest Entities

Background

The Company provides financial guaranties with respect to debt obligations of special purpose entities, including variable interest entities ("VIEs"). The Company does not sponsor any VIEs when underwriting third party financial guaranty insurance or credit derivative transactions, nor has it acted as the servicer or collateral manager for any VIE obligations that it insures. The transaction structure generally provides certain financial protections to the Company.

The Company is not primarily liable for the debt obligations issued by the VIEs it insures and would only be required to make payments on those insured debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due and only for the amount of the shortfall. The Company’s creditors do not have any rights with regard to the collateral supporting the debt issued by the financial guaranty VIE ("FG VIEs").

Accounting Policy

The Company evaluates whether it is the primary beneficiary of its VIEs. If the Company concludes that it is the primary beneficiary it is required to consolidate the entire VIE in the Company's financial statements and eliminate the effects of the financial guaranty insurance contracts issued by AGE on the consolidated FG VIEs debt obligations.

The primary beneficiary of a VIE is the enterprise that has both 1) the power to direct the activities of a VIE that most significantly impact the entity's economic performance; and 2) the obligation to absorb losses of the entity that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE.

As part of the terms of its financial guaranty contracts, the Company obtains certain protective rights with respect to the VIE that are triggered by the occurrence of certain events, such as failure to be in compliance with a covenant due to poor deal performance or a deterioration in a servicer or collateral manager's financial condition. At deal inception, the Company typically is not deemed to control a VIE; however, once a trigger event occurs, the Company's control of the VIE typically increases. The Company continuously evaluates its power to direct the activities that most significantly impact the economic performance of VIEs that have debt obligations insured by the Company and, accordingly, where the Company is obligated to absorb VIE losses or receive benefits that could potentially be significant to the VIE. The Company obtains protective rights under its insurance contracts that give the Company additional controls over a VIE if there is either deterioration of deal performance or in the financial health of the deal servicer. The Company is deemed to be the control party for certain VIEs under GAAP, typically when its protective rights give it the power to both terminate and replace the deal servicer, which are characteristics specific to the Company's financial guaranty contracts. If the protective rights that could make the Company the control party have not been triggered, then the VIE is not consolidated. If the Company is deemed no longer to have those protective rights, the transaction is deconsolidated.

As of December 31, 2015 and December 31, 2014, the Company had financial guaranty contracts outstanding for 19 and 29 VIEs, respectively, that it did not consolidate. To date, the Company's analysis have indicated that it does not have a controlling financial interest in any other VIEs and, as a result, they are not consolidated in the consolidated financial statements. The Company's exposure provided through its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 3, Outstanding Exposure.

9. Investments and Cash

Accounting Policy

The Company's investment portfolio is composed of fixed-maturity and short-term investments, classified as available-for-sale at the time of purchase, and therefore carried at fair value. Unrealized gains and losses on available-for-sale securities are reported as net increases or decreases to accumulated other comprehensive income/(loss). Changes in fair value for other-than-temporarily- impaired ("OTTI") securities are bifurcated between credit losses and non-credit changes in fair value. The credit loss on OTTI securities is recorded in the statement of operations and the non-credit component of the change in fair value of securities, whether OTTI or not, is recorded in OCI. For securities 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, declines in fair value are 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 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 securities 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.

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.

Assessment for Other-Than-Temporary Impairments

The amount of other-than-temporary-impairment recognized in earnings depends on whether (1) an entity intends to sell the security or (2) it is more-likely-than-not that the entity will be required to sell the security before recovery of its amortized cost basis.

If an entity does not intend to sell the security and it is not more-likely-than-not that the Company will be required to sell the security before recovery of its amortized cost basis, the other-than-temporary-impairment is separated into (1) the amount representing the credit loss and (2) the amount related to all other factors.

The Company has a formal review process to determine other-than-temporary-impairment 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;
- the impact of foreign exchange rates; 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 other-than-temporary impairment 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. The assumptions used in these projections require the use of significant management judgment.

The Company's assessment of a decline in value included management's current assessment of the factors noted above. The Company also seeks advice from its outside investment managers. If that assessment changes in the future, the Company may ultimately record a loss after having originally concluded that the decline in value was temporary.

Net Investment Income and Realized Gains (Losses)

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. Accrued investment income, which is recorded in Other Assets, was $4.1 million and $4.3 million as of December 31, 2015 and December 31, 2014, respectively.

Net Investment Income

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Income from fixed-maturity securities	$ 6,920	$ 7,587
Income from short-term investments	9	24
Other	—	13
Gross investment income	6,929	7,624
Investment expenses	(332)	(229)
Net investment income	$ 6,597	$ 7,395

Net Realized Investment Gains (Losses)

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Gross realized gains on investment portfolio	$ 663	$ 2,923
Gross realized losses on investment portfolio	(866)	(365)
Other-than-temporary impairment	(3,489)	(3,317)
Net realized investment gains (losses)	$ (3,692)	$ (759)

There was no credit losses balance as of December 31, 2015 and December 31, 2014 for investments where the Company recognized an other-than-temporary-impairment and a portion of the fair value adjustments related to other factors were recorded in OCI.

Investment Portfolio

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

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI (2) Gain (Loss) on Securities with OTTI	Weighted Average Credit Rating(3)
			(dollars in thousands)				
Fixed-maturity securities:							
Corporate securities	32%	$ 91,696	$ 501	$ (3,748)	$ 88,449	$ 16	AA
U.K. government securities	68	196,787	560	(16,082)	181,265	—	AA+
Total fixed-maturity securities	100	288,483	1,061	(19,830)	269,714	16	AA+
Short-term investments	0	112	—	—	112	—	AAA
Total investment portfolio	100%	$ 288,595	$ 1,061	$ (19,830)	$ 269,826	$ 16	AA+

Fixed-Maturity Securities and Short-Term Investments
by Security Type
As of December 31, 2014

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI (2) Gain (Loss) on Securities with OTTI	Weighted Average Credit Rating(3)
	(dollars in thousands)						
Fixed-maturity securities:							
Corporate securities	29%	$ 83,990	$ 3,571	$ (383)	$ 87,178	$ —	AA
U.K. government securities	66	193,234	3,780	(9,692)	187,322	—	AA+
Total fixed-maturity securities	95	277,224	7,351	(10,075)	274,500	—	AA+
Short-term investments	5	14,674	1	—	14,675	1	AAA
Total investment portfolio	100%	$ 291,898	$ 7,352	$ (10,075)	$ 289,175	$ 1	AA+

(1) Based on amortized cost.

(2) Accumulated OCI ("AOCI"). See also Note 15, Other Comprehensive Income.

(3) Ratings in the tables above represent the lower of the Moody's and S&P classifications. The Company's portfolio consists primarily of high-quality, liquid instruments.

Under the Company's investment guidelines, securities rated lower than A-/A3 by S&P or Moody’s are typically not purchased for the Company’s portfolio unless acquired for loss mitigation or risk management strategies.

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

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2015

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
	(dollars in thousands)					
Corporate securities	$ 54,391	$ (2,061)	$ 17,611	$ (1,687)	$ 72,002	$ (3,748)
U.K. government securities	82,159	(3,007)	81,636	(13,075)	163,795	(16,082)
Total	$ 136,550	$ (5,068)	$ 99,247	$ (14,762)	$ 235,797	$ (19,830)
Number of securities(1)		27		19		37

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

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2014

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
	(dollars in thousands)					
Corporate securities	$ 16,966	$ (383)	$ —	$ —	$ 16,966	$ (383)
U.K. government securities	64,991	(1,285)	43,159	(8,407)	108,150	(9,692)
Total	$ 81,957	$ (1,668)	$ 43,159	$ (8,407)	$ 125,116	$ (10,075)
Number of securities		16		2		18

The unrealized loss is primarily foreign exchange related and not specific to individual issuer credit. The Company has determined that these securities were not other-than-temporarily impaired as of December 31, 2015 and December 31, 2014.

The amortized cost and estimated fair value of available-for-sale fixed-maturity securities by contractual maturity as of December 31, 2015 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, 2015

	Amortized Cost	Estimated Fair Value
	(in thousands)	
Due within one year	$ 38,788	$ 30,387
Due after one year through five years	146,334	139,709
Due after five years through 10 years	100,885	97,010
Due after 10 years	2,476	2,608
Total	$ 288,483	$ 269,714

No material investments of the Company were non-income producing for years ended December 31, 2015 and 2014, respectively.

10. Dividend Restrictions and Statutory Financial Information

Dividend Restrictions

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

The Company did not declare or pay dividends during 2015 and 2014.

Statutory Financial Information

GAAP differs in certain significant respects from U.S. insurance companies' statutory accounting practices prescribed or permitted by insurance regulatory authorities. The principal differences result from the following statutory accounting practices:

- upfront premiums are earned when related principal and interest have expired rather than earned over the expected period of coverage;

- acquisition costs are charged to expense as incurred rather than over the period that related premiums are earned;

- a contingency reserve is computed based on statutory requirements, whereas no such reserve is required under GAAP;

- certain assets designated as “non-admitted assets” are charged directly to statutory surplus, rather than reflected as assets under GAAP;

- investments in subsidiaries are carried on the balance sheet on the equity basis, to the extent admissible, rather than consolidated with the parent;

- the amount of deferred tax assets that may be admitted is subject to an adjusted surplus threshold and is generally limited to the lesser of those assets the Company expects to realize within three years of the balance sheet date or fifteen percent of the Company's adjusted surplus. This realization period and surplus percentage is subject to change based on the amount of adjusted surplus. Under GAAP there is no non-admitted asset determination, rather a valuation allowance is recorded to reduce the deferred tax asset to an amount that is more likely than not to be realized;

- insured credit derivatives are accounted for as insurance contracts rather than as derivative contracts measured at fair value;

- bonds are generally carried at amortized cost rather than fair value;

- expected losses are discounted at a rate of 5.0%, recorded when the loss is deemed probable and without consideration of the unearned premium reserve rather than discounted at the risk free rate at the end of each reporting period and only to the extent they exceed unearned premium reserve;

- the present value of installment premiums and commissions are not recorded on the balance sheet as they are under GAAP.

The following table presents a reconciliation of the Company's GAAP shareholder's equity to statutory surplus for the years ended December 31, 2015 and 2014.

**Reconciliation of GAAP Shareholder's Equity
to Statutory Surplus**

	As of December 31,	
	2015	2014
	(in thousands)	
GAAP shareholder's equity	$ 261,946	$ 271,832
Unearned premium reserve	8,836	9,397
Deferred ceding commissions, net	159,950	169,091
Contingency reserves	(3,387)	(2,564)
Deferred income taxes	(38,274)	(34,124)
Unrealized gain on investments	(7,598)	(12,391)
Premium receivable, net of ceded premium payable	(88,314)	(92,233)
Other	5,461	5,485
Statutory surplus	$ 298,620	$ 314,493

11. 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

In conjunction with AGL's purchase of Assured Guaranty Municipal Holdings Inc. ("AGMH") on July 1, 2009, AGE joined the consolidated federal tax group of Assured Guaranty US Holdings Inc. ("AGUS"), an indirect parent holding company of AGE. A tax sharing agreement was entered into effective July 1, 2009 whereby each company in the AGUS consolidated tax group pays or receives its proportionate share of the consolidated federal tax burden for the group as if each company filed on a separate return basis with current period credit for net losses.

Provision for Income Taxes

The Company has made an election with the Internal Revenue Service ("IRS") pursuant to Section 953(d) of the Internal Revenue Code. Section 953(d) allows for certain foreign insurance companies to elect to be treated as a U.S. corporation for federal income tax purposes. The impact of the election is that the Company will be taxed as a U.S. corporation subject to tax on its worldwide income, subject to a credit for any taxes paid to a non-U.S. jurisdiction. As of December 31, 2015, the U.S. marginal corporate income tax rate was 35%, as compared with a tax rate in the United Kingdom of 20% as of that date.

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

Effective Tax Rate Reconciliation

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Expected tax provision (benefit) at statutory rate	$ 781	$ 6,531
Utilization of U.K. tax benefit	897	—
Other	9	15
Total provision (benefit) for income taxes	$ 1,687	$ 6,546
Effective tax rate	75.6%	35.1%

The expected tax provision at statutory rates in taxable jurisdictions is calculated as the sum of pretax income in each jurisdiction multiplied by the statutory tax rate of the jurisdiction by which it will be taxed.

Components of Net Deferred Tax Assets

	As of December 31,	
	2015	2014
	(in thousands)	
Deferred tax assets:		
Deferred ceding commission	$ 59,149	$ 64,846
Unrealized depreciation on investments	6,574	953
Other	2,102	3,661
Total deferred income tax assets	67,825	69,460
Deferred tax liabilities:		
Unearned premium reserve, net of premiums receivable	(28,092)	(27,317)
Other	(736)	(5,923)
Total deferred income tax liabilities	(28,828)	(33,240)
Net deferred income tax asset	$ 38,997	$ 36,220

There were no unrecognized tax benefits for the years ended December 31, 2015 and 2014, respectively.

Valuation Allowance

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

Audits

AGUS has open tax years with the U.S. IRS for 2009 forward and is currently under audit for the 2009 - 2012 tax years. The Company is not currently under examination in the U.K. and has open tax years of 2014 forward.

Tax Treatment of CDS

The Company treats the guaranty it provides on CDS as an insurance contract for tax purposes and as such a taxable loss does not occur until the Company expects to make a loss payment to the buyer of credit protection based upon the occurrence of one or more specified credit events with respect to the contractually referenced obligation or entity. The Company holds its CDS to maturity, at which time any unrealized fair value loss in excess of credit-related losses would revert to zero. The tax treatment of CDS is an unsettled area of the law. The uncertainty relates to the IRS determination of the income or potential loss associated with CDS as either subject to capital gain (loss) or ordinary income (loss) treatment. In treating CDS as insurance contracts the Company treats both the receipt of premium and payment of losses as ordinary income and believes it is more likely than not that any CDS credit related losses will be treated as ordinary by the IRS. To the extent the IRS takes the view that the losses are capital losses in the future and the Company incurred actual losses associated with the CDS, the Company would need sufficient taxable income of the same character within the carryback and carryforward period available under the tax law.

12. Reinsurance and Other Monoline Exposures

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

Accounting Policy

For ceded business, the accounting model of the underlying direct financial guaranty contract dictates the accounting

model used for the reinsurance contract. For any ceded financial guaranty insurance premiums and ceded financial guaranty insurance losses, the accounting models in Note 5 are followed. For any ceded credit derivative contracts, the accounting model in Note 7 is followed.

Ceded Business

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

The Company cedes portions of its exposure to a diversified group of non-affiliated reinsurers, including other monolines, as of December 31, 2015. Over the past several years, the Company has entered into several commutations in order to reassume previously ceded books of business from its reinsurers. There were no commutations in 2015. Upon reassuming such business from third party reinsurers in 2014, AGE ceded more than 90% of the reassumed business to AGM, pursuant to an approved intercompany pooling agreement. While certain Ceded Business has been reassumed, the Company still has Ceded Business with third parties.

Net Effect of Commutations of Ceded Reinsurance Contracts

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Increase in net unearned premium reserve	$ —	$ 12,535
Increase in net par outstanding	—	484,127
Commutation gains recorded in other income	—	22,699

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

Effect of Reinsurance on Statement of Operations

	Year Ended December 31,	
	2015	2014
	(in thousands)	
Premiums Written:		
Direct (1)	$ 27,494	$ (1,789)
Ceded	(26,608)	(22,372)
Net	$ 886	$ (24,161)
Premiums Earned:		
Direct	$ 103,033	$ 49,971
Ceded	(101,775)	(50,323)
Net	$ 1,258	$ (352)
Loss and LAE:		
Direct	$ (11,340)	$ (4,940)
Ceded	11,179	4,864
Net	$ (161)	$ (76)

(1) Negative direct premiums written were due to cancellations and changes in expected debt service schedules.

Reinsurer Exposure

In addition to ceded reinsurance arrangements, the Company may also have exposure to some financial guaranty reinsurers (i.e., monolines) in other areas. Second-to-pay insured par outstanding represents transactions the Company has insured that were previously insured by other monolines. The Company underwrites such transactions based on the underlying insured obligation without regard to the primary insurer.

Exposure by Reinsurer

	Ratings at July 20, 2016		Par Outstanding (1) As of December 31, 2015	
Reinsurer	Moody's Reinsurer Rating	S&P Reinsurer Rating	Ceded Par Outstanding	Second-to-Pay Insured Par Outstanding
			(dollars in millions)	
Affiliated Companies (2)	(3)	(3)	$ 19,719	$ —
Non-Affiliated Companies:				
Tokio Marine & Nichido Fire Insurance Co., Ltd.	Aa3 (4)	A+ (4)	1,061	—
American Overseas Reinsurance Company Limited (2)	WR (5)	WR	633	—
Mitsui Sumitomo Insurance Co. Ltd.	A1	A+ (3)	211	—
Swiss Reinsurance Co. (2)	Aa3	AA-	24	—
FGIC UK Limited	WR	NR (6)	—	14
MBIA	(7)	(7)	—	12
Syncora Guarantee Inc	WR	WR	—	5
Total			$ 21,648	$ 31

____

(1) Includes par related to insured credit derivatives.

(2) The total collateral posted by all affiliated and non-affiliated reinsurers required or agreeing to post collateral as of December 31, 2015, is approximately $358 million.

(3) The affiliated reinsurers to which AGE cedes exposure are Assured Guaranty Re Ltd. ("AG Re"), Assured Guaranty Re Overseas Ltd. ("AGRO") and AGM. Effective April 8, 2015, at the request of AG Re and AGRO, Moody's withdrew the financial strength ratings it had assigned to those insurers. Moody's assigns a financial strength rating of A2 (stable) to AGM. S&P assigns a financial strength rating of AA (stable) to each of AG Re, AGRO and AGM. Since May 5, 2015, A.M. Best Company, Inc. has assigned a financial strength rating of A+ (stable) to AGRO. Kroll Bond Rating Agency assigns a financial strength rating of AA+ (stable) to AGM.

(4) The Company has structural collateral agreements satisfying the triple-A credit requirement of S&P and/or Moody's.

(5) Represents "Withdrawn Rating."

(6) Represents "Not Rated."

(7) MBIA includes subsidiaries MBIA Insurance Corp., rated CCC by S&P and Caa1 by Moody's. and MBIA U.K. Insurance Ltd., rated BB by S&P and Ba2 by Moody's.

Ceded Par Outstanding by Reinsurer and Credit Rating
As of December 31, 2015

Reinsurer	AAA	AA	A	BBB	BIG	Total
	Internal Credit Rating					
	(in millions)					
Affiliated Companies	$ 149	$ 34	$ 4,107	$ 14,655	$ 774	$ 19,719
Tokio Marine & Nichido Fire Insurance Co., Ltd.	47	1	379	555	79	1,061
American Overseas Reinsurance Company Limited	11	0	148	453	21	633
Mitsui Sumitomo Insurance Co. Ltd.	2	0	88	121	—	211
Swiss Reinsurance Co.	—	—	—	24	—	24
Total	$ 209	$ 35	$ 4,722	$ 15,808	$ 874	$ 21,648

Second-to-Pay
Insured Par Outstanding by Internal Rating
As of December 31, 2015(1)

	Public Finance		Structured Finance	
	A	BBB	BIG	Total
	(in millions)			
FGIC UK Limited	$ 14	$ —	$ —	$ 14
MBIA Insurance Corporation and MBIA UK	6	5	1	12
Syncora Guarantee Inc.	—	5	—	5
Total	$ 20	$ 10	$ 1	$ 31

(1) Assured Guaranty's internal rating.

Amounts Due (To) From Reinsurers
As of December 31, 2015

	Ceded Premium, net of Commissions	Ceded Expected Loss to be Paid
	(in thousands)	
Affiliated Companies	$ (187,941)	$ 35,029
Tokio Marine & Nichido Fire Insurance Co., Ltd.	(8,366)	5,768
American Overseas Reinsurance Company Limited.	(3,525)	1,239
Mitsui Sumitomo Insurance Co. Ltd.	(2,210)	—
Swiss Reinsurance Co.	(3,223)	—
Total	$ (205,265)	$ 42,036

13. Related Party Transactions

Cooperative Agreements

The Company is party to cooperative agreements with various affiliated entities for joint use of personnel and property. As such, the Company is allocated a portion of costs for personnel and services in accordance with the agreements.

The following table summarizes the allocated expenses from (to) affiliate companies under the cooperative agreements.

Expenses Allocated From (To) Affiliated Companies

	As of December 31,	
	2015	2014
	(in thousands)	
Affiliated companies:		
Assured Guaranty Finance Overseas Ltd.	$ 9,236	$ 7,815
Assured Guaranty (UK) Services Limited	5,197	5,621
Total	$ 14,433	$ 13,436

The following table summarizes the amounts due (to) from affiliate companies under the cooperative agreements.

Amounts Due (To) From Affiliated Companies

	As of December 31,	
	2015	2014
	(in thousands)	
Affiliated companies:		
Assured Guaranty Finance Overseas Ltd.	$ (2,370)	$ (1,936)
Assured Guaranty (UK) Services Limited	(2,006)	(2,847)
AGL	(1,078)	(763)
AGM	(900)	(891)
Other	(280)	(226)
Total	$ (6,634)	$ (6,663)

Assured Guaranty Credit Protection Limited

The Company has issued financial guarantees that cover the obligations of AGCPL in respect of credit default swaps pursuant to which AGCPL sold credit protection to counterparties. AGCPL may incur losses in the event of payment defaults by the obligors referenced in such credit default swaps. AGCPL has not entered into a new credit default swap since 2008 and the Company does not intend to issue any new financial guarantees of such AGCPL obligations in the future.

Assured Guaranty Municipal Corp.

AGM currently provides support to its subsidiary AGE through a quota share and excess of loss reinsurance agreement (the "Reinsurance Agreement") and a net worth maintenance agreement (the "Net Worth Agreement"). Such agreements replace and supersede the second amended and restated quota share and stop loss reinsurance agreement and the second amended and restated net worth maintenance agreement, respectively, previously in place between the parties. For transactions closed prior to 2011, AGE typically guaranteed all of the guaranteed obligations directly and AGM reinsured under the quota share cover of the Reinsurance Agreement approximately 92% of AGE's retention after cessions to other reinsurers. In 2011, AGE and AGM implemented a co-guarantee structure pursuant to which (i) AGE directly guarantees a portion of the guaranteed obligations in an amount equal to what would have been AGE's pro rata retention percentage under the quota share cover, (ii) AGM directly guarantees the balance of the guaranteed obligations, and (iii) AGM also provides a second-to-pay guarantee for AGE's portion of the guaranteed obligations.

Under the excess of loss cover of the Reinsurance Agreement, AGM will pay AGE quarterly the amount by which (i) the sum of (a) AGE's incurred losses calculated in accordance with U.K. GAAP as reported by AGE in its financial returns filed with the U.K. PRA and (b) AGE's paid losses and LAE, in both cases net of all other performing reinsurance, including the reinsurance provided by AGM under the quota share cover of the Reinsurance Agreement, exceeds (ii) an amount equal to (a) AGE's capital resources under U.K. law minus (b) the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K. In addition, the

Reinsurance Agreement permits AGE to terminate the Reinsurance Agreement upon the following events: a downgrade of AGM's ratings by Moody's below Aa3 or by S&P below AA- if the company fails to restore its rating(s) to the required level within a prescribed period of time; AGM's insolvency; failure by AGM to maintain the minimum capital required by its domiciliary jurisdiction; or AGM filing a petition in bankruptcy, going into liquidation or rehabilitation or having a receiver appointed. The Reinsurance Agreement also provides that no amounts are owing under the excess of loss cover (or the stop loss cover of the second amended and restated quota share and stop loss reinsurance agreement previously in place between the parties) with respect to any quarter ending prior to April 1, 2014.

The quota share and excess loss covers each exclude transactions guaranteed by AGE on or after July 1, 2009 that are not municipal, utility, project finance or infrastructure risks or similar types of risks.

The Reinsurance Agreement also contemplates the establishment of collateral by AGM to support its reinsurance obligations to AGE. In December 2014, to satisfy a new PRA requirement that AGM post collateral to support its reinsurance obligations to AGE, AGM and AGE amended the Reinsurance Agreement to incorporate the PRA's requirement. Pursuant to such amended Reinsurance Agreement, AGM's collateral requirement will be measured as of the end of each calendar quarter by (i) using the PRA's FG Benchmark Model to calculate at the 99.5% confidence interval the losses expected to be borne collectively by AGE's three affiliated reinsurers, AGM, AG Re and AGRO; (ii) deducting from such calculation AGE's capital resources under such model; and (iii) requiring AGM, AG Re and AGRO collectively to maintain collateral equal to fifty percent (50%) of such difference, i.e., the excess of AGM's, AG Re's and AGRO's assumed modeled losses over AGE's capital resources. As of January 1, 2016, the FG Benchmark Model is no longer applicable and the PRA has agreed to allow AGM's collateral requirement to be determined using AGE's internal capital requirement model under the same formula described above. This change is subject to approval by the New York State Department of Financial Services ("NYDFS"). In December 2014, AGM and AGE also entered into a related trust agreement pursuant to which AGM, prior to year-end, established, and deposited assets into a reinsurance trust account for the benefit of AGE to satisfy the PRA's collateral requirement as of September 30, 2014, as measured in accordance with such amended Reinsurance Agreement. The total collateral required to be funded into such reinsurance trust account by AGM as of December 31, 2015 was approximately $244 million.

Pursuant to the Net Worth Agreement, AGM is obligated to cause AGE to maintain capital resources equal to 110% of the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K., provided that AGM's contributions (a) do not exceed 35% of its policyholders' surplus on an accumulated basis as determined by the laws of the State of New York, and (b) are in compliance with Section 1505 of the New York Insurance Law. AGM has never been required to make any contributions to AGE's capital under the current Net Worth Agreement or the prior net worth maintenance agreement.

Reinsurance Agreements

The Company cedes to and assumes business from affiliated entities under certain reinsurance agreements. See below for material balance sheet and statement of operations items related to insurance transactions.

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

	As of December 31,	
	2015	2014
	(in thousands)	
Assets:		
Ceded unearned premium reserve		
AGM	$ 471,963	$ 519,511
AG Re	130,943	139,756
AGC	28,800	—
Reinsurance recoverable on paid losses (1)		
AGM	21,054	27,478
AG Re	5,096	6,280
AGC	3,300	—
Net credit derivative assets		
AGM	2,657	3,305
AG Re	1,781	1,523
AGC	101	—
Liabilities:		
Ceded premium payable, net of ceding commission (2)		
AGM	152,966	154,105
AG Re	25,119	29,158
AGC	9,856	—
Deferred ceding commissions		
AGM	147,460	155,853
AG Re	38,018	40,572
AGC	7,406	—
Other information:		
Exposure		
Ceded par outstanding		
AGM	$ 14,653,284	$ 16,583,546
AG Re	4,182,638	4,568,887
AGC	883,559	—

____

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

(2) Included in ceded reinsurance balances payable on the consolidated balance sheets.

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

	Year Ended December 31, 2015	Year Ended December 31, 2014
	(in thousands)	
Revenues:		
Net earned premiums		
AGM	$ (77,723)	$ (34,194)
AG Re	(9,828)	(10,170)
AGC	(7,263)	—
Realized gains and other settlements on credit derivatives		
AGM	(296)	(578)
AG Re	(53)	(89)
AGC	(4)	—
Net unrealized gains (losses) on credit derivatives		
AGM	(610)	(2,020)
AG Re	261	(822)
AGC	98	—
Expenses:		
Loss and loss adjustment expenses (recoveries)		
AGM	6,424	2,456
AG Re	1,184	1,083
AGC	(3,300)	—

14. Commitments and Contingencies

Lease

AGE entered into an operating lease effective January 29, 2016 for new office space at Bury Court, 6 Bevis Marks in London. AGE has moved the principal place of business of Assured Guaranty Ltd.'s other U.K. based subsidiaries to this new location. The new lease starts in February 2016 and runs until September 2029, with an option, subject to certain conditions, to renew for five years at a fair market rent. The fixed annual rent, which commences after an initial rent holiday, is at £529,425 per year and will be reviewed every five years upwards only to the open market rent.

Legal Proceedings

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, and annual basis and updates its accruals, disclosures and estimates of reasonably possible loss based on such reviews.

Litigation

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

15. Other Comprehensive Income

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

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2015

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in thousands)	
Balance, December 31, 2014	$ (1,771)	$ 1	$ (1,770)
Other comprehensive income (loss) before reclassifications	(10,522)	(2,307)	(12,829)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	127	3,565	3,692
Tax (provision) benefit	(44)	(1,248)	(1,292)
Total amount reclassified from AOCI, net of tax	83	2,317	2,400
Net current period other comprehensive income (loss)	(10,439)	10	(10,429)
Balance, December 31, 2015	$ (12,210)	$ 11	$ (12,199)

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2014

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in thousands)	
Balance, December 31, 2013	$ 2,922	$ —	$ 2,922
Other comprehensive income (loss) before reclassifications	(2,707)	(2,478)	(5,185)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(3,055)	3,814	759
Tax (provision) benefit	1,069	(1,335)	(266)
Total amount reclassified from AOCI, net of tax	(1,986)	2,479	493
Net current period other comprehensive income (loss)	(4,693)	1	(4,692)
Balance, December 31, 2014	$ (1,771)	$ 1	$ (1,770)

16. Subsequent Events

Subsequent events have been considered through July 21, 2016, the date on which these financial statements were issued.

APPENDIX 2

2014 FINANCIAL STATEMENTS OF ASSURED GUARANTY (EUROPE) LTD.

Assured Guaranty (Europe) Ltd.

(an indirect wholly-owned subsidiary of

Assured Guaranty Ltd.)

Consolidated Financial Statements

December 31, 2014 and 2013

(Expressed in U.S. Dollars)

FINANCIAL STATEMENTS
ASSURED GUARANTY (EUROPE) LTD.

Independent Auditor's Report

To the Board of Directors of Assured Guaranty (Europe) Ltd.:

We have audited the accompanying consolidated financial statements of Assured Guaranty (Europe) Ltd. (the "Company"), which comprise the consolidated balance sheets as of December 31, 2014 and December 31, 2013, and the related consolidated statements of operations and comprehensive income, 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.

Auditor's 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 (Europe) Ltd. at December 31, 2014 and December 31, 2013, 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.

PricewaterhouseCoopers LLP

New York, New York
June 26, 2015

Assured Guaranty (Europe) Ltd.

Consolidated Balance Sheets

(dollars in thousands except per share and share amounts)

	As of December 31,	
	2014	2013
Assets		
Investment portfolio:		
Fixed maturity securities, available-for-sale, at fair value (amortized cost of $277,224 and $250,862)	$ 274,500	$ 255,151
Short term investments, at fair value	14,675	6,727
Total investment portfolio	289,175	261,878
Cash	16,790	32,485
Premiums receivable	306,336	350,436
Ceded unearned premium reserve	746,620	765,596
Reinsurance recoverable on unpaid losses	47,219	52,082
Credit derivative assets	6,869	10,905
Deferred tax asset, net	36,220	55,859
Current income tax receivable	1,396	2,463
Other assets	4,341	4,204
Total assets	**$ 1,454,966**	**$ 1,535,908**
Liabilities and shareholder's equity		
Unearned premium reserve	$ 726,672	$ 767,027
Loss and loss adjustment expense reserve	47,909	52,849
Ceded reinsurance balances payable	210,637	242,614
Credit derivative liabilities	7,479	15,939
Deferred ceding commissions, net	180,382	183,063
Other liabilities	10,055	10,005
Total liabilities	**1,183,134**	**1,271,497**
Commitments and contingencies (See Note 16)		
Common stock (500,000,000 shares authorized; 55,000,000 issued and outstanding; par value of £1 each)	81,206	81,206
Additional paid-in capital	118,634	118,634
Retained earnings	73,762	61,649
Accumulated other comprehensive income (loss), net of tax of $(953) and $1,574	(1,770)	2,922
Total shareholder's equity	**271,832**	**264,411**
Total liabilities and shareholder's equity	**$ 1,454,966**	**$ 1,535,908**

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

Assured Guaranty (Europe) Ltd.

Consolidated Statements of Operations and Comprehensive Income

(in thousands)

	Year Ended December 31,	
	2014	2013
Revenues		
Net earned premiums	$ (352)	$ 216
Net investment income	7,395	6,896
Net realized investment gains (losses):		
Other-than-temporary impairment losses	(3,317)	(2,027)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	—	(160)
Net impairment loss	(3,317)	(1,867)
Other net realized investment gains (losses)	2,558	(656)
Net realized investment gains (losses)	(759)	(2,523)
Net change in fair value of credit derivatives:		
Realized gains (losses) and other settlements	362	3,743
Net unrealized gains (losses)	580	193
Net change in fair value of credit derivatives	942	3,936
Other income (loss)	13,529	3,168
Total revenues	20,755	11,693
Expenses		
Loss and loss adjustment expenses	(76)	86
Amortization of deferred ceding commissions	(13,020)	(16,263)
Other operating expenses	15,192	13,614
Total expenses	2,096	(2,563)
Income (loss) before income taxes	18,659	14,256
Provision (benefit) for income taxes:		
Current	(15,620)	(3,982)
Deferred	22,166	6,321
Total provision (benefit) for income taxes	6,546	2,339
Net income (loss)	**12,113**	**11,917**
Unrealized holding gains (losses) arising during the period:		
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $(1,458) and $(1,393)	(2,707)	(2,590)
Investments with other-than-temporary impairment, net of tax provision (benefit) of $(1,335) and $(1,219)	(2,478)	(2,264)
Unrealized holding gains (losses) arising during the period, net of tax	(5,185)	(4,854)
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $(266) and $(883)	(493)	(1,640)
Other comprehensive income (loss)	(4,692)	(3,214)
Comprehensive income (loss)	**$ 7,421**	**$ 8,703**

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

Assured Guaranty (Europe) Ltd.

Consolidated Statements of Shareholder’s Equity

Years Ended December 31, 2014 and 2013

(dollars in thousands, except shares)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholder's Equity
	Shares	Amount				
Balance at December 31, 2012	55,000,000	$ 81,206	$ 118,634	$ 49,732	$ 6,136	$ 255,708
Net income	—	—	—	11,917	—	11,917
Other comprehensive loss	—	—	—	—	(3,214)	(3,214)
Balance at December 31, 2013	**55,000,000**	**$ 81,206**	**$ 118,634**	**$ 61,649**	**$ 2,922**	**$ 264,411**
Net income	—	—	—	12,113	—	12,113
Other comprehensive loss	—	—	—	—	(4,692)	(4,692)
Balance at December 31, 2014	**55,000,000**	**$ 81,206**	**$ 118,634**	**$ 73,762**	**$ (1,770)**	**$ 271,832**

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

Assured Guaranty (Europe) Ltd.

Consolidated Statements of Cash Flows

(in thousands)

	Year Ended December 31, 2014	Year Ended December 31, 2013
Operating Activities:		
Net Income	$ 12,113	$ 11,917
Adjustments to reconcile net income to net cash flows provided by (used in) operating activities:		
Net realized investment losses (gains)	759	2,523
Net amortization of premium (discount) on investments	2,524	2,332
Provision (benefit) for deferred income taxes	22,166	6,321
Net unrealized losses (gains) on credit derivatives	(580)	(193)
Change in premiums receivable, net of premiums payable and commissions	12,123	5,931
Change in deferred ceding commissions, net	(2,681)	(14,642)
Change in ceded unearned premium reserve	18,976	58,304
Change in loss and loss adjustment expense reserve, net	(77)	86
Change in unearned premium reserve	(40,355)	(57,420)
Other changes in credit derivative assets and liabilities, net	(3,844)	4,254
Change in current income tax	1,067	(320)
Other	1,444	(769)
Net cash flows provided by (used in) operating activities	**23,635**	**18,324**
Investing activities		
Fixed-maturity securities:		
Purchases	(79,605)	(70,523)
Sales	28,348	3,499
Maturities	21,713	61,903
Net sales (purchases) of short-term investments	(8,254)	(1,090)
Net cash flows provided by (used in) investing activities	**(37,798)**	**(6,211)**
Net cash flows provided by (used in) financing activities	—	—
Effect of foreign exchange rate changes	(1,532)	464
Increase (decrease) in cash	(15,695)	12,577
Cash at beginning of period	32,485	19,908
Cash at end of period	**$ 16,790**	**$ 32,485**
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$ (16,688)	$ (3,647)

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

Assured Guaranty (Europe) Ltd.

Notes to Consolidated Financial Statements

December 31, 2014 and 2013

1. Business and Basis of Presentation

Business

Assured Guaranty (Europe) Ltd. (“AGE” or the “Company”) is an insurance company organized in the United Kingdom (“U.K.”) and authorized by the U.K. Prudential Regulation Authority (the “U.K. PRA”) to transact the following classes of insurance: 14 (credit), 15 (suretyship) and 16 (miscellaneous financial loss). AGE is also permitted on a passport basis to conduct insurance business in certain member countries of the European Economic Area (“EEA”) from its home office in the U.K. The principal activity of AGE is providing financial guarantees for the international public finance (including infrastructure) market and, with the approval of the U.K. PRA, the asset-backed and other structured finance market.

Management and the U.K. PRA have agreed that any new business written by AGE will be guaranteed using a co-insurance structure pursuant to which AGE will co-insure public finance transactions with its affiliate Assured Guaranty Municipal Corp. ("AGM"), and structured finance transactions with its affiliate Assured Guaranty Corp. ("AGC"). AGE must obtain the approval of the U.K. PRA before it can guarantee any new structured finance transaction. AGE's financial guarantee will cover a proportionate share (expected to be approximately 3 to 10%) of the total exposure, and AGM or AGC, as the case may be, will guarantee the remaining exposure under the transaction (subject to compliance with EEA licensing requirements). AGM or AGC, as the case may be, will also issue a second-to-pay guarantee to cover AGE's financial guarantee.

AGE applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guarantees that protect holders of debt instruments and other monetary obligations from defaults in scheduled payments, including scheduled interest and principal payments ("Debt Service"). AGE markets its financial guarantees directly to issuers and underwriters of securities as well as to investors in such obligations. Financial guarantees provide an unconditional and irrevocable guaranty that protects the holder of a financial obligation against non-payment of Debt Service when due. Upon an obligor's default on scheduled Debt Service payments due on the obligation, AGE is required under the financial guarantee to pay the principal or interest shortfall.

In the past, AGE had sold credit protection by issuing financial guarantees that guaranteed payment obligations of Assured Guaranty Credit Protection Ltd. ("AGCPL") and former affiliates under credit derivatives, primarily credit default swaps ("CDS"). Financial guaranty contracts accounted for as credit derivatives are generally structured such that the circumstances giving rise to AGE’s obligation to make loss payments are similar to those for financial guaranty insurance contracts. AGE's credit derivative transactions are governed by International Swaps and Derivative Association, Inc. (“ISDA”) documentation.

AGE has not guaranteed any new CDS under which credit protection has been sold since 2008. AGE actively pursues opportunities to terminate existing CDS, which have the effect of reducing future fair value volatility in income and/or reducing rating agency capital charges.

Corporate Structure

The ultimate parent of AGE is Assured Guaranty Ltd. ("AGL" and, together with its subsidiaries, "Assured Guaranty"). AGL is a Bermuda-based holding company that provides, through its operating subsidiaries, credit protection products to the public finance, infrastructure and structured finance markets in the EEA, the United States ("U.S."), and in other jurisdictions around the world.

In July 2013, as part of a series of transactions that AGL completed to increase the capitalization of one of the Company's affiliates, Municipal Assurance Corp., to $800 million on a statutory basis, Assured Guaranty Municipal Insurance Company ("AGMIC") was merged into AGM, with AGM as the surviving company. Up to that point, AGMIC was the immediate parent company of AGE.

Solvency II Directive

The Company has invested significant financial and management resources into conforming with the requirements established by the European Union's "Solvency II" directive (Directive 2009/138/EC). The Company intends to use the Standard Formula, which was developed by the European Insurance and Occupational Pensions Authority under the direction of the European Commission, for the calculation of its Solvency Capital Requirement. The date for the scheduled adoption of Solvency II is 1 January 2016.

Prior to the adoption of Solvency II, the Company is required to assess and manage the risks to which it is exposed and to make an assessment of its capital needs - referred to as an individual capital assessment or "ICA". The U.K. PRA supplements the Company's own ICA with a requirement that the Company maintain a level of capital determined by reference to a "financial guarantee benchmark" capital adequacy model ("Benchmark Model"). The U.K. PRA may, after review of the Company's ICA and the results of the Benchmark Model, require the Company to undertake further analysis of its capital needs, following which the U.K. PRA may issue individual capital guidance setting out the level of capital the U.K. PRA believes the Company should maintain, which may be in excess of that required by the Benchmark Model.

Basis of Presentation

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") and, in the opinion of management, reflect all adjustments that are of a normal recurring nature necessary for a fair statement of the financial condition, results of operations and cash flows of the Company for the periods presented. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The consolidated financial statements include the accounts of AGE and its affiliate, AGCPL. Intercompany accounts and transactions between the consolidated entities have been eliminated.

Significant Accounting Policies

The Company's functional currency is the U.S. dollar. The Company revalues assets, liabilities, revenue and expenses denominated in non-U.S. currencies into U.S. dollars using applicable exchange rates and reports related gains and losses in the consolidated statement of operations. Monetary assets and liabilities denominated in foreign currencies are translated at the spot rate at the balance sheet date. Non-monetary assets and liabilities are recorded at historical rates. Revenues and expenses denominated in foreign currencies are translated at average rates prevailing during the year.

The chief operating decision maker manages the operations of the Company at a consolidated level. Therefore, all results of operations are reported as one segment.

Other significant accounting policies are included in the following notes.

Significant Accounting Policies

Premium revenue recognition	Note 4
Policy acquisition cost	Note 5
Expected loss to be paid (Insurance and Credit Derivatives)	Note 6
Loss and loss adjustment expense (Insurance Contracts)	Note 7
Fair value measurement	Note 8
Credit derivatives	Note 9
Variable interest entities	Note 10
Investments and Cash	Note 11
Income Taxes	Note 13
Reinsurance and Other Monoline Exposures	Note 14

Future Application of Accounting Standards

Consolidation

In February 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-02, Consolidation *(Topic 810): Amendments to the Consolidation Analysis*, which is intended to improve certain areas of consolidation guidance for legal entities such as limited partnerships, limited liability companies, and securitization structures. The ASU will be effective on January 1, 2016. Early adoption is permitted, including adoption in an interim period. The Company does not expect that ASU 2015-02 will have any material effect on its Consolidated Financial Statements.

2. Rating Actions

When a rating agency assigns a public rating to a financial obligation guaranteed by AGE, it generally awards that obligation the same rating it has assigned to the financial strength of the insurance company. Investors in products guaranteed by AGE frequently rely on ratings published by the rating agencies because such ratings influence the trading value of securities and form the basis for many institutions' investment guidelines as well as individuals' bond purchase decisions. Therefore, AGE manages its business with the goal of achieving strong financial strength ratings. However, the methodologies and models used by rating agencies differ, presenting conflicting goals that may make it inefficient or impractical to reach the highest rating level. The methodologies and models are not fully transparent, contain subjective elements and data (such as assumptions about future market demand for AGE's products) and change frequently. Ratings are subject to continuous review and revision or withdrawal at any time. If the financial strength ratings of AGE were reduced below current levels, AGE expects that could have adverse effects on the Company's future business opportunities as well as the premiums the Company could charge for its insurance policies. For a discussion of other effects of rating actions on AGE, see Note 14, Reinsurance and Other Monoline Exposures

In the last several years, Standard & Poor's Ratings Services ("S&P") and Moody's Investors Service, Inc. ("Moody's") have changed, multiple times, their financial strength ratings of AGE, or changed the outlook on such ratings. The rating agencies' most recent actions and proposals related to AGE are:

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

- On July 2, 2014, Moody's affirmed AGE's A2 (stable outlook) financial strength ratings.

- On January 20, 2015, Moody's adopted changes to its credit methodology for financial guaranty insurance companies, and on February 18, 2015 Moody's published a credit opinion maintaining its existing ratings of AGE under that new methodology.

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

3. Outstanding Exposure

The Company's financial guaranty contracts are written in either insurance or credit derivative form, but collectively are considered financial guaranty contracts. The Company seeks to limit its exposure to losses by underwriting obligations that are investment grade at inception, diversifying its insured portfolio and maintaining rigorous subordination or collateralization requirements on structured finance obligations. The Company also has utilized reinsurance by ceding business to third-party and affiliated reinsurers.

Significant Risk Management Activities

Assured Guaranty's Portfolio Risk Management Committee, which includes members of senior management and senior credit and surveillance officers of the Company, sets specific risk policies and limits and is responsible for enterprise risk management, establishing the Company's risk appetite, credit underwriting of new business, surveillance and work-out.

Surveillance personnel are responsible for monitoring and reporting on all transactions in the insured portfolio. The primary objective of the surveillance process is to monitor trends and changes in transaction credit quality, detect any deterioration in credit quality, and recommend to management such remedial actions as may be necessary or appropriate. All transactions in the insured portfolio are assigned internal credit ratings, and surveillance personnel are responsible for recommending adjustments to those ratings to reflect changes in transaction credit quality.

Work-out personnel are responsible for managing work-out and loss mitigation situations, working with surveillance and legal personnel (as well as outside vendors) as appropriate. They develop strategies for the Company to enforce its contractual rights and remedies and to mitigate its losses, engage in negotiation discussions with transaction participants and, when necessary, manage (along with legal personnel) the Company's litigation proceedings.

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 investment grade credits to determine whether any need to be internally downgraded to BIG and refreshes its internal credit ratings on individual credits in quarterly, semi-annual or annual cycles based on the Company’s view of the credit’s quality, loss potential, volatility and sector. Ratings on credits in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter. The Company models the performance of many of its structured finance transactions as part of its periodic internal credit rating review of them.

Credits identified as BIG are subjected to further review to determine the probability of a loss. See Note 6, Expected Loss to be Paid for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. For surveillance purposes, the Company calculates present value using a constant discount rate of 5%. (A risk-free rate is used for calculating the expected loss for financial statement measurement purposes.)

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

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

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

- BIG Category 3: Below-investment-grade transactions for which future losses are expected and on which claims (other than liquidity claims) have been paid.

Components of Outstanding Exposure

Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding	
	December 31, 2014	December 31, 2013	December 31, 2014	December 31, 2013
	(in thousands)			
Public finance	$ 49,944,212	$ 55,276,769	$ 943,568	$ 995,243
Structured finance	1,322,887	2,393,545	30,549	53,837
Total financial guaranty	$ 51,267,099	$ 57,670,314	$ 974,117	$ 1,049,080

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

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2014

	Public Finance		Structured Finance		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
	(dollars in thousands)					
AAA	$ 68	0.0%	$ 10,913	39.1%	$ 10,981	2.4%
AA	7,958	1.8	8,743	31.3	16,701	3.6
A	100,509	23.1	2,432	8.7	102,941	22.2
BBB	311,932	71.6	4,564	16.4	316,496	68.3
BIG	15,034	3.5	1,256	4.5	16,290	3.5
Total net par outstanding	$ 435,501	100.0%	$ 27,908	100.0%	$ 463,409	100.0%

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

Rating Category	Public Finance		Structured Finance		Total	
	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
			(dollars in thousands)			
AAA	$ 86	0.0%	$ 28,473	56.9%	$ 28,559	5.7%
AA	9,051	2.0	10,296	20.6	19,347	3.8
A	99,315	22.0	2,177	4.3	101,492	20.3
BBB	324,393	72.0	7,602	15.2	331,995	66.3
BIG	17,899	4.0	1,520	3.0	19,419	3.9
Total net par outstanding	$ 450,744	100.0%	$ 50,068	100.0%	$ 500,812	100.0%

Financial Guaranty Portfolio
by Sector

Sector	As of December 31, 2014	As of December 31, 2013
	(in thousands)	
Public finance:		
Non-U.S. Public infrastructure finance	$ 227,705	$ 238,400
Non-U.S. Utility finance	153,019	148,676
Non-U.S. Municipal and other public finance	54,777	63,668
Total public finance	435,501	450,744
Structured finance:		
Non-U.S. Residential mortgage-backed security (“RMBS”)	19,222	22,746
U.S. and non-U.S. Pooled corporate obligations	8,686	27,322
Total structured finance	27,908	50,068
Total net par outstanding	$ 463,409	$ 500,812

Actual maturities of insured obligations could differ from contractual maturities because borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties. The expected maturities of structured finance obligations are, in general, considerably shorter than the contractual maturities for such obligations.

Expected Amortization of
Net Par Outstanding
As of December 31, 2014

	(in thousands)
0 to 5 years	$ 40,384
5 to 10 years	61,091
10 to 15 years	38,351
15 to 20 years	56,499
20 years and above	267,084
Total net par outstanding	$ 463,409

Geographic Distribution of Net Par Outstanding

The Company seeks to maintain a diversified portfolio of insured obligations designed to spread its risk across a number of geographic areas.

Geographic Distribution of Net Par Outstanding
As of December 31, 2014

	Number of Risks	Net Par Outstanding	Percent of Total Net Par Outstanding
		(dollars in thousands)	
Country			
United Kingdom	69	$ 318,305	68.7%
France	8	60,250	13.0
Italy	8	40,277	8.7
Japan	8	14,605	3.2
Spain	2	9,036	1.9
Hungary	2	7,860	1.7
Poland	1	6,278	1.3
Germany	1	2,603	0.6
USA	1	1,257	0.3
Mexico	1	928	0.2
Other	1	2,010	0.4
Total	102	$ 463,409	100.0%

Exposure to the Selected European Countries

Several European countries continue to experience significant economic, fiscal and/or political strains such that the likelihood of default on obligations with a nexus to those countries may be higher than the Company anticipated when such factors did not exist. The European countries where the Company has exposure and believes heightened uncertainties exist are: Hungary, Italy, Portugal and Spain (collectively, the “Selected European Countries”). The Company is closely monitoring its exposures in the Selected European Countries where it believes heightened uncertainties exist. Previously, the Company had included Ireland on this list but removed it during the third quarter of 2014 because of Ireland's strengthening economic performance and improving prospects; in 2014, Ireland's long-term foreign currency rating was upgraded one notch by S&P

(to ‘A-’) and three notches by Moody’s (to ‘Baa1’). The Company’s direct economic exposure to the Selected European Countries (based on par for financial guaranty contracts and notional amount for financial guaranty contracts accounted for as derivatives) is shown in the following table, net of ceded reinsurance.

Net Direct Economic Exposure to Selected European Countries(1)
As of December 31, 2014

	Hungary	Italy	Spain	Total
	(in thousands)			
Sovereign and sub-sovereign exposure:				
Non-infrastructure public finance (2)	$ —	$ 30,824	$ 2,074	$ 32,898
Infrastructure finance	6,603	103	6,356	13,062
Total sovereign and sub-sovereign	$ 6,603	$ 30,927	$ 8,430	$ 45,960
Non-sovereign exposure:				
Regulated utilities	—	1,629	—	1,629
RMBS	1,257	7,429	—	8,686
Total non-sovereign exposure	1,257	9,058	—	10,315
Total	$ 7,860	$ 39,985	$ 8,430	$ 56,275
Total BIG (See Note 6)	$ 7,860	$ —	$ 8,430	$ 16,290

____

(1) While the Company’s exposures are shown in U.S. dollars, the obligations the Company insures are in various currencies, primarily Euros. One of the RMBS included in the table above includes residential mortgages in both Italy and Germany, and only the portion of the transaction equal to the portion of the original mortgage pool in Italian mortgages is shown in the table.

(2) The exposure shown in the "Non-infrastructure public finance" category is from transactions backed by receivable payments from sub-sovereigns in Italy and Spain. Sub-sovereign debt is debt issued by a governmental entity or government backed entity, or supported by such an entity, that is other than direct sovereign debt of the ultimate governing body of the country.

When the Company directly insures an obligation, it assigns the obligation to a geographic location or locations based on its view of the geographic location of the risk.

The Company has excluded from the exposure tables above its indirect economic exposure to the Selected European Countries through policies it provides on pooled corporate transactions. The Company calculates indirect exposure to a country by multiplying the par amount of a transaction insured by the Company times the percent of the relevant collateral pool reported as having a nexus to the country. On that basis, the Company has calculated exposure of $0.9 million to Selected European Countries in transactions with $16.3 million of net par outstanding.

4. Financial Guaranty Insurance Premiums

The portfolio of outstanding exposures discussed in Note 3, Outstanding Exposure, includes financial guaranty contracts that meet the definition of insurance contracts as well as those that meet the definition of a derivative under GAAP. Amounts presented in this note relate only to financial guaranty insurance contracts. See Note 9, Financial Guaranty Contracts Accounted for as Credit Derivatives for amounts that relate to CDS.

Accounting Policies

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 the contract was written on a direct basis, assumed from another financial guarantor under a reinsurance treaty, ceded to another insurer under a reinsurance treaty, or acquired in a business combination.

Premium receivables comprise the present value of contractual or expected future premium collections discounted using a risk-free rate.

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

- For premiums received upfront on financial guaranty insurance contracts that were originally underwritten by the Company, 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 that were originally underwritten by the Company unearned premium reserve is the present value of either (1) contractual premiums due or (2) in cases where the underlying collateral is comprised of homogeneous pools of assets, the expected premiums to be collected over the life of the contract. To be considered a homogeneous pool of assets prepayments must be contractually prepayable, the amount of prepayments must be probable, and the timing and amount of prepayments must be reasonably estimable. 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 and prospective changes are recognized in premium reserves. 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. 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.

The Company recognizes unearned premium reserve as earned premium over the contractual period or expected 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 principal 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 principal amounts outstanding in the reporting period compared with the sum of each of the insured principal 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.

Financial Guaranty Insurance Premiums

Unearned premium reserve ceded to reinsurers (ceded unearned premium reserve) is recorded as an asset. Direct, assumed and ceded earned premium revenue are presented together as net earned premiums in the statement of operations. Net earned premiums comprise the following:

Net Earned Premiums

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Scheduled net earned premiums	$ (119)	$ (354)
Acceleration of net earned premiums	(48)	307
Accretion of discount on net premiums receivable	(185)	263
Net earned premiums	$ (352)	$ 216

(1) Negative net earned premiums are due to cessions of commutation premiums.

Gross Premium Receivable
Roll Forward

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Beginning of period, December 31	$ 350,436	$ 370,188
Gross premium written	478	1,285
Gross premiums received	(27,810)	(34,832)
Adjustments:		
Changes in the expected term of financial guaranty insurance contracts	(2,267)	(4,756)
Accretion of discount	11,405	11,497
Foreign exchange translation	(25,906)	7,054
End of period, December 31	$ 306,336	$ 350,436

Foreign exchange translation relates to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 99.4%, and 99.5% of installment premiums at December 31, 2014 and 2013, respectively, are denominated in currencies other than the U.S. dollar, primarily the Euro and British Pound Sterling.

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

Expected Collections of
Gross Premiums Receivable,
(Undiscounted)

	As of December 31, 2014
	(in thousands)
2015 (January 1 - March 31)	$ 9,187
2015 (April 1 - June 30)	11,507
2015 (July 1 - September 30)	6,051
2015 (October 1 - December 31)	6,908
2016	25,362
2017	24,324
2018	22,639
2019	22,458
2020-2024	102,400
2025-2029	81,773
2030-2034	62,170
After 2034	69,772
Total	$ 444,551

Scheduled Net Earned Premiums

	As of December 31, 2014
	(in thousands)
2015 (January 1 - March 31)	$ (189)
2015 (April 1 - June 30)	(193)
2015 (July 1 - September 30)	(196)
2015 (October 1- December 31)	(199)
Subtotal 2015	(777)
2016	(772)
2017	(788)
2018	(755)
2019	(727)
2020- 2024	(3,513)
2025 - 2029	(3,165)
2030 - 2034	(2,464)
After 2034	(6,987)
Net unearned premium reserve	(19,948)
Future accretion	3,643
Total future net earned premiums	$ (16,305)

Selected Information for Policies Paid in Installments

	As of December 31, 2014	As of December 31, 2013
	(dollars in thousands)	
Premiums receivable	$ 306,336	$ 350,436
Gross unearned premium reserve	383,636	409,421
Weighted-average risk-free rate used to discount premiums	3.8%	3.8%
Weighted-average period of premiums receivable (in years)	11.4	11.7

5. Financial Guaranty Insurance Acquisition Costs

Accounting Policy

Policy acquisition costs that are directly related and essential to successful insurance contract acquisition and ceding commission income on ceded reinsurance contracts are deferred for contracts accounted for as insurance and reported net. Amortization of deferred ceding commissions includes the accretion of discount on ceding commission income and expense. Acquisition costs associated with derivative contracts are not deferred.

These costs include expenses such as the cost of underwriting personnel attributable to successful underwriting efforts. Ceding commission income on ceded reinsurance contracts that are associated with premiums received in installments are calculated at their contractually defined rates and included in deferred acquisition costs ("DAC"), with a corresponding offset to net premiums receivable or reinsurance balances payable. Management uses its judgment in determining the type and amount of costs to be deferred. The Company conducts an annual study to determine which operating costs qualify for deferral. 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. DAC, net of deferred ceding commission income, is amortized in proportion to net earned premiums. When an insured obligation is retired early, the remaining related DAC, net of ceding commission income is recognized at that time.

Expected losses and loss adjustment expenses (“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 Ceding Commissions,
Net of DAC

	Year Ended December 31, 2014	Year Ended December 31, 2013
	(in thousands)	
Beginning of period	$ 183,063	$ 197,705
Amounts deferred during the period:		
Commissions on ceded business	6,957	(1,412)
Overheads and premium taxes	3	(223)
Total	6,960	(1,635)
Amounts amortized during the period	(9,641)	(13,007)
End of period	$ 180,382	$ 183,063

6. Expected Loss to be Paid

The insured portfolio includes policies accounted for under two separate accounting models depending on the characteristics of the contract. The Company may pay future losses on policies which fall under either of the two accounting models. The following provides a summarized description of the two accounting models prescribed by GAAP with a reference to the notes that describe the accounting policies and required disclosures throughout this report. The two models are insurance and derivatives.

In order to effectively evaluate and manage the economics and liquidity of the entire insured portfolio, management compiles and analyzes loss information for all policies on a consistent basis. The Company monitors and assigns ratings and calculates expected losses in the same manner for all its exposures regardless of form or differing accounting models.

This note provides information regarding expected claim payments to be made under all contracts in the insured portfolio. Net expected loss to be paid in the tables below consists of the present value of future: expected claim and LAE payments, expected recoveries in the transaction structures, cessions to reinsurers, and other loss mitigation strategies. 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, regardless of the accounting model. Expected loss to be paid is an important measure used by management to analyze the net economic loss on all contacts.

Accounting Policy

Insurance Accounting

For contracts accounted for as financial guaranty insurance, loss and LAE reserve is recorded only to the extent and for the amount that expected losses to be paid exceed unearned premium reserve. As a result, the Company has expected loss to be paid that have not yet been expensed. Such amounts will be recognized in future periods as unearned premium reserve amortizes into income. Expected loss to be expensed is important because it presents the Company's projection of incurred losses that will be recognized in future periods (excluding accretion of discount). See Note 7, Financial Guaranty Insurance Losses.

There were no expected loss to be paid for credit derivative contracts for 2014 and 2013. The expected loss to be paid in this note relates only to contracts accounted for as financial guaranty insurance.

Expected Loss to be Paid

The expected loss to be paid is equal to the present value of expected future cash outflows for claim and LAE payments, net of inflows for expected salvage and subrogation, using current risk-free rates. Net expected loss to be paid is defined as expected loss to be paid, net of amounts ceded to reinsurers.

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

Economic Loss Development

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

Loss Estimation Process

The Company's loss reserve committees estimate expected loss to be paid for all contracts. Surveillance personnel present analyses related to potential losses to the Company's loss reserve committees for consideration in estimating the expected loss to be paid. Such analyses include the consideration of various scenarios with corresponding probabilities assigned to them. Depending upon the nature of the risk, the Company's view of the potential size of any loss and the information available to the Company, that analysis may be based upon individually developed cash flow models, internal credit rating assessments and sector-driven loss severity assumptions or judgmental assessments. The Company's loss reserve committees review and refresh the estimate of expected loss to be paid each quarter. The Company's estimate of ultimate loss on a policy is subject to significant uncertainty over the life of the insured transaction due to the potential for significant variability in credit performance as a result of economic, fiscal and financial market variability over the long duration of most contracts. The determination of expected loss to be paid is an inherently subjective process involving numerous estimates, assumptions and judgments.

The following tables present a roll forward of the present value of net expected loss to be paid for financial guaranty contracts by sector. The Company used weighted average risk-free rates that ranged from 0.0% to 1.50% as of December 31, 2014 and 0.0% to 2.82% as of December 31, 2013.

Net Expected Loss to be Paid,
Roll Forward by Sector
Year Ended December 31, 2014

	Net Expected Loss to be Paid as of December 31, 2013(2)	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid as of December 31, 2014
		(in thousands)		
Other structured finance	$ 19	$ 15	$ —	$ 34
Non-U.S. public finance	997	(119)	—	878
Total	$ 1,016	$ (104)	$ —	$ 912

Net Expected Loss to be Paid,
Roll Forward by Sector
Year Ended December 31, 2013

	Net Expected Loss to be Paid as of December 31, 2012	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid as of December 31, 2013
		(in thousands)		
Other structured finance	$ 38	$ (19)	$ —	$ 19
Non-U.S. public finance	851	146	0	997
Total	$ 889	$ 127	$ 0	$ 1,016

(1) Net of ceded paid losses, whether or not such amounts have been settled with reinsurers. Ceded paid losses are typically settled 45 days after the end of the reporting period. Such amounts are recorded in reinsurance recoverable on paid losses included in other assets. The Company did not pay LAE for the years ended December 31, 2014 and 2013.

Certain Selected European Country Transactions

The Company guarantees credits with sub-sovereign exposure to various Spanish issuers where a Spanish sovereign default may cause the regions also to default. The Company's gross exposure to these credits is $504 million and its exposure net of reinsurance is $8 million. The Company rates all of these issuers in the BB category due to the financial condition of Spain and their dependence on the sovereign. The Company's Hungary exposure is to infrastructure bonds dependent on payments from Hungarian governmental entities and covered mortgage bonds issued by Hungarian banks. The Company's gross exposure to these Hungarian credits is $398 million and its exposure net of reinsurance is $8 million, all of which is rated BIG. The Company estimated net expected losses of $0.9 million related to these Spanish and Hungarian credits. The positive economic loss development during 2014 was approximately $0.1 million, which was primarily attributable to the favorable movement in the exchange rates between the U.S. Dollar and both the Euro and Hungarian Forint during the year.

7. Financial Guaranty Insurance Losses

Accounting Policies

Loss and LAE Reserve

Loss and LAE reserve reported on the balance sheet relates only to direct contracts that are accounted for as insurance, all of which are financial guaranty insurance contracts. The corresponding reserve ceded to reinsurers is reported as reinsurance recoverable on unpaid losses. As discussed in Note 8, Fair Value Measurement, contracts that meet the definition of a derivative, are recorded separately at fair value. Any expected losses on credit derivatives, if applicable, are not recorded as loss and LAE reserve on the consolidated balance sheet.

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 an insurance contract is only recorded when the expected loss to be paid exceeds the unearned premium reserve on a contract by contract basis.

Expected Loss to be Expensed

Expected loss to be expensed represents past or expected future net claim payments that have not yet been expensed. Such amounts will be expensed in future periods as deferred premium revenue 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.

Insurance Contracts' Loss Information

The following table provides balance sheet information on loss and LAE reserves and salvage and subrogation recoverable, net of reinsurance. The Company used weighted average risk-free rates for financial guaranty insurance obligations that ranged from 0.0% to 2.95% as of December 31, 2014 and 0.0% to 2.82% as of December 31, 2013. The Company had no financial guaranty insurance expected LAE reserve as of December 31, 2014 and December 31, 2013.

Loss and LAE Reserve
Net of Reinsurance
Insurance Contracts

	As of December 31, 2014	As of December 31, 2013
	(in thousands)	
Other structured finance	$ 32	$ —
Non-U.S. public finance	658	767
Total	$ 690	$ 767

The following table reconciles the reported gross and ceded reserve amount to the financial guaranty net reserves in the financial guaranty BIG transaction loss summary tables.

Components of Net Reserves
Insurance Contracts

	As of December 31, 2014	As of December 31, 2013
	(in thousands)	
Loss and LAE reserve	$ 47,909	$ 52,849
Reinsurance recoverable on unpaid losses	(47,219)	(52,082)
Financial guaranty net reserves	$ 690	$ 767

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

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

	As of December 31, 2014
	(in thousands)
Net expected loss to be paid	$ 912
Loss and LAE reserve, net of reinsurance	(690)
Net expected loss to be expensed (present value)	$ 222

The following table provides a schedule of the expected timing of net expected losses to be expensed. The amount and timing of actual loss and LAE may differ from the estimates shown below due to factors such as refundings, accelerations, commutations, changes in expected lives and updates to loss estimates.

Net Expected Loss to be Expensed
Financial Guaranty Insurance Contracts

	As of December 31, 2014
	(in thousands)
2015 (January 1 - March 31)	$ 7
2015 (April 1 - June 30)	6
2015 (July 1 - September 30)	6
2015 (October 1- December 31)	6
Subtotal 2015	25
2016	24
2017	22
2018	21
2019	19
2020 - 2024	73
2025 - 2029	33
2030 - 2033	5
Net expected loss to be expensed	222
Discount	11
Total future value	$ 233

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

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Structured finance	$ 32	$ —
Non-U.S. public finance	(108)	86
Total loss and LAE	$ (76)	$ 86

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

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of December 31, 2014

	BIG Categories						
	BIG 1		BIG 2		BIG 3		Total BIG, Net
	Gross	Ceded	Gross	Ceded	Gross	Ceded	
	(dollars in thousands)						
Number of risks(1)	4	(4)	—	—	—	—	4
Remaining weighted-average contract period (in years)	8.0	8.0	—	—	—	—	7.9
Outstanding exposure:							
Principal	$ 901,502	$ (885,212)	$ —	$ —	$ —	$ —	$ 16,290
Interest	377,450	(371,262)	—	—	—	—	6,188
Total	$ 1,278,952	$ (1,256,474)	$ —	$ —	$ —	$ —	$ 22,478
Expected cash outflows (inflows)	$ 56,110	$ (55,187)	$ —	$ —	$ —	$ —	$ 923
Potential recoveries	—	—	—	—	—	—	—
Subtotal	56,110	(55,187)	—	—	—	—	923
Discount	(649)	638	—	—	—	—	(11)
Present value of expected cash flows	$ 55,461	$ (54,549)	$ —	$ —	$ —	$ —	$ 912
Deferred premium revenue	$ 7,553	$ (7,331)	$ —	$ —	$ —	$ —	$ 222
Reserves(2)	$ 47,909	$ (47,219)	$ —	$ —	$ —	$ —	$ 690

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of December 31, 2013

	BIG Categories						
	BIG 1		BIG 2		BIG 3		Total BIG, Net
	Gross	Ceded	Gross	Ceded	Gross	Ceded	
	(dollars in thousands)						
Number of risks(1)	4	(4)	—	—	—	—	4
Remaining weighted-average contract period (in years)	8.7	8.7	—	—	—	—	8.6
Outstanding exposure:							
Principal	$ 1,068,440	$ (1,049,021)	$ —	$ —	$ —	$ —	$ 19,419
Interest	477,971	(470,113)	—	—	—	—	7,858
Total	$ 1,546,411	$ (1,519,134)	$ —	$ —	$ —	$ —	$ 27,277
Expected cash outflows (inflows)	$ 64,659	$ (63,591)	$ —	$ —	$ —	$ —	$ 1,068
Potential recoveries	—	—	—	—	—	—	—
Subtotal	64,659	(63,591)	—	—	—	—	1,068
Discount	(3,218)	3,166	—	—	—	—	(52)
Present value of expected cash flows	$ 61,441	$ (60,425)	$ —	$ —	$ —	$ —	$ 1,016
Deferred premium revenue	$ 20,296	$ (19,912)	$ —	$ —	$ —	$ —	$ 384
Reserves(2)	$ 52,849	$ (52,082)	$ —	$ —	$ —	$ —	$ 767

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

(2) See table “Components of net reserves.”

8. Fair Value Measurement

The Company carries its investment portfolio and credit derivative contracts 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 2014, no changes were made to the Company’s valuation models that had or are expected to have, a material impact on the Company’s consolidated balance sheets or statements of operations and comprehensive income.

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

The fair value hierarchy is determined based on whether the inputs to valuation techniques used to measure fair value are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Company estimates of market assumptions. The fair value hierarchy prioritizes model inputs into three broad levels as follows, with Level 1 being the highest and Level 3 the lowest. An asset or liability’s categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation.

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

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

Level 3—Model derived valuations in which one or more significant inputs or significant value drivers are unobservable. Financial instruments are considered Level 3 when their values are determined using pricing models, discounted

cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation.

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

Measured and Carried at Fair Value

Fixed-Maturity Securities and Short-Term Investments

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

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

Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company’s credit derivatives consist of insured CDS contracts that fall under derivative accounting standards requiring fair value accounting through the statement of operations. The Company does not enter into CDS with the intent to trade these contracts and the Company may not unilaterally terminate a CDS contract absent an event of default or termination event that entitles the Company to terminate; however, the Company has mutually agreed with various counterparties to terminate certain CDS transactions. Such terminations generally are not completed at fair value but instead for an amount that approximates the present value of future premiums.

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

Due to the lack of quoted prices and other observable inputs for its instruments or for similar instruments, the Company determines the fair value of its credit derivative contracts primarily through internally developed, proprietary models that use both observable and unobservable market data inputs to derive an estimate of the fair value of the Company's contracts in its principal markets (see "Assumptions and Inputs"). There is no established market where financial guaranty insured credit derivatives are actively traded, therefore, management has determined that the exit market for the Company’s credit

derivatives is a hypothetical one based on its entry market. Management has tracked the historical pricing of the Company's deals to establish historical price points in the hypothetical market that are used in the fair value calculation. These contracts are classified as Level 3 in the fair value hierarchy since there is reliance on at least one unobservable input deemed significant to the valuation model, most importantly the Company's estimate of the value of the non-standard terms and conditions of its credit derivative contracts and of the Company's current credit standing.

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

The fair value of the Company's credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay and the estimated present value of premiums that a financial guarantor of comparable credit-worthiness would hypothetically charge or pay at the reporting date for the same protection. The fair value of the Company's credit derivatives depends on a number of factors, including notional amount of the contract, expected term, credit spreads, changes in interest rates, the credit ratings of referenced entities, the Company's own credit risk and remaining contractual cash flows. The expected remaining contractual premium cash flows are the most readily observable inputs since they are based on the CDS contractual terms. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. Consistent with previous years, market conditions at December 31, 2014 were such that market prices of the Company's CDS contracts were not available.

Management considers factors such as current prices charged for similar agreements, when available, performance of underlying assets, life of the instrument, and the nature and extent of activity in the financial guaranty credit derivative marketplace. The assumptions that management uses to determine the fair value may change in the future due to market conditions. Due to the inherent uncertainties of the assumptions used in the valuation models, actual experience may differ from the estimates reflected in the Company's consolidated financial statements and the differences may be material.

Assumptions and Inputs

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

· Gross spread.

· The allocation of gross spread among:

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

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

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

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

· The rates used to discount future expected premium cash flows ranged from 0.30% to 2.15% at December 31, 2014 and 0.29% to 2.90% at December 31, 2013.

The Company obtains gross spreads on its outstanding contracts from market data sources published by third parties (e.g. dealer spread tables for the collateral similar to assets within the Company's transactions), as well as collateral-specific

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

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

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

- Actual collateral specific credit spreads (if up-to-date and reliable market-based spreads are available).
- Deals priced or closed during a specific quarter within a specific asset class and specific rating. There were no deals closed during the period presented.
- Credit spreads interpolated based upon market indices.
- Credit spreads provided by the counterparty of the CDS.
- Credit spreads extrapolated based upon transactions of similar asset classes, similar ratings, and similar time to maturity.

Information by Credit Spread Type (1)

	As of December 31, 2014	As of December 31, 2013
Based on actual collateral specific spreads	—%	—%
Based on market indices	100%	100%
Provided by the CDS counterparty	—%	—%
Total	100%	100%

(1) Based on par.

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

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

The premium the Company receives is referred to as the "net spread." The Company's pricing model takes into account not only how credit spreads on risks that it assumes affect pricing, but also how the Company's own credit spread affects the pricing of its deals. The Company's own credit risk is factored into the determination of net spread based on the impact of changes in the quoted market price for credit protection bought on the Company, as reflected by quoted market prices on CDS referencing AGM, which the Company uses as a proxy for the Company's credit cost. For credit spreads on the Company's name, the Company obtains the quoted price of CDS contracts traded on AGM from market data sources published by third parties. The cost to acquire CDS protection referencing AGM affects the amount of spread on CDS deals that the Company retains and, hence, their fair value. As the cost to acquire CDS protection referencing AGM increases, the amount of premium the Company retains on a deal generally decreases. As the cost to acquire CDS protection referencing AGM decreases, the amount of premium the Company retains on a deal generally increases. In the Company's valuation model, the premium the Company captures is not permitted to go below the minimum rate that the Company would currently charge to assume similar risks. This assumption can have the effect of mitigating the amount of unrealized gains that are recognized on certain CDS contracts. As of December 31, 2014 and December 31, 2013, based on the number of deals of the Company's CDS contracts approximately 20% and 100%, respectively, are fair valued using this minimum premium. The Company corroborates the assumptions in its fair value model, including the portion of exposure to the Company hedged by its counterparties, with independent third parties each reporting period. The current level of the Company's own credit spread has resulted in the bank or deal originator hedging a significant portion of its exposure to the Company. This reduces the amount of contractual cash flows the Company can capture as premium for selling its protection. For the portion of risk on each credit derivative that is ceded to AGM, no adjustment is made to the fair value for additional credit risk as the credit rating of the Company and AGM are the same. For the portion of risk on each credit derivative that is ceded to external reinsurers or affiliated reinsurers with a lower credit rating, the Company makes an adjustment to the fair value for any additional credit risk associated with external reinsurers or affiliated reinsurers as applicable.

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

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

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

Example

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

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

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

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

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

Strengths and Weaknesses of Model

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

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

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

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

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

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

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

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

- At December 31, 2014 and 2013, the markets for the inputs to the model were highly illiquid, which impacts their reliability.

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

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

Not Carried at Fair Value

Financial Guaranty Insurance Contracts

The fair value of the Company's financial guaranty contracts accounted for as insurance was based on management's estimate of what a similarly rated financial guaranty insurance company would demand to acquire the Company's in-force book of financial guaranty insurance business. This amount was based on the pricing assumptions management has observed for portfolio transfers and acquisitions that have occurred in the financial guaranty market and included adjustments to the carrying value of unearned premium reserve for stressed losses, ceding commissions and return on capital. The significant inputs were not readily observable. The Company accordingly classified this fair value measurement as Level 3.

Other Assets

The Company's other assets consist predominantly of accrued interest, the carrying values of which approximate fair value.

Financial Instruments Carried at Fair Value

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

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2014

	Fair Value	Fair Value Hierarchy Level 1	Level 2	Level 3
	(in thousands)			
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Corporate securities	$ 87,178	$ —	$ 87,178	$ —
Non-U.S. government securities	187,322	—	187,322	—
Total fixed-maturity securities	274,500	—	274,500	—
Short-term investments	14,675	112	14,563	—
Credit derivative assets	6,869	—	—	6,869
Total assets carried at fair value	$ 296,044	$ 112	$ 289,063	$ 6,869
Liabilities:				
Credit derivative liabilities	$ 7,479	$ —	$ —	$ 7,479
Total liabilities carried at fair value	$ 7,479	$ —	$ —	$ 7,479

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2013

	Fair Value	Fair Value Hierarchy Level 1	Level 2	Level 3
	(in thousands)			
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Corporate securities	$ 73,649	$ —	$ 73,649	$ —
Asset-backed securities	172	—	172	—
Non-U.S. government securities	181,330	—	181,330	—
Total fixed-maturity securities	255,151	—	255,151	—
Short-term investments	6,727	106	6,621	—
Credit derivative assets	10,905	—	—	10,905
Total assets carried at fair value	$ 272,783	$ 106	$ 261,772	$ 10,905
Liabilities:				
Credit derivative liabilities	$ 15,939	$ —	$ —	$ 15,939
Total liabilities carried at fair value	$ 15,939	$ —	$ —	$ 15,939

Changes in Level 3 Fair Value Measurements

The table below presents a roll forward of the Company's Level 3 financial instruments carried at fair value on a recurring basis during the years ended December 31, 2014 and 2013.

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2014

	Credit Derivative Asset (Liability), net(2) (in thousands)
Fair value as of December 31, 2013	$ (5,034)
Total pretax realized and unrealized gains/(losses) recorded in: (1)	
Net income (loss)	942
Settlements	3,482
Fair value as of December 31, 2014	$ (610)
Change in unrealized gains/(losses) related to financial instruments held as of December 31, 2014	$ 580

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2013

	Credit Derivative Asset (Liability), net(2) (in thousands)
Fair value as of December 31, 2012	$ (973)
Total pretax realized and unrealized gains/(losses) recorded in: (1)	
Net income (loss)	3,936
Settlements	(7,997)
Fair value as of December 31, 2013	$ (5,034)
Change in unrealized gains/(losses) related to financial instruments held as of December 31, 2013	$ 193

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

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

Level 3 Fair Value Disclosures

Quantitative Information About Level 3 Fair Value Inputs
As of December 31, 2014

Financial Instrument Description (1)	Fair Value at December 31, 20143 (in thousands)		Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Liabilities:					
Credit derivative liabilities, net	$	(610	Hedge cost (in bps)	21.3 - 81.3	53.8
			Bank profit (in bps)	38.5 - 229.4	146.6
			Internal floor (in bps)	12.5 - 30.0	25.0
			Internal credit rating	AAA - BBB	AA

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

Quantitative Information About Level 3 Fair Value Inputs
As of December 31, 2013

Financial Instrument Description (1)	Fair Value at December 31, 2013 (in thousands)		Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Liabilities:					
Credit derivative liabilities, net	$	(5,034	Hedge cost (in bps)	55.0 - 131.3	79.8
			Bank profit (in bps)	66.0 - 421.7	188.9
			Internal floor (in bps)	12.5 - 30.0	25.0
			Internal credit rating	AAA - BBB	AA+

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

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

Fair Value of Financial Instruments

	As of December 31, 2014		As of December 31, 2013	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in thousands)			
Assets:				
Fixed-maturity securities	$ 274,500	$ 274,500	$ 255,151	$ 255,151
Short-term investments	14,675	14,675	6,727	6,727
Credit derivative assets	6,869	6,869	10,905	10,905
Financial guaranty insurance contracts(1)	114,957	120,003	105,624	104,391
Other assets	4,319	4,319	4,170	4,170
Liabilities:				
Credit derivative liabilities	7,479	7,479	15,939	15,939

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

9. Financial Guaranty Contracts Accounted for as Credit Derivatives

Accounting Policy

Credit derivatives are recorded at fair value. Changes in fair value are recorded in “net change in fair value of credit derivatives” on the consolidated statement of operations. Realized gains and other settlements on credit derivatives include credit derivative premiums received and receivable for credit protection the Company has sold under its insured CDS contracts, premiums paid and payable for credit protection the Company has purchased, claims paid and payable and received and receivable related to insured credit events under these contracts, ceding commissions expense or income and realized gains or losses related to their early termination. Fair value of credit derivatives is reflected as either net assets or net liabilities determined on a contract by contract basis in the Company’s consolidated balance sheets. See Note 8, Fair Value Measurement, for a discussion on the fair value methodology for credit derivatives.

Credit Derivatives

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

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

Fair Value of Credit Derivatives

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

	Year Ended December 31, 2014	Year Ended December 31, 2013
	(in thousands)	
Realized gains on credit derivatives	$ 362	$ 3,743
Net change in unrealized gains (losses) on credit derivatives		
Funded collateralized loan obligations (“CLOs”) and collateralized debt obligations	20	19
Other(1)	560	174
Net change in unrealized gains (losses) on credit derivatives(2)	580	193
Net change in fair value of credit derivatives	$ 942	$ 3,936

(1) “Other” includes all other international asset classes, such as commercial receivables and international infrastructure.

(2) Except for net estimated credit impairments (i.e., net expected loss to be paid as discussed in Note 6), the unrealized gains and losses on credit derivatives are expected to reduce to zero as the exposure approaches its maturity date. With considerable volatility continuing in the market, unrealized gains (losses) on credit derivatives may fluctuate significantly in future periods.

In 2014 and 2013, unrealized fair value gains were generated primarily by the run-off of par outstanding and the lapse of time in the other category as these transactions approach maturity.

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

The following table presents the net par outstanding and fair value for contracts accounted for as derivatives. There were no expected claim payments or recoveries as of December 31, 2014 and 2013.

Net Par Outstanding and Net Fair Value of Credit Derivatives by Sector

	Net Par Outstanding		Fair Value of Credit Derivative Asset (Liability), net	
Asset Type	As of December 31, 2014	As of December 31, 2013	As of December 31, 2014	As of December 31, 2013
	(in thousands)		(in thousands)	
CLOs/Collateralized bond obligations	$ 8,171	$ 25,203	$ 132	$ 194
Other	11,689	12,352	(742)	(5,228)
Total	$ 19,860	$ 37,555	$ (610)	$ (5,034)

10. Variable Interest Entities

The Company provides financial guaranties with respect to debt obligations of special purpose entities, including variable interest entities ("VIEs"). The Company does not sponsor any VIEs when underwriting third party financial guaranty insurance or credit derivative transactions, nor has it acted as the servicer or collateral manager for any VIE obligations that it insures. The transaction structure generally provides certain financial protections to the Company.

The Company is not primarily liable for the debt obligations issued by the VIEs it insures and would only be required to make payments on these insured debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due and only for the amount of the shortfall. The Company’s creditors do not have any rights with regard to the collateral supporting the debt issued by the FG VIEs.

Accounting Policy

The Company evaluates whether it is the primary beneficiary of its VIEs. If the Company concludes that it is the primary beneficiary it is required to consolidate the entire VIE in the Company's financial statements and eliminate the effects of the financial guaranty insurance contracts issued by AGE on the consolidated Financial Guaranty VIE ("FG VIEs") debt obligations.

The primary beneficiary of a VIE is the enterprise that has both 1) the power to direct the activities of a VIE that most significantly impact the entity's economic performance; and 2) the obligation to absorb losses of the entity that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE.

As part of the terms of its financial guaranty contracts, the Company obtains certain protective rights with respect to the VIE that are triggered by the occurrence of certain events, such as failure to be in compliance with a covenant due to poor deal performance or a deterioration in a servicer or collateral manager's financial condition. At deal inception, the Company typically is not deemed to control a VIE; however, once a trigger event occurs, the Company's control of the VIE typically increases. The Company continuously evaluates its power to direct the activities that most significantly impact the economic performance of VIEs that have debt obligations insured by the Company and, accordingly, where the Company is obligated to absorb VIE losses or receive benefits that could potentially be significant to the VIE. The Company obtains protective rights under its insurance contracts that give the Company additional controls over a VIE if there is either deterioration of deal performance or in the financial health of the deal servicer. The Company is deemed to be the control party for certain VIEs under GAAP, typically when its protective rights give it the power to both terminate and replace the deal servicer, which are characteristics specific to the Company's financial guaranty contracts. If the protective rights that could make the Company the control party have not been triggered, then the VIE is not consolidated. If the Company is deemed no longer to have those protective rights, the transaction is deconsolidated.

As of December 31, 2014, the Company had issued financial guaranty contracts for 29 VIEs that it did not consolidate. To date, the Company’s analyses have indicated that it does not have a controlling financial interest in any VIEs and, as a result, they are not consolidated in the consolidated financial statements. The Company’s exposure provided through its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 3, Outstanding Exposure.

11. Investments and Cash

Accounting Policy

The Company’s investment portfolio is composed 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 ("OTTI") securities are bifurcated between credit losses and non-credit changes in fair value. The credit loss on OTTI securities is recorded in the statement of operations and the non-credit component of the change in fair value of securities whether OTTI or not, is recorded in other comprehensive income ("OCI"). For securities 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, declines in fair value are 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 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.

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.

Assessment for Other-Than-Temporary Impairments

The amount of other-than-temporary-impairment recognized in earnings depends on whether (1) an entity intends to sell the security or (2) it is more-likely-than-not that the entity will be required to sell the security before recovery of its amortized cost basis.

If an entity does not intend to sell the security and it is not more-likely-than-not that the Company will be required to sell the security before recovery of its amortized cost basis, the other-than-temporary-impairment is separated into (1) the amount representing the credit loss and (2) the amount related to all other factors.

The Company has a formal review process to determine other-than-temporary-impairment 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;
- the impact of foreign exchange rates; 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 impaired and the net present value is less than the amortized cost of the investment, an other-than-temporary impairment 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 including default rates, recoveries and changes in value. The assumptions used in these projections requires the use of significant management judgment.

The Company's assessment of a decline in value included management's current assessment of the factors noted above. The Company also seeks advice from its outside investment managers. If that assessment changes in the future, the Company may ultimately record a loss after having originally concluded that the decline in value was temporary.

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 was $4.3 million and $4.2 million as of December 31, 2014 and December 31, 2013, respectively.

Net Investment Income

	Year Ended December 31, 2014	Year Ended December 31, 2013
	(in thousands)	
Income from fixed-maturity securities	$ 7,587	$ 7,060
Income from short-term investments	24	17
Other	13	—
Gross investment income	7,624	7,077
Investment expenses	(229)	(181)
Net investment income	$ 7,395	$ 6,896

Net Realized Investment Gains (Losses)

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Gross realized gains on investment portfolio	$ 2,923	$ 674
Gross realized losses on investment portfolio	(365)	(1,330)
Other-than-temporary impairment	(3,317)	(1,867)
Net realized investment gains (losses)	$ (759)	$ (2,523)

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

Roll Forward of Credit Losses in the Investment Portfolio

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Balance, beginning of period	$ —	$ 3,784
Additions for credit losses on securities for which an other-than-temporary-impairment was not previously recognized	3,317	1,867
Reductions for securities sold and disposed during the period	(2,980)	(5,651)
Balance, end of period	$ 337	$ —

Investment Portfolio

Fixed-Maturity Securities and Short-Term Investments by Security Type As of December 31, 2014

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI (2) Gain (Loss) on Securities with OTTI	Weighted Average Credit Quality(3)
	(dollars in thousands)						
Fixed-maturity securities:							
Corporate securities	29%	$ 83,990	$ 3,571	$ (383)	$ 87,178	$ —	AA
Non-U.S. government securities	66	193,234	3,780	(9,692)	187,322	—	AA+
Total fixed-maturity securities	95	277,224	7,351	(10,075)	274,500	—	AA+
Short-term investments	5	14,674	1	—	14,675	1	AAA
Total investment portfolio	100%	$ 291,898	$ 7,352	$ (10,075)	$ 289,175	$ 1	AA+

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

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI Gain (Loss) on Securities with OTTI	Weighted Average Credit Quality(3)
	(dollars in thousands)						
Fixed-maturity securities:							
Corporate securities	27%	$ 69,373	$ 4,328	$ (52)	$ 73,649	$ —	AA
Asset-backed securities	0	153	19	—	172	—	AAA
Non-U.S. government securities	70	181,336	6,897	(6,903)	181,330	—	AA+
Total fixed-maturity securities	97	250,862	11,244	(6,955)	255,151	—	AA+
Short-term investments	3	6,520	207	—	6,727	—	AAA
Total investment portfolio	100%	$ 257,382	$ 11,451	$ (6,955)	$ 261,878	$ —	AA+

____

(1) Based on amortized cost.

(2) Accumulated OCI ("AOCI"). See also Note 17, Other Comprehensive Income.

(3) Ratings in the tables above represent the lower of the Moody's and S&P classifications. The Company's portfolio consists primarily of high-quality, liquid instruments.

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

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2014

	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
	(dollars in thousands)					
Corporate securities	$ 16,966	$ (383)	$ —	$ —	$ 16,966	$ (383)
Non-U.S. government securities	64,991	(1,285)	43,159	(8,407)	108,150	(9,692)
Total	$ 81,957	$ (1,668)	$ 43,159	$ (8,407)	$ 125,116	$ (10,075)
Number of securities		16		2		18

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

	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
	(dollars in thousands)					
Corporate securities	$ 2,735	$ (33)	$ 2,271	$ (19)	$ 5,006	$ (52)
Non-U.S. government securities	11,858	(13)	67,306	(6,890)	79,164	(6,903)
Total	$ 14,593	$ (46)	$ 69,577	$ (6,909)	$ 84,170	$ (6,955)
Number of securities		3		7		10

At December 31, 2014 there were 18 securities where the aggregate amortized cost exceeded fair value by $10 million or 8% of their total fair value. At December 31, 2013 there were 10 securities where the aggregate amortized cost exceeded fair value by $7 million or 8% of their total fair value. The unrealized loss is primarily foreign exchange related and not specific to individual issuer credit. The Company has determined that these securities were not other-than-temporarily impaired as of December 31, 2014 and December 31, 2013.

The amortized cost and estimated fair value of available-for-sale fixed-maturity securities by contractual maturity as of December 31, 2014 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, 2014

	Amortized Cost	Estimated Fair Value
	(in thousands)	
Due within one year	$ 14,662	$ 12,244
Due after one year through five years	137,521	134,684
Due after five years through 10 years	122,547	124,708
Due after 10 years	2,494	2,864
Total	$ 277,224	$ 274,500

No material investments of the Company were non income producing for years ended December 31, 2014 and 2013, respectively.

12. Dividend

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

The Company did not declare or pay dividends during 2014 and 2013.

13. 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

In conjunction with AGL's purchase of Assured Guaranty Municipal Holdings Inc. on July 1, 2009, AGE joined the consolidated federal tax group of Assured Guaranty US Holdings Inc. ("AGUS"), an indirect parent holding company of AGE. A tax sharing agreement was entered into effective July 1, 2009 whereby each company in the AGUS consolidated tax group pays or receives its proportionate share of the consolidated federal tax burden for the group as if each company filed on a separate return basis with current period credit for net losses.

Provision for Income Taxes

The Company has made an election with the Internal Revenue Service pursuant to Section 953(d) of the Internal Revenue Code. Section 953(d) allows for certain foreign insurance companies to elect to be treated as a U.S. corporation for federal income tax purposes. The impact of the election is that the Company will be taxed as a U.S. corporation subject to tax on its worldwide income, subject to a credit for any taxes paid to a non-U.S. jurisdiction. As of December 31, 2014, the U.S. Federal tax rate was 35%, as compared with a tax rate in the United Kingdom of 21% as of that date, which rate became 20% on April 1, 2015.

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

Effective Tax Rate Reconciliation

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Expected tax provision (benefit) at statutory rate	$ 6,531	$ 4,990
Deferred inventory adjustment	0	(1,762)
U.K. tax benefit	—	(897)
Other	15	8
Total provision (benefit) for income taxes	$ 6,546	$ 2,339
Effective tax rate	35.1%	16.4%

The deferred inventory adjustment in the table above represents adjustments recorded in 2013 related to prior years, as a result of enhancements to the Company's analysis of the deferred tax inventory. The amount relates to the periods 2009 and prior.

The expected tax provision at statutory rates in taxable jurisdictions is calculated as the sum of pretax income in each jurisdiction multiplied by the statutory tax rate of the jurisdiction by which it will be taxed.

Components of Net Deferred Tax Assets

	As of December 31,	
	2014	2013
	(in thousands)	
Deferred tax assets:		
Deferred ceding commission	$ 64,846	$ 68,056
Foreign tax credit	—	25,672
Other	4,614	2,739
Total deferred income tax assets	69,460	96,467
Deferred tax liabilities:		
Unearned premium reserve, net of premiums receivable	(27,317)	(36,852)
Other	(5,923)	(3,756)
Total deferred income tax liabilities	(33,240)	(40,608)
Net deferred income tax asset	$ 36,220	$ 55,859

The Company has utilized all of its foreign tax credit carry-forward balances as of December 31, 2014.

There were no unrecognized tax benefits for the years ended December 31, 2014 and 2013, respectively.

Valuation Allowance

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

Audits

AGUS has open tax years with the U.S. Internal Revenue Service (“IRS”) for 2009 forward and is currently under audit for the 2009 - 2012 tax years. The IRS concluded its field work with respect to tax years 2006 through 2008 without adjustment. On February 20, 2013 the IRS notified AGUS that the Joint Committee on Taxation completed its review of the 2006 through 2008 tax years and has accepted the results of the IRS examination without exception. AGMH and subsidiaries have separate open tax years with the IRS of January 1, 2009 through the July 1, 2009 when they joined the AGUS consolidated group. The IRS concluded its field work with respect to tax years 2008 for AGMH and subsidiaries while members of the Dexia Holdings Inc. consolidated tax group without adjustment. The Company is indemnified by Dexia for any potential liability associated with any audit of any periods prior to the acquisition of AGMH. The Company is not currently under examination and has open tax years of 2012 forward.

Tax Treatment of CDS

The Company treats the guaranty it provides on CDS as an insurance contract for tax purposes and as such a taxable loss does not occur until the Company expects to make a loss payment to the buyer of credit protection based upon the occurrence of one or more specified credit events with respect to the contractually referenced obligation or entity. The Company holds its CDS to maturity, at which time any unrealized fair value loss in excess of credit-related losses would revert to zero. The tax treatment of CDS is an unsettled area of the law. The uncertainty relates to the IRS determination of the income or potential loss associated with CDS as either subject to capital gain (loss) or ordinary income (loss) treatment. In treating CDS as insurance contracts the Company treats both the receipt of premium and payment of losses as ordinary income and believes it is more likely than not that any CDS credit related losses will be treated as ordinary by the IRS. To the extent the IRS takes the view that the losses are capital losses in the future and the Company incurred actual losses associated with the CDS, the Company would need sufficient taxable income of the same character within the carryback and carryforward period available under the tax law.

14. Reinsurance and Other Monoline Exposures

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

Accounting Policy

For ceded business, the accounting model of the underlying direct financial guaranty contract dictates the accounting model used for the reinsurance contract. For any ceded financial guaranty insurance premiums, the accounting model described in Note 4 is followed, for ceded financial guaranty insurance losses, the accounting model in Note 7 is followed. For any ceded credit derivative contracts, the accounting model in Note 9 is followed.

Ceded Business

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

The Company cedes portions of its exposure to a diversified group of non-affiliated reinsurers, including other monolines, as of December 31, 2014. Over the past several years, the Company has entered into several commutations in order to reassume previously ceded books of business from its reinsurers. Upon reassuming such business from third party reinsurers in 2014, AGE ceded more than 90% of the reassumed business to AGM, pursuant to an approved intercompany pooling agreement. While certain Ceded Business has been reassumed, the Company still has Ceded Business with third parties.

Net Effect of Commutations of Ceded
Reinsurance Contracts

	Year Ended December 31, 2014	2013
	(in thousands)	
Increase in net unearned premium reserve	$ 12,535	$ 271
Increase in net par outstanding	484,127	22,162
Commutation gains recorded in other income	22,699	258

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

Effect of Reinsurance on Statement of Operations

	Year Ended December 31, 2014	2013
	(in thousands)	
Premiums Written:		
Direct (1)	$ (1,789)	$ (3,471)
Ceded (2)	(22,372)	4,494
Net	$ (24,161)	$ 1,023
Premiums Earned:		
Direct	$ 49,971	$ 65,446
Ceded	(50,323)	(65,230)
Net	$ (352)	$ 216
Loss and LAE:		
Direct	$ (4,940)	$ 8,493
Ceded	4,864	(8,407)
Net	$ (76)	$ 86

(1) Negative direct premiums written were due to cancellations and changes in expected debt service schedules.

(2) Positive ceded premiums written were due to cancellations, commutations and changes in expected debt service schedules.

Reinsurer Exposure

In addition to ceded reinsurance arrangements, the Company may also have exposure to some financial guaranty reinsurers (i.e., monolines) in other areas. Second-to-pay insured par outstanding represents transactions the Company has insured that were previously insured by other monolines. The Company underwrites such transactions based on the underlying insured obligation without regard to the primary insurer.

Exposure by Reinsurer

	Ratings at June 23, 2015		Par Outstanding (1) As of December 31, 2014	
Reinsurer	**Moody's Reinsurer Rating**	**S&P Reinsurer Rating**	**Ceded Par Outstanding**	**Second-to-Pay Insured Par Outstanding**
			(dollars in millions)	
Affiliated Companies	(2)	(2)	$ 21,152	$ —
Non-Affiliated Companies:				
Tokio Marine & Nichido Fire Insurance Co., Ltd.	Aa3 (3)	AA- (3)	1,226	—
Radian Asset Assurance Inc.	(4)	(4)	1,043	—
American Overseas Reinsurance Company Limited (f/k/a Ram Re)	WR (5)	WR	712	—
Mitsui Sumitomo Insurance Co. Ltd.	A1	A+ (3)	227	—
Swiss Reinsurance Co.	Aa3	AA-	26	—
Financial Guaranty Insurance Co	WR	WR	—	14
MBIA	(6)	(6)	—	13
Syncora Guarantee Inc	WR	WR	—	6
Total			$ 24,386	$ 33

(1) Includes par related to insured credit derivatives.

(2) The affiliated reinsurers to which AGE cedes exposure are Assured Guaranty Re Ltd. ("AG Re"), Assured Guaranty Re Overseas Ltd. ("AGRO") and AGM. Effective April 8, 2015, at the request of AG Re and AGRO, Moody's withdrew the financial strength ratings it had assigned to those insurers. Moody's assigns a financial strength rating of A2 (stable) to AGM. S&P assigns a financial strength rating of AA (stable) to each of AG Re, AGRO and AGM. Since May 5, 2015, A.M. Best Company, Inc. has assigned a financial strength rating of A+ (stable) to AGRO. Kroll Bond Rating Agency assigns a financial strength rating of AA+ (stable) to AGM.

(3) The Company has structural collateral agreements satisfying the triple-A credit requirement of S&P and/or Moody's.

(4) On April 1, 2015, AGC completed the acquisition of Radian Asset Assurance Inc. ("Radian Asset") and merged Radian Asset with and into AGC, with AGC as the surviving company of the merger.

(5) Represents "Withdrawn Rating."

(6) MBIA includes subsidiaries MBIA Insurance Corp., rated B by S&P and B2 by Moody's. and MBIA U.K. Insurance Ltd., rated B by S&P and Ba2 by Moody's.

Ceded Par Outstanding by Reinsurer and Credit Rating
As of December 31, 2014

Reinsurer	AAA	AA	A	BBB	BIG	Total
	(in millions)					
Affiliated Companies	$ 414	$ 479	$ 4,112	$ 15,433	$ 714	$ 21,152
Tokio Marine & Nichido Fire Insurance Co., Ltd.	97	27	423	590	89	1,226
Radian Asset Assurance Inc.	1	13	341	626	62	1,043
American Overseas Reinsurance Company Limited (f/k/a Ram Re)	25	9	164	494	20	712
Mitsui Sumitomo Insurance Co. Ltd.	3	2	93	129	—	227
Swiss Reinsurance Co.	—	—	—	26	—	26
Total	$ 540	$ 530	$ 5,133	$ 17,298	$ 885	$ 24,386

Second-to-Pay
Insured Par Outstanding by Rating
As of December 31, 2014(1)

	Public Finance		Structured Finance	
	A	BBB	BIG	Total
	(in millions)			
Financial Guaranty Insurance Co	$ 14	$ —	$ —	$ 14
MBIA Insurance Corporation	7	5	1	13
Syncora Guarantee Inc.	—	6	—	6
Total	$ 21	$ 11	$ 1	$ 33

(1) Assured Guaranty's internal rating.

Amounts Due (To) From Reinsurers
As of December 31, 2014

	Ceded Premium, net of Commissions	Ceded Expected Loss and LAE
	(in thousands)	
Affiliated Companies	$ (183,263)	$ 40,229
Tokio Marine & Nichido Fire Insurance Co., Ltd.	(8,647)	7,838
Radian Asset Assurance Inc.	(9,952)	4,773
American Overseas Reinsurance Company Limited.	(4,075)	1,709
Mitsui Sumitomo Insurance Co. Ltd.	(2,224)	—
Swiss Reinsurance Co.	(2,476)	—
Total	$ (210,637)	$ 54,549

15. Related Party Transactions

Cooperative Agreements

The Company is party to cooperative agreements with various affiliated entities for joint use of personnel and property. As such, the Company is allocated a portion of costs for personnel and services in accordance with the agreements. Amounts included in other liabilities at December 31, 2014 are $5.9 million and at December 31, 2013 are $5.0 million, respectively, for unsettled expense allocations due to/from affiliated entities. Amounts included in other operating expenses for the years ended December 31, 2014 and 2013 are $13.4 million and $11.1 million, respectively, for expense allocations. Including in these expense allocations are share-based and deferred cash-based compensation expenses allocated to the Company of $1.5 million and $2.0 million for the years ended December 31, 2014 and 2013, respectively.

Assured Guaranty Credit Protection Limited

The Company has issued financial guarantees that cover the obligations of AGCPL in respect of credit default swaps pursuant to which AGCPL sold credit protection to counterparties. AGCPL may incur losses in the event of payment defaults by the obligors referenced in such credit default swaps. AGCPL has not entered into a new credit default swap since 2008 and the Company does not intend to issue any new financial guarantees of such AGCPL obligations in the future.

Assured Guaranty Municipal Corp.

AGM currently provides support to its subsidiary AGE through a quota share and excess of loss reinsurance agreement (the "Reinsurance Agreement") and a net worth maintenance agreement (the "Net Worth Agreement"). Such agreements replace and supersede the second amended and restated quota share and stop loss reinsurance agreement and the second amended and restated net worth maintenance agreement, respectively, previously in place between the parties. For transactions closed prior to 2011, AGE typically guaranteed all of the guaranteed obligations directly and AGM reinsured under the quota share cover of the Reinsurance Agreement approximately 92% of AGE's retention after cessions to other reinsurers. In 2011, AGE and AGM implemented a co-guarantee structure pursuant to which (i) AGE directly guarantees a portion of the guaranteed obligations in an amount equal to what would have been AGE's pro rata retention percentage under the quota share cover, (ii) AGM directly guarantees the balance of the guaranteed obligations, and (iii) AGM also provides a second-to-pay guarantee for AGE's portion of the guaranteed obligations.

Under the excess of loss cover of the Reinsurance Agreement, AGM will pay AGE quarterly the amount by which (i) the sum of (a) AGE's incurred losses calculated in accordance with U.K. GAAP as reported by AGE in its financial returns filed with the U.K. PRA and (b) AGE's paid losses and LAE, in both cases net of all other performing reinsurance, including the reinsurance provided by AGM under the quota share cover of the Reinsurance Agreement, exceeds (ii) an amount equal to (a) AGE's capital resources under U.K. law minus (b) the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K. In addition, the Reinsurance Agreement permits AGE to terminate the Reinsurance Agreement upon the following events: a downgrade of AGM's ratings by Moody's below Aa3 or by S&P below AA- if the company fails to restore its rating(s) to the required level within a prescribed period of time; AGM's insolvency; failure by AGM to maintain the minimum capital required by its domiciliary jurisdiction; or AGM filing a petition in bankruptcy, going into liquidation or rehabilitation or having a receiver appointed. The Reinsurance Agreement also provides that no amounts are owing under the excess of loss cover (or the stop loss cover of the second amended and restated quota share and stop loss reinsurance agreement previously in place between the parties) with respect to any quarter ending prior to April 1, 2014.

The quota share and excess loss covers each exclude transactions guaranteed by AGE on or after July 1, 2009 that are not municipal, utility, project finance or infrastructure risks or similar types of risks.

The Reinsurance Agreement also contemplates the establishment of collateral by AGM to support its reinsurance obligations to AGE. In December 2014, to satisfy a new PRA requirement that AGM post collateral to support its reinsurance obligations to AGE, AGM and AGE amended the Reinsurance Agreement to incorporate the PRA's requirement. Pursuant to such amended Reinsurance Agreement, AGM's collateral requirement will be measured as of the end of each calendar quarter by (i) using the PRA's FG Benchmark Model to calculate at the 99.5% confidence interval the losses expected to be borne collectively by AGE's three affiliated reinsurers, AGM, AG Re and AGRO; (ii) deducting from such calculation AGE's capital resources under such model; and (iii) requiring AGM, AG Re and AGRO collectively to maintain collateral equal to fifty percent (50%) of such difference, i.e., the excess of AGM's, AG Re's and AGRO's assumed modeled losses over AGE's capital resources. The FG Benchmark Model is the model currently used by the PRA to determine the capital adequacy of UK financial guaranty companies. It broadly adopts Basel II's risk weighting approach for setting bank capital requirements, but with certain modifications to account for differences between banks and financial guarantors. In December 2014, AGM and AGE also entered into a related trust agreement pursuant to which AGM, prior to year-end, established, and deposited assets into a reinsurance trust account for the benefit of AGE to satisfy the PRA's collateral requirement as of September 30, 2014, as measured in accordance with such amended Reinsurance Agreement. The total collateral required to be funded into such reinsurance trust account by AGM as of December 31, 2014 was approximately £142 million.

Pursuant to the Net Worth Agreement, AGM is obligated to cause AGE to maintain capital resources equal to 110% of the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K., provided that AGM's contributions (a) do not exceed 35% of its policyholders' surplus on an accumulated basis as determined by the laws of the State of New York, and (b) are in compliance with Section 1505 of the New York Insurance Law. AGM has never been required to make any contributions to AGE's capital under the current Net Worth Agreement or the prior net worth maintenance agreement.

The amounts included in the financial statements resulting from such transactions with AGM are as follows:

	As of December 31,	
	2014	2013
	(in thousands)	
Balance sheets:		
Ceded unearned premium reserve	$ 519,511	$ 512,102
Reinsurance recoverable on paid losses	27,478	29,934
Net credit derivative assets	3,305	1,292
Deferred ceding commissions	(155,853)	(153,630)
Ceded premium payable, net of ceding commission	(154,105)	(175,208)
Additional information:		
Ceded par outstanding	$ 16,583,546	$ 18,072,109

The table below summarizes ceded activity to AGM reflected in the consolidated statements of operations.

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Statements of operations:		
Net earned premiums	$ (34,194)	$ (45,445)
Realized gains and other settlements on credit derivatives	(578)	(7,555)
Net unrealized gains (losses) on credit derivatives	(2,020)	(123)
Losses and loss adjustment expense incurred ceded	(2,456)	5,510

Assured Guaranty Re Ltd.

The Company cedes business to AG Re under certain reinsurance agreements. The following table summarizes the affiliated components of each balance sheet item, where applicable.

	As of December 31,	
	2014	2013
	(in thousands)	
Balance sheets:		
Ceded unearned premium reserve	$ 139,756	$ 148,698
Reinsurance recoverable on paid losses	6,280	7,364
Net credit derivative assets	1,523	(1,254)
Deferred ceding commissions	(40,572)	(43,155)
Ceded premium payable, net of ceding commission	(29,158)	(34,092)
Additional information:		
Ceded par outstanding	$ 4,568,887	$ 4,963,084

The table below summarizes ceded activity to AG Re reflected in the consolidated statements of operations.

	Year Ended December 31,	
	2014	2013
	(in thousands)	
Statements of operations:		
Net earned premiums	$ (10,170)	$ (11,178)
Realized gains and other settlements on credit derivatives	(89)	(6,013)
Net unrealized gains (losses) on credit derivatives	(822)	(12,236)
Losses and loss adjustment expense incurred ceded	(1,083)	1,647

16. Commitments and Contingencies

Legal Proceedings

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, and annual basis and updates its accruals, disclosures and estimates of reasonably possible loss based on such reviews.

Litigation

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

17. Other Comprehensive Income

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

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2014

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in thousands)	
Balance, December 31, 2013	$ 2,922	$ —	$ 2,922
Other comprehensive income (loss) before reclassifications	(2,707)	(2,478)	(5,185)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(3,055)	3,814	759
Tax (provision) benefit	1,069	(1,335)	(266)
Total amount reclassified from AOCI, net of tax	(1,986)	2,479	493
Net current period other comprehensive income (loss)	(4,693)	1	(4,692)
Balance, December 31, 2014	$ (1,771)	$ 1	$ (1,770)

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2013

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in thousands)	
Balance, December 31, 2012	$ 5,853	$ 283	$ 6,136
Other comprehensive income (loss) before reclassifications	(2,590)	(2,264)	(4,854)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(525)	3,048	2,523
Tax (provision) benefit	184	(1,067)	(883)
Total amount reclassified from AOCI, net of tax	(341)	1,981	1,640
Net current period other comprehensive income (loss)	(2,931)	(283)	(3,214)
Balance, December 31, 2013	$ 2,922	$ —	$ 2,922

18. Subsequent Events

Subsequent events have been considered through June 26, 2015, the date on which these financial statements were issued.

APPENDIX 3

2015 FINANCIAL STATEMENTS OF ASSURED GUARANTY MUNICIPAL CORP.

Exhibit 99.1

Assured Guaranty Municipal Corp.

Consolidated Financial Statements

December 31, 2015 and 2014

ASSURED GUARANTY MUNICIPAL CORP.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Independent Auditor's Report

To the Board of Directors of Assured Guaranty Municipal Corp.:

We have audited the accompanying consolidated financial statements of Assured Guaranty Municipal Corp. and its subsidiaries (the “Company”), which comprise the consolidated balance sheets as of December 31, 2015 and December 31, 2014, and the related consolidated statements of operations, of comprehensive income, 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.

Auditor's 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 Municipal Corp. and its subsidiaries at December 31, 2015 and December 31, 2014, 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
March 30, 2016

Assured Guaranty Municipal Corp.

Consolidated Balance Sheets

(dollars in millions except per share and share amounts)

	As of December 31, 2015	As of December 31, 2014
Assets		
Investment portfolio:		
Fixed-maturity securities, available-for-sale, at fair value (amortized cost of $5,901 and $5,920)	$ 6,090	$ 6,212
Short-term investments, at fair value	257	377
Other invested assets (includes Surplus Note from affiliate of $300 and $300)	360	406
Total investment portfolio	6,707	6,995
Cash	22	23
Premiums receivable	425	450
Ceded unearned premium reserve	845	958
Reinsurance recoverable on unpaid losses	154	133
Salvage and subrogation recoverable	109	130
Credit derivative assets	63	79
Deferred tax asset, net	103	161
Financial guaranty variable interest entities’ assets, at fair value	735	823
Other assets	132	154
Total assets	**$ 9,295**	**$ 9,906**
Liabilities and shareholder's equity		
Unearned premium reserve	$ 2,933	$ 3,425
Loss and loss adjustment expense reserve	488	404
Reinsurance balances payable, net	118	158
Notes payable	13	19
Credit derivative liabilities	154	287
Current income tax payable	16	57
Financial guaranty variable interest entities’ liabilities with recourse, at fair value	713	830
Financial guaranty variable interest entities’ liabilities without recourse, at fair value	121	114
Other liabilities	295	322
Total liabilities	**4,851**	**5,616**
Commitments and contingencies (See Note 15)		
Preferred stock ($1,000 par value, 5,000.1 shares authorized; 0 shares issued and outstanding)	—	—
Common stock ($45,455 par value, 330 shares authorized; issued and outstanding)	15	15
Additional paid-in capital	975	1,000
Retained earnings	2,967	2,752
Accumulated other comprehensive income, net of tax of $66 and $107	110	184
Total shareholder's equity attributable to Assured Guaranty Municipal Corp.	**4,067**	**3,951**
Noncontrolling interest	377	339
Total shareholder's equity	**4,444**	**4,290**
Total liabilities and shareholder's equity	**$ 9,295**	**$ 9,906**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Operations

(in millions)

	Year Ended December 31,	
	2015	2014
Revenues		
Net earned premiums	$ 404	$ 374
Net investment income	282	267
Net realized investment gains (losses):		
Other-than-temporary impairment losses	(32)	(69)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	(1)	1
Net impairment loss	(31)	(70)
Other net realized investment gains (losses)	4	11
Net realized investment gains (losses)	(27)	(59)
Net change in fair value of credit derivatives:		
Realized gains (losses) and other settlements	17	22
Net unrealized gains (losses)	117	19
Net change in fair value of credit derivatives	134	41
Fair value gains (losses) on committed capital securities	12	(4)
Fair value gains (losses) on financial guaranty variable interest entities	32	234
Other income (loss)	19	4
Total revenues	856	857
Expenses		
Loss and loss adjustment expenses	110	(25)
Amortization of deferred ceding commissions	(14)	(4)
Interest expense	(2)	2
Other operating expenses	107	111
Total expenses	201	84
Income (loss) before income taxes	655	773
Provision (benefit) for income taxes:		
Current	88	102
Deferred	98	127
Total provision (benefit) for income taxes	186	229
Net income (loss)	**469**	**544**
Less: Noncontrolling interest	39	32
Net income (loss) attributable to Assured Guaranty Municipal Corp.	**$ 430**	**$ 512**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Comprehensive Income

(in millions)

	Year Ended December 31,	
	2015	2014
Net income (loss)	**$ 469**	**$ 544**
Unrealized holding gains (losses) arising during the period on:		
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $(27) and $56	(49)	103
Investments with other-than-temporary impairment, net of tax provision (benefit) of $(20) and $(15)	(37)	(28)
Unrealized holding gains (losses) arising during the period, net of tax	(86)	75
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $(6) and $(21)	(11)	(40)
Other comprehensive income (loss)	(75)	115
Comprehensive income (loss)	**394**	**659**
Less: Comprehensive income (loss) attributable to noncontrolling interest	38	49
Comprehensive income (loss) attributable to Assured Guaranty Municipal Corp.	**$ 356**	**$ 610**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Shareholder’s Equity

(dollars in millions, except share data)

	Common Shares Outstanding	Common Stock Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholder's Equity Attributable to Assured Guaranty Municipal Corp.	Noncontrolling Interest	Total Shareholder's Equity
Balance at December 31, 2013	**330**	**15**	**1,051**	**2,400**	**86**	**$ 3,552**	**$ 289**	**$ 3,841**
Net income	—	—	—	512	—	512	32	544
Dividends	—	—	—	(160)	—	(160)	—	(160)
Other comprehensive income (loss)	—	—	—	—	98	98	17	115
Return of capital:								
Repayment of Surplus Note	—	—	(50)	—	—	(50)	—	(50)
Other	—	—	(1)	—	—	(1)	1	—
Balance at December 31, 2014	**330**	**15**	**1,000**	**2,752**	**184**	**3,951**	**339**	**4,290**
Net income	—	—	—	430	—	430	39	469
Dividends	—	—	—	(215)	—	(215)	—	(215)
Other comprehensive income (loss)	—	—	—	—	(74)	(74)	(1)	(75)
Return of capital:								
Repayment of Surplus Note	—	—	(25)	—	—	(25)	—	(25)
Balance at December 31, 2015	**330**	**$ 15**	**$ 975**	**$ 2,967**	**$ 110**	**$ 4,067**	**$ 377**	**$ 4,444**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Cash Flows

(in millions)

	Year Ended December 31,	
	2015	2014
Operating Activities:		
Net Income	$ 469	$ 544
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Net amortization of premium (discount) on investments	(32)	(15)
Provision (benefit) for deferred income taxes	98	127
Net realized investment losses (gains)	18	59
Net unrealized losses (gains) on credit derivatives	(117)	(19)
Fair value losses (gains) on committed capital securities	(12)	4
Change in deferred ceding commissions, net	(3)	(8)
Change in premiums receivable, net of premiums payable	(3)	75
Change in unearned premium reserve net of ceded unearned premium reserve	(379)	(138)
Change in loss and loss adjustment expense reserve and salvage and subrogation, net	20	66
Change in current income tax	(41)	(76)
Change in financial guaranty variable interest entities' assets and liabilities, net	(4)	(145)
(Purchases) sales of trading securities, net	8	37
Other	19	(49)
Net cash flows provided by (used in) operating activities	**41**	**462**
Investing activities		
Fixed-maturity securities:		
Purchases	(1,193)	(1,387)
Sales	566	362
Maturities	515	459
Net sales (purchases) of short-term investments	195	312
Net proceeds from paydowns on financial guaranty variable interest entities' assets	253	360
Other	33	(1)
Net cash flows provided by (used in) investing activities	**369**	**105**
Financing activities		
Dividends paid	(215)	(160)
Repayment of notes payable	(4)	(19)
Net paydowns of financial guaranty variable interest entities' liabilities	(166)	(365)
Repayment of Surplus Note	(25)	(50)
Net cash flows provided by (used in) financing activities	**(410)**	**(594)**
Effect of foreign exchange rate changes	(1)	(3)
Increase (decrease) in cash	**(1)**	**(30)**
Cash at beginning of period	23	53
Cash at end of period	**$ 22**	**$ 23**
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$ 120	$ 155
Interest	$ 0	$ 3

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

1. Business and Basis of Presentation

Business

Assured Guaranty Municipal Corp. (“AGM,” or together with its direct and indirect subsidiaries, the “Company”), a New York domiciled insurance company, is a wholly owned subsidiary of Assured Guaranty Municipal Holdings Inc. (“AGMH”). AGMH is an indirect and wholly owned subsidiary of Assured Guaranty Ltd. (“AGL” and, together with its subsidiaries, “Assured Guaranty”). AGL is a Bermuda-based holding company that provides, through its operating subsidiaries, credit protection products to the United States (“U.S.”) and international public finance (including infrastructure) and structured finance markets. AGM was formerly known as Financial Security Assurance Inc.

The Company applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guaranty insurance that protects holders of debt instruments and other monetary obligations from defaults in scheduled payments. If an obligor defaults on a scheduled payment due on an obligation, including a scheduled principal or interest payment (“Debt Service”), the Company is required under its unconditional and irrevocable financial guaranty to pay the amount of the shortfall to the holder of the obligation. Obligations insured by the Company include bonds issued by U.S. state or municipal governmental authorities and notes issued to finance international infrastructure projects. AGM had previously offered insurance and reinsurance in the global structured finance market, but has not done so since mid-2008. AGM and its indirect subsidiary Municipal Assurance Corp. ("MAC") markets its financial guaranty insurance directly to issuers and underwriters of public finance securities as well as to investors in such obligations. The Company guarantees obligations issued principally in the U.S. and the United Kingdom ("U.K."), and also guarantees obligations issued in other countries and regions, including Australia and Western Europe.

In the past, the Company sold credit protection by issuing policies that guaranteed payment obligations under credit derivatives, primarily credit default swaps (“CDS”). Financial guaranty contracts accounted for as credit derivatives are generally structured such that the circumstances giving rise to the Company’s obligation to make loss payments are similar to those for financial guaranty insurance contracts. The Company’s credit derivative transactions are governed by International Swaps and Derivative Association, Inc. (“ISDA”) documentation. The Company has not entered into any new CDS in order to sell credit protection since 2008. Regulatory guidelines were issued in 2009 that limited the terms under which such protection could be sold. The capital and margin requirements applicable under the Dodd-Frank Wall Street Reform and Consumer Protection Act also contributed to the Company not entering into new CDS. The Company actively pursues opportunities to terminate existing CDS, which have the effect of reducing future fair value volatility in income and/or reducing rating agency capital charges.

Basis of Presentation

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) and, in the opinion of management, reflect all adjustments that are of a normal recurring nature, necessary for a fair statement of the financial condition, results of operations and cash flows of the Company and its consolidated financial guaranty variable interest entities (“FG VIEs”) for the periods presented. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The consolidated financial statements include the accounts of AGM, its direct and indirect subsidiaries (collectively, the “Subsidiaries”), and its consolidated FG VIEs. Intercompany accounts and transactions between and among all consolidated entities have been eliminated. Certain prior year balances have been reclassified to conform to the current year's presentation.

AGM's direct and indirect subsidiaries are as follows:

- Assured Guaranty (Europe) Ltd. (“AGE”), organized in the U.K. and 100% owned by AGM;
- Municipal Assurance Holdings Inc. (“MAC Holdings”), incorporated in Delaware and 60.7% owned by AGM and 39.3% owned by AGM's affiliate, Assured Guaranty Corp. ("AGC"); and
- MAC, domiciled in New York and 100% owned by MAC Holdings.

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 AGM's foreign currency transactions are reported in the consolidated statement of operations.

The chief operating decision maker manages the operations of the Company at a consolidated level. Therefore, all results of operations are reported as one segment.

Other significant accounting policies are included in the following notes.

Significant Accounting Policies

Expected loss to be paid (insurance, credit derivatives and FG VIE contracts)	Note 4
Financial guaranty insurance (premium revenue recognition, loss and loss adjustment expense and policy acquisition cost)	Note 5
Fair value measurement	Note 6
Credit derivatives (at fair value)	Note 7
Variable interest entities (at fair value)	Note 8
Investments and cash	Note 9
Income taxes	Note 12

Future Application of Accounting Standards

Leases

In February 2016, the Financial Accounting Standards Board ("FASB") issued ASU 2016-02, *Leases (Topic 842)*. This ASU requires lessees to present right-of-use assets and lease liabilities on the balance sheet. ASU 2016-02 is to be applied using a modified retrospective approach at the beginning of the earliest comparative period in the financial statements. The ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The Company is evaluating the impact that this ASU will have on its Consolidated Financial Statements.

Financial Instruments

In January 2016, the FASB issued Accounting Standards Update ("ASU") 2016-01, *Financial Instruments - Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities*. The amendments in this ASU are intended to make targeted improvements to GAAP by addressing certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. One of the amendments pertains to liabilities that an entity has elected to measure at fair value in accordance with the fair value option for financial instruments. For these liabilities, the portion of fair value change related to credit risk will be separately presented in other comprehensive income. Currently, the entire change in the fair value of these liabilities is reflected in the income statement.

The ASU is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Entities will be required to record a cumulative-effect adjustment to the statement of financial position as of the beginning of the fiscal year in which the guidance is adopted. For the Company, this would be as of January 1, 2018. Early adoption is permitted only for the amendment related to the change in presentation of financial liabilities that are fair valued using the fair value option. The Company is currently evaluating the effect of adopting this ASU on its Consolidated Financial Statements.

Short Duration Insurance Contracts

In May 2015, the FASB issued ASU 2015-09, *Financial Services - Insurance (Topic 944) - Disclosures about Short-Duration Contracts.* The primary objective of this ASU is to improve disclosures for insurance entities which issue short-duration contracts. The ASU 2015-09 will have no impact on the Company's financial statement disclosures. The ASU is effective for annual periods beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016.

Consolidation

In February 2015, the FASB issued ASU No. 2015-02, Consolidation *(Topic 810): Amendments to the Consolidation Analysis*, which is intended to improve certain areas of consolidation guidance for legal entities such as limited partnerships, limited liability companies, and securitization structures. The ASU will be effective on January 1, 2016. Early adoption is permitted, including adoption in an interim period. The Company does not expect that ASU 2015-02 will have an effect on its Consolidated Financial Statements.

2. Rating Actions

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

The Company periodically assesses the value of each rating assigned to each of its companies, and may as a result of such assessment request that a rating agency add or drop a rating from certain of its companies. For example, the Kroll Bond Rating Agency ("KBRA") ratings were first assigned to MAC in 2013 and to AGM in 2014, while a Moody's Investors Service, Inc. ("Moody's") rating was never requested for MAC.

In the last several years, Standard & Poor's Ratings Services ("S&P") and Moody's have changed, multiple times, their financial strength ratings of AGM and AGE, or changed the outlook on such ratings. More recently, KBRA has assigned financial strength ratings to MAC and AGM. The rating agencies' most recent actions related to AGM and its subsidiaries are:

- On March 18, 2014, S&P upgraded the financial strength ratings of AGM, AGE and MAC to AA (stable outlook) from AA- (stable outlook); it most recently affirmed such ratings in a credit analysis issued on June 29, 2015.

- On July 2, 2014, Moody's affirmed AGM's and AGE's A2 (stable outlook) financial strength ratings. Moody's adopted changes to its credit methodology for financial guaranty insurance companies on January 20, 2015 and, on February 18, 2015, Moody's published a credit opinion maintaining its existing ratings of AGM and AGE under that new methodology. On December 8, 2015 Moody's published credit opinions maintaining its existing insurance financial strength ratings of A2 (stable outlook) on AGM.

- On June 22, 2013, KBRA assigned a financial strength rating of AA+ (stable outlook) to MAC, and affirmed that rating on August 3, 2015. On November 13, 2014, KBRA assigned a financial strength rating of AA+ (stable outlook) to AGM, and affirmed that rating on December 10, 2015.

There can be no assurance that any of the rating agencies will not take negative action on the financial strength ratings of AGM or its insurance subsidiaries in the future.

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

- Note 5, Financial Guaranty Insurance
- Note 13, Reinsurance and Other Monoline Exposures
- Note 16, Notes Payable and Credit Facilities (regarding the impact on AGM's insured leveraged lease transactions)

3. Outstanding Exposure

The Company's financial guaranty contracts are written in either insurance or credit derivative form, but collectively are considered financial guaranty contracts. The Company seeks to limit its exposure to losses by underwriting obligations that it views as investment grade at inception, although, as part of its loss mitigation strategy for existing troubled credits, it may underwrite new issuances that it views as below-investment-grade ("BIG"). The Company diversifies its insured portfolio across asset classes and, in the structured finance portfolio, requires rigorous subordination or collateralization requirements. Reinsurance may be used in order to reduce net exposure to certain insured transactions.

The Company has issued financial guaranty insurance policies on public finance obligations and, prior to mid-2008, structured finance obligations. Public finance obligations insured by the Company consist primarily of general obligation bonds supported by the taxing powers of U.S. state or municipal governmental authorities, as well as tax-supported bonds, revenue bonds and other obligations supported by covenants from state or municipal governmental authorities or other municipal obligors to impose and collect fees and charges for public services or specific infrastructure projects. The Company also includes within public finance obligations those obligations backed by the cash flow from leases or other revenues from projects serving substantial public purposes, including utilities, toll roads, health care facilities and government office buildings. The Company also includes within public finance similar obligations issued by territorial and non-U.S. sovereign and sub-sovereign issuers and governmental authorities.

Structured finance obligations insured by the Company are generally issued by special purpose entities, including VIEs, and backed by pools of assets having an ascertainable cash flow or market value or other specialized financial obligations. Some of these VIEs are consolidated as described in Note 8, Consolidated Variable Interest Entities. Unless otherwise specified, the outstanding par and Debt Service amounts presented in this note include outstanding exposures on VIEs whether or not they are consolidated. While AGM has ceased insuring new originations of asset-backed securities, a significant portfolio of such obligations remains outstanding. AGM's wholly owned subsidiary AGE provides financial guarantees in the international public finance market and intends to provide such guarantees in the international structured finance market, subject to regulatory approval.

Debt Service and par outstanding exposures presented in these financial statements are presented on a consolidated basis. That is, amounts presented include 100% of the exposures of AGM, AGE and MAC, despite the fact that AGM indirectly owns only 60.7% of MAC.

Significant Risk Management Activities

The Portfolio Risk Management Committee, which includes members of senior management and senior credit and surveillance officers, sets specific risk policies and limits and is responsible for enterprise risk management, establishing the Company's risk appetite, credit underwriting of new business, surveillance and work-out.

As part of the surveillance process, the Company monitors trends and changes in transaction credit quality, detects any deterioration in credit quality, and recommends such remedial actions as may be necessary or appropriate. All transactions in the insured portfolio are assigned internal credit ratings, which are updated based on changes in transaction credit quality. The Company also develops strategies to enforce its contractual rights and remedies and to mitigate its losses, engage in negotiation discussions with transaction participants and, when necessary, manage the Company's litigation proceedings.

Surveillance Categories

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

The Company monitors its investment grade credits to determine whether any need to be internally downgraded to BIG and refreshes its internal credit ratings on individual credits in quarterly, semi-annual or annual cycles based on the Company's view of the credit's quality, loss potential, volatility and sector. Ratings on credits in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter.

Credits identified as BIG are subjected to further review to determine the probability of a loss. See Note 4, Expected Loss to be Paid for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. For surveillance purposes, the Company calculates present value using a constant discount rate of 5%. (A risk-free rate is used for calculating the expected loss for financial statement measurement purposes.)

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

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

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

- BIG Category 3: Below-investment-grade transactions for which future losses are expected and on which claims (other than liquidity claims) have been paid.

Components of Outstanding Exposure

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

The Company purchases securities that it has insured, and for which it has expected losses to be paid, in order to mitigate the economic effect of insured losses ("loss mitigation securities"). The Company excludes amounts attributable to loss mitigation securities (unless otherwise indicated) from par and Debt Service outstanding, because it manages such securities as investments and not insurance exposure. The following table presents the gross and net debt service for all financial guaranty contracts.

Financial Guaranty
Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding(1)	
	December 31, 2015	December 31, 2014	December 31, 2015	December 31, 2014
	(in millions)			
Public finance	$ 415,968	$ 473,492	$ 302,557	$ 348,905
Structured finance	22,880	33,196	20,479	29,756
Total financial guaranty	$ 438,848	$ 506,688	$ 323,036	$ 378,661

(1) Includes $104.5 billion and $132.0 billion of net debt service outstanding, as of December 31, 2015 and 2014, respectively, from MAC, which represents 100% of MAC's net debt service outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2015

	Public Finance U.S.		Public Finance Non-U.S.		Structured Finance U.S.		Structured Finance Non-U.S.		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
	(dollars in millions)									
AAA	$ 2,431	1.3%	$ 553	3.0%	$ 8,529	57.6%	$ 1,786	66.1%	$ 13,299	6.1%
AA	47,028	25.9	134	0.7	3,421	23.1	35	1.3	50,618	23.3
A	98,954	54.6	5,126	27.7	41	0.3	153	5.7	104,274	48.0
BBB	30,443	16.8	11,832	64.1	123	0.9	329	12.1	42,727	19.6
BIG	2,522	1.4	837	4.5	2,681	18.1	401	14.8	6,441	3.0
Total net par outstanding (1) (2)	$ 181,378	100.0%	$ 18,482	100.0%	$ 14,795	100.0%	$ 2,704	100.0%	$ 217,359	100.0%

(1) Excludes $659 million of loss mitigation securities insured and held by the Company as of December 31, 2015, which are primarily BIG.

(2) Includes $73.5 billion of net par outstanding as of December 31, 2015, from MAC, which represents 100% of MAC's net par outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2014

	Public Finance U.S.		Public Finance Non-U.S.		Structured Finance U.S.		Structured Finance Non-U.S.		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
	(dollars in millions)									
AAA	$ 3,254	1.6%	$ 541	2.7%	$ 13,185	61.3%	$ 3,311	73.1%	$ 20,291	8.0%
AA	62,175	30.1	348	1.7	4,883	22.7	312	6.9	67,718	26.8
A	112,119	54.3	5,488	27.1	45	0.2	175	3.9	117,827	46.6
BBB	25,604	12.4	12,891	63.5	266	1.2	226	5.0	38,987	15.5
BIG	3,274	1.6	1,024	5.0	3,130	14.6	501	11.1	7,929	3.1
Total net par outstanding (1) (2)	$ 206,426	100.0%	$ 20,292	100.0%	$ 21,509	100.0%	$ 4,525	100.0%	$ 252,752	100.0%

(1) Excludes $675 million of loss mitigation securities insured and held by the Company as of December 31, 2014, which are primarily BIG.
(2) Includes $90.6 billion of net par outstanding as of December 31, 2014, from MAC, which represents 100% of MAC's net par outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

Financial Guaranty Portfolio
by Sector

Sector	Gross Par Outstanding		Ceded Par Outstanding		Net Par Outstanding	
	As of December 31, 2015	As of December 31, 2014	As of December 31, 2015	As of December 31, 2014	As of December 31, 2015	As of December 31, 2014
			(in millions)			
Public finance:						
U.S.:						
General obligation	$ 111,296	$ 124,967	$ 28,164	$ 29,979	$ 83,132	$ 94,988
Tax backed	47,218	51,522	12,458	12,510	34,760	39,012
Municipal utilities	39,896	45,468	8,631	9,045	31,265	36,423
Transportation	17,772	20,632	4,067	4,528	13,705	16,104
Healthcare	10,564	11,184	3,640	3,828	6,924	7,356
Higher education	8,367	9,693	1,966	2,449	6,401	7,244
Infrastructure finance	2,795	2,606	806	1,284	1,989	1,322
Housing	1,794	2,677	284	509	1,510	2,168
Other public finance	1,886	1,998	194	189	1,692	1,809
Total public finance-U.S.	241,588	270,747	60,210	64,321	181,378	206,426
Non-U.S.:						
Infrastructure finance	13,164	14,242	4,376	4,794	8,788	9,448
Regulated utilities	11,229	12,996	5,778	6,705	5,451	6,291
Other public finance	5,693	6,115	1,450	1,562	4,243	4,553
Total public finance-non-U.S.	30,086	33,353	11,604	13,061	18,482	20,292
Total public finance	$ 271,674	$ 304,100	$ 71,814	$ 77,382	$ 199,860	$ 226,718
Structured finance:						
U.S.:						
Pooled corporate obligations	9,185	$ 14,517	$ 704	$ 943	8,481	$ 13,574
Residential Mortgage-Backed Securities ("RMBS")	4,668	5,777	566	810	4,102	4,967
Financial products	1,906	2,276	—	—	1,906	2,276
Insurance securitizations	—	383	—	55	—	328
Consumer receivables	143	170	8	10	135	160
Commercial receivables	33	40	2	2	31	38
Other structured finance	246	290	106	124	140	166
Total structured finance-U.S.	16,181	23,453	1,386	1,944	14,795	21,509
Non-U.S.:						
Pooled corporate obligations	2,545	4,310	579	881	1,966	3,429
RMBS	529	837	78	113	451	724
Other structured finance	310	400	23	28	287	372
Total structured finance- non-U.S.	3,384	5,547	680	1,022	2,704	4,525
Total structured finance	$ 19,565	$ 29,000	$ 2,066	$ 2,966	$ 17,499	$ 26,034
Total net par outstanding	$ 291,239	$ 333,100	$ 73,880	$ 80,348	$ 217,359	$ 252,752

In addition to amounts shown in the tables above, AGM had outstanding commitments to provide guaranties of $471 million for public finance obligations as of December 31, 2015, all of which expired prior to the date of this filing. AGM also had outstanding commitments of $124 million as of December 31, 2015 which can be used together with AGC, an affiliate of the Company. The expiration dates for these commitments range between June 30, 2016 and February 25, 2017. The commitments are contingent on the satisfaction of all conditions set forth in them and may expire unused or be canceled at the counterparty's request. Therefore, the total commitment amount does not necessarily reflect actual future guaranteed amounts.

Actual maturities of insured obligations could differ from contractual maturities because borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties. The expected maturities of structured finance obligations are, in general, considerably shorter than the contractual maturities for such obligations.

Expected Amortization of
Net Par Outstanding
As of December 31, 2015

	Public Finance	Structured Finance	Total
		(in millions)	
0 to 5 years	$ 65,045	$ 13,267	$ 78,312
5 to 10 years	43,083	1,383	44,466
10 to 15 years	36,669	1,237	37,906
15 to 20 years	26,649	955	27,604
20 years and above	28,414	657	29,071
Total net par outstanding	$ 199,860	$ 17,499	$ 217,359

Components of BIG Portfolio

Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of December 31, 2015

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
U.S. public finance	$ 1,559	$ 902	$ 61	$ 2,522	$ 181,378
Non-U.S. public finance	622	215	—	837	18,482
Structured finance:					
First lien U.S. RMBS:					
Prime first lien	—	17	—	17	49
Alt-A first lien	26	30	438	494	644
Option ARM	2	—	45	47	101
Subprime	45	143	807	995	2,200
Second lien U.S. RMBS	341	18	626	985	1,108
Total U.S. RMBS	414	208	1,916	2,538	4,102
Other structured finance	451	54	39	544	13,397
Total	$ 3,046	$ 1,379	$ 2,016	$ 6,441	$ 217,359

Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of December 31, 2014

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
U.S. public finance	$ 2,748	$ 464	$ 62	$ 3,274	$ 206,426
Non-U.S. public finance	1,024	—	—	1,024	20,292
Structured finance:					
First lien U.S. RMBS:					
Prime first lien	—	—	—	—	57
Alt-A first lien	27	98	523	648	819
Option ARM	4	—	56	60	175
Subprime	46	483	573	1,102	2,487
Second lien U.S. RMBS	636	19	495	1,150	1,429
Total U.S. RMBS	713	600	1,647	2,960	4,967
Other structured finance	565	62	44	671	21,067
Total	$ 5,050	$ 1,126	$ 1,753	$ 7,929	$ 252,752

BIG Net Par Outstanding
and Number of Risks
As of December 31, 2015

	Net Par Outstanding			Number of Risks(2)		
Description	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
			(dollars in millions)			
BIG:						
Category 1	$ 2,955	$ 91	$ 3,046	59	2	61
Category 2	1,379	—	1,379	14	—	14
Category 3	2,000	16	2,016	43	2	45
Total BIG	$ 6,334	$ 107	$ 6,441	116	4	120

BIG Net Par Outstanding
and Number of Risks
As of December 31, 2014

Description	Net Par Outstanding: Financial Guaranty Insurance(1)	Net Par Outstanding: Credit Derivative	Net Par Outstanding: Total	Number of Risks(2): Financial Guaranty Insurance(1)	Number of Risks(2): Credit Derivative	Number of Risks(2): Total
	(dollars in millions)					
BIG:						
Category 1	$ 4,940	$ 110	$ 5,050	71	2	73
Category 2	1,126	—	1,126	14	—	14
Category 3	1,734	19	1,753	38	2	40
Total BIG	$ 7,800	$ 129	$ 7,929	123	4	127

____

(1) Includes net par outstanding for FG VIEs.

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

Geographic Distribution of Net Par Outstanding

The Company seeks to maintain a diversified portfolio of insured obligations designed to spread its risk across a number of geographic areas.

Geographic Distribution of
Net Par Outstanding
As of December 31, 2015

	Number of Risks	Net Par Outstanding	Percent of Total Net Par Outstanding
		(dollars in millions)	
U.S.:			
U.S. Public finance:			
California	1,286	$ 30,555	14.1%
Pennsylvania	882	15,027	6.9
Illinois	726	14,843	6.8
Texas	1,186	14,546	6.7
New York	897	13,597	6.3
Florida	272	9,818	4.5
New Jersey	512	8,122	3.7
Michigan	531	7,437	3.4
Georgia	154	4,674	2.2
Ohio	423	4,348	2.0
Other states and U.S. territories	3,404	58,411	26.9
Total U.S. public finance	10,273	181,378	83.5
U.S. Structured finance (multiple states)	224	14,795	6.8
Total U.S.	10,497	196,173	90.3
Non-U.S.:			
United Kingdom	72	9,880	4.5
Canada	9	2,834	1.3
Australia	13	2,014	0.9
France	11	1,401	0.6
Italy	8	986	0.5
Other	41	4,071	1.9
Total non-U.S.	154	21,186	9.7
Total	10,651	$ 217,359	100.0%

Exposure to Puerto Rico

The Company has insured exposure to general obligation bonds of the Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations, aggregating $2.14 billion net par as of December 31, 2015, $2.06 billion of which is rated BIG. In 2015, the Company's Puerto Rico exposures increased due to a commutation of previously ceded Puerto Rico exposures.

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

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

On June 28, 2015, Governor García Padilla of Puerto Rico (the "Governor") publicly stated that the Commonwealth’s public debt, considering the current level of economic activity, is unpayable and that a comprehensive debt restructuring may be necessary, and he has made similar statements since then. On June 29, 2015 a report commissioned by the Commonwealth and authored by former World Bank Chief Economist and former Deputy Director of the International Monetary Fund Dr. Anne Krueger and economists Dr. Ranjit Teja and Dr. Andrew Wolfe and calling for debt restructuring of all Puerto Rico bonds was released ("Krueger Report").

Puerto Rico Public Finance Corporation (“PFC”), a subsidiary of the GDB, failed to make most of an approximately $58 million Debt Service payment on August 3, 2015 and to make subsequent Debt Service payments because the Commonwealth’s legislature did not appropriate funds for payment. The Company does not insure any obligations of the PFC. On January 1, 2016 Puerto Rico Infrastructure Finance Authority ("PRIFA") defaulted on payment of a portion of the interest due on its bonds on that date. The Company does not insure any obligations of PRIFA, although the Company's affiliate AGC does, and paid approximately $451 thousand of claims for the interest payments on which PRIFA had defaulted.

On September 9, 2015, the Working Group for the Fiscal and Economic Recovery of Puerto Rico (“Working Group”) established by the Governor published its “Puerto Rico Fiscal and Economic Growth Plan” (the “FEGP”). The FEGP projected that the Commonwealth would face a cumulative financing gap of $27.8 billion from fiscal year 2016 to fiscal year 2020 without corrective action. Various stakeholders and analysts have publicly questioned the accuracy of the $27.8 billion gap projected by the Working Group. The FEGP recommended economic development, structural, fiscal and institutional reform measures that it projects would reduce that gap to $14.0 billion. The Working Group asserts that the Commonwealth’s debt, including debt with a constitutional priority, is not sustainable. The FEGP included a recommendation that the Commonwealth’s advisors begin to work on a voluntary exchange offer to its creditors as part of the FEGP. The FEGP does not have the force of law and implementation of its recommendations would require actions by the governments of the Commonwealth and of the United States as well as the cooperation and agreement of various creditors.

On November 30, 2015, and December 8, 2015, the Governor issued executive orders (“Clawback Orders”) directing the Puerto Rico Department of Treasury and the Puerto Rico Tourism Company to retain or transfer certain taxes and revenues pledged to secure the payment of bonds issued by PRHTA, PRIFA and Puerto Rico Convention Center District Authority ("PRCCDA"). On January 7, 2016 the Company sued various Puerto Rico governmental officials in the United States District Court, District of Puerto Rico asserting that this attempt to “claw back” pledged taxes and revenues is unconstitutional, and demanding declaratory and injunctive relief. The Puerto Rico credits insured by the Company impacted by the Clawback Orders are shown in the table “Puerto Rico Net Par Outstanding” below.

On January 18, 2016 the Working Group published an updated FEGP that projected the cumulative financing gap beyond 2020 would continue to increase to $63.4 billion without corrective action. The Working Group followed that up with the publication on February 1, 2016, of a proposal for a voluntary exchange of $49.2 billion of tax supported debt into $26.5 billion of new mandatorily payable base bonds and $22.7 billion of growth bonds.

There have been a number of other proposals, plans and legislative initiatives offered in Puerto Rico and in the United States aimed at addressing Puerto Rico’s fiscal issues. Among the responses proposed is a federal financial control board and access to bankruptcy courts or another restructuring mechanism. U.S. House of Representatives Speaker Paul Ryan has asked that a legislative response be presented to the House of Representatives by the end of March 2016. The final shape and timing of responses to Puerto Rico’s distress eventually enacted or implemented by Puerto Rico or the United States, if any, and the impact of any such actions on obligations insured by the Company, is uncertain and may differ substantially from the recommendations of the Working Group or any other proposals or plans described in the press or offered to date or in the future.

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

PREPA

As of December 31, 2015, the Company had $431 million insured net par outstanding of PREPA obligations. In August 2014, PREPA entered into forbearance agreements with the GDB, its bank lenders, and bondholders and financial guaranty insurers (including AGM and AGC) that hold or guarantee more than 60% of PREPA's outstanding bonds, in order to address its near-term liquidity issues. Creditors, including AGM and AGC, agreed not to exercise available rights and remedies until March 31, 2015, and the bank lenders agreed to extend the maturity of two revolving lines of credit to the same date. PREPA agreed it would continue to make principal and interest payments on its outstanding bonds, and interest payments on its lines of credit. It also agreed it would develop a five year business plan and a recovery program in respect of its operations. Subsequently, most of the parties extended these forbearance agreements several times.

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

On December 24, 2015, AGM and AGC entered into a Restructuring Support Agreement ("RSA") with PREPA, an ad hoc group of uninsured bondholders and a group of fuel-line lenders that would, subject to certain conditions, result in, among other things, modernization of the utility and a restructuring of current debt. Upon finalization of the contemplated restructuring transaction, insured PREPA revenue bonds (with no reduction to par or stated interest rate or extension of maturity) will be supported by securitization bonds issued by a special purpose corporation and secured by a transition charge assessed on ratepayers. To facilitate the securitization transaction, which enables PREPA to achieve debt relief and more efficient capital markets financing, AGM and AGC will issue surety insurance policies in an aggregate amount not expected to exceed $113 million ($99 million for AGM and $14 million for AGC) in exchange for a market premium and to support a portion of the reserve fund for the securitization bonds. Certain of the creditors also agreed, subject to certain conditions, to participate in a bridge financing. The AGM's and AGC's shares of the bridge financing is approximately $15 million ($13 million for AGM and $2 million for AGC). Legislation purportedly meeting the requirements of the RSA was enacted on February 16, 2016. The closing of the restructuring transaction, the issuance of the surety bonds and the closing of the bridge financing are subject to certain conditions, including confirmation that the enacted legislation meets all requirements of the RSA and execution of acceptable documentation and legal opinions.

There can be no assurance that the conditions in the RSA will be met or that, if the conditions are met, the RSA's other provisions, including those related to the restructuring of the insured PREPA revenue bonds, will be implemented. PREPA, during the pendency of the agreements, has suspended deposits into its debt service fund.

PRHTA

As of December 31, 2015, the Company had $289 million insured net par outstanding of PRHTA (Transportation revenue) bonds and $219 million net par of PRHTA (Highway revenue) bonds. In March 2015, legislation was passed in the Commonwealth that would have supported proposals involving the GDB and PRIFA and would have, among other things, strengthened PRHTA. The proposals involved the issuance of up to $2.95 billion of bonds by PRIFA, but the Company believes the Commonwealth is no longer pursuing those proposals. In addition, PRHTA is one of the public corporations affected by the Clawback Orders.

Municipal Finance Agency

As of December 31, 2015, the Company had $206 million net par outstanding of bonds issued by the Puerto Rico Municipal Finance Agency ("MFA") secured by a pledge of local property tax revenues. On October 13, 2015, the Company and AGC filed a motion to intervene in litigation between Centro de Recaudación de Ingresos Municipales ("CRIM") and the GDB in which CRIM was seeking to ensure that the pledged tax revenues are, and will continue to be, available to support the MFA bonds. While the Company's motion to intervene was denied, the GDB and CRIM have reported that they executed a new deed of trust that requires the GDB, as fiduciary, to keep the pledged tax revenues separate from any other GDB monies or accounts and that governs the manner in which the pledged revenues may be invested and dispersed.

The following tables show the Company's insured exposure to general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations.

Puerto Rico
Gross Par and Gross Debt Service Outstanding

	Gross Par Outstanding		Gross Debt Service Outstanding	
	December 31, 2015	December 31, 2014	December 31, 2015	December 31, 2014
	(in millions)			
Previously Subject to the Voided Recovery Act (1)	$ 1,708	$ 1,844	$ 2,639	$ 2,868
Not Previously Subject to the Voided Recovery Act	2,053	2,204	3,442	3,711
Total	$ 3,761	$ 4,048	$ 6,081	$ 6,579

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

Puerto Rico
Net Par Outstanding

	As of December 31, 2015			As of December 31, 2014		
	Total (2)		Internal Rating	Total		Internal Rating
			(in millions)			
Exposures Previously Subject to the Voided Recovery Act:						
PRHTA (Transportation revenue) ("Primary policies") (3)	$	209	CCC-	$	223	BB-
PRHTA (Transportation revenue) ("Second-to-pay policies") (1)(3)		80	AA		80	AA
Total		289			303	
PREPA		431	CC		464	B-
PRHTA (Highway revenue) (3)		219	CCC		197	BB
Total		939			964	
Exposures Not Previously Subject to the Voided Recovery Act:						
Commonwealth of Puerto Rico - General Obligation Bonds		720	CCC		749	BB
Puerto Rico Sales Tax Financing Corporation		261	CCC+		261	BBB
MFA		206	CCC-		223	BB-
Puerto Rico Public Buildings Authority		14	B		18	BB+
Total		1,201			1,251	
Total net exposure to Puerto Rico	$	2,140		$	2,215	

(1) Represents exposure as to which AGM guarantees payment of principal and interest when due in the event that both the obligor and the AGM affiliate that issued a primary insurance policy fail to pay.

(2) As of December 31, 2015, the Company's Puerto Rico net exposures include a commutation of previously ceded Puerto Rico exposures.

(3) The Governor issued executive orders on November 30, 2015, and December 8, 2015, directing the Puerto Rico Department of Treasury and the Puerto Rico Tourism Company to retain or transfer certain taxes and revenues pledged to secure the payment of bonds issued by PRHTA. On January 7, 2016 the Company sued various Puerto Rico governmental officials in the United States District Court, District of Puerto Rico asserting that this attempt to “claw back” pledged taxes and revenues is unconstitutional, and demanding declaratory and injunctive relief.

The following table shows the scheduled amortization of the insured general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations rated BIG by the Company. The Company guarantees payments of interest and principal when those amounts are scheduled to be paid and cannot be required to pay on an accelerated basis. In the event that obligors default on their obligations, the Company would only be required to pay the shortfall between the principal and interest due in any given period and the amount paid by the obligors.

Amortization Schedule of Puerto Rico BIG Net Par Outstanding and Net Debt Service Outstanding As of December 31, 2015

	Scheduled BIG Net Par Amortization			Scheduled BIG Net Debt Service Amortization		
	Previously Subject to the Voided Recovery Act	Not Previously Subject to the Voided Recovery Act	Total	Previously Subject to the Voided Recovery Act	Not Previously Subject to the Voided Recovery Act	Total
	(in millions)					
2016	$ 36	$ 74	$ 110	$ 78	$ 138	$ 216
2017	29	74	103	70	134	204
2018	23	41	64	61	96	157
2019	33	58	91	72	110	182
2020	47	51	98	83	101	184
2021	35	13	48	68	60	128
2022	31	25	56	62	72	134
2023	73	12	85	104	56	160
2024	58	45	103	85	90	175
2025	49	43	92	73	84	157
2026 - 2030	246	138	384	332	322	654
2031 - 2035	170	287	457	201	429	630
2036 - 2040	29	187	216	30	260	290
2041 - 2043	—	153	153	—	168	168
Total	$ 859	$ 1,201	$ 2,060	$ 1,319	$ 2,120	$ 3,439

Exposure to the Selected European Countries

Several European countries continue to experience significant economic, fiscal and/or political strains such that the likelihood of default on obligations with a nexus to those countries may be higher than the Company anticipated when such factors did not exist. The European countries where the Company has exposure and believes heightened uncertainties exist are: Hungary, Italy, Portugal and Spain (collectively, the “Selected European Countries”). The Company is closely monitoring its exposures in the Selected European Countries where it believes heightened uncertainties exist. The Company’s direct economic exposure to the Selected European Countries (based on par for financial guaranty contracts and notional amount for financial guaranty contracts accounted for as derivatives) is shown in the following table, net of ceded reinsurance.

Net Direct Economic Exposure to Selected European Countries(1)
As of December 31, 2015

	Hungary	Italy	Portugal	Spain	Total
			(in millions)		
Sub-sovereign exposure:					
Non-infrastructure public finance (2)	$ —	$ 632	$ 79	$ 166	$ 877
Infrastructure finance	210	5	—	111	326
Total sub-sovereign exposure	210	637	79	277	1,203
Non-sovereign exposure:					
Regulated utilities	—	122	—	—	122
RMBS	160	215	—	—	375
Total non-sovereign exposure	160	337	—	—	497
Total	$ 370	$ 974	$ 79	$ 277	$ 1,700
Total BIG (See Note 4)	$ 305	$ —	$ 79	$ 277	$ 661

____
(1) While the Company's exposures are shown in U.S. dollars, the obligations the Company insures are in various currencies, primarily Euros. One of the RMBS included in the table above includes residential mortgages in both Italy and Germany, and only the portion of the transaction equal to the portion of the original mortgage pool in Italian mortgages is shown in the table.

(2) The exposure shown in the “Non-infrastructure public finance” category is from transactions backed by receivable payments from sub-sovereigns in Italy, Spain and Portugal. Sub-sovereign debt is debt issued by a governmental entity or government backed entity, or supported by such an entity, that is other than direct sovereign debt of the ultimate governing body of the country.

When the Company directly insures an obligation, it assigns the obligation to a geographic location or locations based on its view of the geographic location of the risk.

The Company has excluded from the exposure tables above its indirect economic exposure to the Selected European Countries through policies it provides on pooled corporate transactions. The Company calculates indirect exposure to a country by multiplying the par amount of a transaction insured by the Company times the percent of the relevant collateral pool reported as having a nexus to the country. On that basis, the Company has calculated exposure of $46 million to Selected European Countries in transactions with $2.2 billion of net par outstanding.

4. Expected Loss to be Paid

The insured portfolio includes policies accounted for under three separate accounting models depending on the characteristics of the contract and the Company's control rights. The Company has paid and expects to pay future losses on policies which fall under each of the three accounting models. The following provides a summarized description of the three accounting models prescribed by GAAP with a reference to the notes that describe the accounting policies and required disclosures throughout this report. The three models are: (1) insurance, (2) derivative and (3) VIE consolidation.

In order to effectively evaluate and manage the economics and liquidity of the entire insured portfolio, management compiles and analyzes loss information for all policies on a consistent basis. The Company monitors and assigns ratings and calculates expected losses in the same manner for all its exposures regardless of form or differing accounting models.

This note provides information regarding expected claim payments to be made under all contracts in the insured portfolio. Net expected loss to be paid in the tables below consists of the present value of future: expected claim and loss adjustment expenses ("LAE") payments, expected recoveries in the transaction structures, cessions to reinsurers, and expected recoveries for breaches of representations and warranties ("R&W") and other loss mitigation strategies. 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, regardless of the accounting model. Expected loss to be paid is an important measure used by management to analyze the net economic loss on all contracts.

Accounting Policy

Insurance Accounting

For contracts accounted for as financial guaranty insurance, loss and LAE reserve is recorded only to the extent and for the amount that expected losses to be paid, exceed unearned premium reserve. As a result, the Company has expected loss to be paid that have not yet been expensed. Such amounts will be recognized in future periods as deferred premium revenue amortizes into income. Expected loss to be expensed is important because it presents the Company's projection of incurred losses that will be recognized in future periods (excluding accretion of discount). See "Financial Guaranty Insurance Losses" in Note 5, Financial Guaranty Insurance.

Derivative Accounting, at Fair Value

For contracts that do not meet the financial guaranty scope exception in the derivative accounting guidance (primarily due to the fact that the insured is not required to be exposed to the insured risk throughout the life of the contract), the Company records such credit derivative contracts at fair value on the consolidated balance sheet with changes in fair value recorded in the consolidated statement of operations. The fair value recorded on the balance sheet represents an exit price in a hypothetical market because the Company does not trade its credit derivative contracts. The fair value is determined using significant Level 3 inputs in an internally developed model while the expected loss to be paid (which represents the net present value of expected cash outflows) uses methodologies and assumptions consistent with financial guaranty insurance expected losses to be paid. See Note 6, Fair Value Measurement and Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives.

VIE Consolidation, at Fair Value

For financial guaranty insurance contracts issued on the debt of variable interest entities over which the Company is deemed to be the primary beneficiary due to its control rights, as defined in GAAP, the Company consolidates the FG VIE. The Company carries the assets and liabilities of the FG VIEs at fair value under the fair value option election. Management assesses the losses on the insured debt of the consolidated FG VIEs in the same manner as other financial guaranty insurance and credit derivative contracts. See Note 8, Consolidated Variable Interest Entities.

Expected Loss to be Paid

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

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

Economic Loss Development

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

Expected loss to be paid and economic loss development include the effects of loss mitigation strategies such as negotiated and estimated recoveries for breaches of R&W, and purchases of insured debt obligations. Additionally, in certain cases, issuers of insured obligations elected, or the Company and an issuer mutually agreed as part of a negotiation, to deliver the underlying collateral or insured obligation to the Company.

In circumstances where the Company has purchased its own insured obligations that have expected losses, expected loss to be paid is reduced by the proportionate share of the insured obligation that is held in the investment portfolio. The difference between the purchase price of the obligation and the fair value excluding the value of the Company's insurance, is treated as a paid loss. Assets that are purchased by the Company are recorded in the investment portfolio, at fair value, excluding the value of the Company's insurance. See Note 9, Investments and Cash and Note 6, Fair Value Measurement.

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 and sector-driven loss severity assumptions or judgmental assessments. 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 and scenarios and the probabilities it assigns to those scenarios based on actual developments during the quarter and its view of future performance.

The financial guaranties issued by the Company insure the credit performance of the guaranteed obligations over an extended period of time, in some cases over 30 years, and in most circumstances, the Company has no right to cancel such financial guaranties. As a result, the Company's estimate of ultimate losses on a policy is subject to significant uncertainty over the life of the insured transaction. Credit performance can be adversely affected by economic, fiscal and financial market variability over the long duration of most contracts.

The determination of expected loss to be paid is an inherently subjective process involving numerous estimates, assumptions and judgments by management, using both internal and external data sources with regard to frequency, severity of loss, economic projections, governmental actions, negotiations and other factors that affect credit performance. These estimates, assumptions and judgments, and the factors on which they are based, may change materially over a quarter, and as a result the Company’s loss estimates may change materially over that same period. Changes over a quarter 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. For example, changes over a quarter in the Company’s loss estimates for its RMBS transactions may be influenced by such factors as the level and timing of loan defaults experienced; changes in housing prices; results from the Company’s loss mitigation activities; and other variables. Similarly, changes over a quarter in the Company’s

loss estimates for municipal obligations supported by specified revenue streams, such as revenue bonds issued by toll road authorities, municipal utilities or airport authorities, generally will be influenced by factors impacting their revenue levels, such as changes in demand; changing demographics; and other economic factors, especially if the obligations do not benefit from financial support from other tax revenues or governmental authorities. On the other hand, changes over a quarter in the Company’s loss estimates for its tax-supported public finance transactions generally will be influenced by factors impacting the public issuer’s ability and willingness to pay, such as changes in the economy and population of the relevant area; changes in the issuer’s ability or willingness to raise taxes, decrease spending or receive federal assistance; new legislation; rating agency downgrades that reduce the issuer’s ability to refinance maturing obligations or issue new debt at a reasonable cost; changes in the priority or amount of pensions and other obligations owed to workers; developments in restructuring or settlement negotiations; and other political and economic factors.

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

In some instances, the terms of the Company's policy gives it the option to pay principal losses that have been recognized in the transaction but which it is not yet required to pay, thereby reducing the amount of guaranteed interest due in the future. The Company has sometimes exercised this option, which uses cash but reduces projected future losses.

The following tables present a roll forward of the present value of net expected loss to be paid for all contracts, whether accounted for as insurance, credit derivatives or FG VIEs, by sector, after the benefit for expected recoveries for breaches of R&W or other expected recoveries. The Company used weighted average risk-free rates for U.S. dollar denominated obligations that ranged from 0.0% to 3.25% as of December 31, 2015 and 0.0% to 2.95% as of December 31, 2014.

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

	Year Ended December 31, 2015 (in millions)
Net expected loss to be paid, beginning of period	$ 619
Economic loss development due to:	
Accretion of discount	14
Changes in discount rates	(11)
Changes in timing and assumptions	76
Total economic loss development	79
Paid losses	(133)
Net expected loss to be paid, end of period	$ 565

Net Expected Loss to be Paid,
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Year Ended December 31, 2015

	Net Expected Loss to be Paid (Recovered) as of December 31, 2014(2)	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid (Recovered) as of December 31, 2015(2)
		(in millions)		
Public Finance:				
U.S. public finance	$ 142	$ 87	$ (15)	$ 214
Non-U.S. public finance	34	(8)	—	26
Public Finance	176	79	(15)	240
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	237	(40)	(108)	89
Option ARM	(19)	(16)	4	(31)
Subprime	223	20	(36)	207
Total first lien	441	(36)	(140)	265
Second lien	(22)	37	22	37
Total U.S. RMBS	419	1	(118)	302
Other structured finance	24	(1)	0	23
Structured Finance	443	0	(118)	325
Total	$ 619	$ 79	$ (133)	$ 565

Net Expected Loss to be Paid,
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Year Ended December 31, 2014

	Net Expected Loss to be Paid (Recovered) as of December 31, 2013	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid (Recovered) as of December 31, 2014(2)
		(in millions)		
Public Finance:				
U.S. public finance	$ 61	$ 97	$ (16)	$ 142
Non-U.S. public finance	42	(8)	—	34
Public Finance	103	89	(16)	176
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	183	(73)	127	237
Option ARM	(4)	(34)	19	(19)
Subprime	222	(12)	13	223
Total first lien	401	(119)	159	441
Second lien	(128)	(40)	146	(22)
Total U.S. RMBS	273	(159)	305	419
Other structured finance	27	(2)	(1)	24
Structured Finance	300	(161)	304	443
Total	$ 403	$ (72)	$ 288	$ 619

(1) Net of ceded paid losses, whether or not such amounts have been settled with reinsurers. Ceded paid losses are typically settled 45 days after the end of the reporting period. Such amounts are recorded in reinsurance recoverable on paid losses included in other assets. The Company paid $8 million and $23 million in LAE for the years ended December 31, 2015 and 2014, respectively.

(2) Includes expected LAE to be paid of $3 million as of December 31, 2015 and $4 million as of December 31, 2014.

Future Net R&W Benefit
As of December 31, 2015, 2014 and 2013

	Future Net R&W Benefit as of December 31, 2015 (1)	Future Net R&W Benefit as of December 31, 2014	Future Net R&W Benefit as of December 31, 2013
		(in millions)	
U.S. RMBS:			
First lien	$ (9)	$ 115	$ 293
Second lien	71	76	127
Total	$ 62	$ 191	$ 420

(1) See the section "Breaches of Representations and Warranties" below for eligible assets held in trust.

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

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

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives (2)	Total
		(in millions)		
Public Finance:				
U.S. public finance	$ 214	$ —	$ —	$ 214
Non-U.S. public finance	26	—	—	26
Public Finance	240	—	—	240
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	72	17	—	89
Option ARM	(31)	—	—	(31)
Subprime	147	60	—	207
Total first lien	188	77	—	265
Second lien	(4)	37	4	37
Total U.S. RMBS	184	114	4	302
Other structured finance	20	—	3	23
Structured Finance	204	114	7	325
Total	$ 444	$ 114	$ 7	$ 565

Net Expected Loss to be Paid (Recovered)
By Accounting Model
As of December 31, 2014

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives (2)	Total
		(in millions)		
Public Finance:				
U.S. public finance	$ 142	$ —	$ —	$ 142
Non-U.S. public finance	34	—	—	$ 34
Public Finance	176	—	—	176
Structured Finance				
U.S. RMBS:				
First lien:				
Alt-A first lien	220	17	—	237
Option ARM	(19)	—	—	(19)
Subprime	153	70	—	223
Total first lien	354	87	—	441
Second lien	(58)	32	4	(22)
Total U.S. RMBS	296	119	4	419
Other structured finance	22	—	2	24
Structured Finance	318	119	6	443
Total	$ 494	$ 119	$ 6	$ 619

(1) Refer to Note 8, Consolidated Variable Interest Entities.

(2) Refer to Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives.

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

Net Economic Loss Development (Benefit)
By Accounting Model
Year Ended December 31, 2015

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
		(in millions)		
Public Finance:				
U.S. public finance	$ 87	$ —	$ —	$ 87
Non-U.S. public finance	(8)	—	—	(8)
Public Finance	79	—	—	79
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	(40)	—	—	(40)
Option ARM	(16)	—	—	(16)
Subprime	11	9	—	20
Total first lien	(45)	9	—	(36)
Second lien	30	6	1	37
Total U.S. RMBS	(15)	15	1	1
Other structured finance	(2)	—	1	(1)
Structured Finance	(17)	15	2	0
Total	$ 62	$ 15	$ 2	$ 79

Net Economic Loss Development (Benefit)
By Accounting Model
Year Ended December 31, 2014

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
		(in millions)		
Public Finance:				
U.S. public finance	$ 97	$ —	$ —	$ 97
Non-U.S. public finance	(8)	—	—	(8)
Public Finance	89	—	—	89
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	(72)	(1)	—	(73)
Option ARM	(35)	1	—	(34)
Subprime	(19)	7	—	(12)
Total first lien	(126)	7	—	(119)
Second lien	(127)	90	(3)	(40)
Total U.S. RMBS	(253)	97	(3)	(159)
Other structured finance	1	—	(3)	(2)
Structured Finance	(252)	97	(6)	(161)
Total	$ (163)	$ 97	$ (6)	$ (72)

____
(1) Refer to Note 8, Consolidated Variable Interest Entities.

(2) Refer to Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives.

Selected U.S. Public Finance Transactions

The Company insures general obligation bonds of the Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations aggregating $2.14 billion net par as of December 31, 2015, $2.06 billion of which is rated BIG. For additional information regarding the Company's exposure to general obligations of Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations, please refer to "Exposure to Puerto Rico" in Note 3, Outstanding Exposure.

On February 25, 2015, a plan of adjustment resolving the bankruptcy filing of the City of Stockton, California under chapter 9 of the U.S. Bankruptcy Code became effective. As of December 31, 2015, the Company’s net exposure subject to the plan consists of $61 million of pension obligation bonds. As part of the plan settlement, the City will repay the pension obligation bonds from certain fixed payments and certain variable payments contingent on the City's revenue growth.

The Company projects that its total net expected loss across its troubled U.S. public finance credits as of December 31, 2015, which incorporated the likelihood of the various outcomes, will be $214 million compared with a net expected loss of $142 million as of December 31, 2014. Economic loss development in 2015 was $87 million, which was primarily attributable to Puerto Rico exposures.

Certain Selected European Country Sub-Sovereign Transactions

The Company insures credits with sub-sovereign exposure to various Spanish and Portuguese issuers where a Spanish and Portuguese sovereign default may cause the sub-sovereigns also to default. The Company's gross exposure to these Spanish and Portuguese credits is $445 million and $91 million, respectively and exposure net of reinsurance for Spanish and Portuguese credits is $277 million and $79 million, respectively. The Company rates most of these issuers in the BB category due to the financial condition of Spain and Portugal and their dependence on the sovereign. The Company's Hungary exposure is to infrastructure bonds dependent on payments from Hungarian governmental entities. The Company's gross exposure to these Hungarian credits is $274 million and its exposure net of reinsurance is $210 million, all of which is rated BIG. The Company estimated net expected losses of $26 million related to these Spanish, Portuguese and Hungarian credits. The economic benefit of approximately $8 million during 2015, was primarily related to changes in the exchange rate between the Euro and US Dollar and certain assumption updates.

Infrastructure Finance

As of December 31, 2015, the Company had exposure of approximately $2.6 billion to infrastructure transactions with refinancing risk. The Company may be required to make claim payments on such exposure, the aggregate amount of the claim payments may be substantial and, although the Company may not experience ultimate loss on a particular transaction, reimbursement may not occur for an extended time. These transactions generally involve long-term infrastructure projects that were financed by bonds that mature prior to the expiration of the project concession. The Company expects the cash flows from these projects to be sufficient to repay all of the debt over the life of the project concession, but also expects the debt to be refinanced in the market at or prior to its maturity. If the issuer is unable to refinance the debt due to market conditions, the Company may have to pay a claim when the debt matures, and then recover from cash flows produced by the project in the future. The Company generally projects that in most scenarios it will be fully reimbursed for such claim payments. However, the recovery of such amounts is uncertain and may take from 10 to 35 years, depending on the transaction and the performance of the underlying collateral. As of December 31, 2015, the Company estimated total claims for the two largest transactions with significant refinancing risk, assuming no refinancing, and based on certain performance assumptions, could be $1.5 billion on a gross basis; such claims would occur from 2017 through 2022. Of such $1.5 billion in estimated gross claims, an estimated $1.3 billion related to obligations of Skyway Concession Company LLC (“SCC”), which owned the concession for the Chicago Skyway toll road. On February 25, 2016, a consortium of three Canadian pension plans purchased SCC for $2.8 billion and the various SCC obligations insured by the Company were retired without a claim on the Company.

Approach to Projecting Losses in U.S. RMBS

The Company projects losses on its insured U.S. RMBS on a transaction-by-transaction basis by projecting the performance of the underlying pool of mortgages over time and then applying the structural features (i.e., payment priorities and tranching) of the RMBS and any R&W agreements to the projected performance of the collateral over time. The resulting projected claim payments or reimbursements are then discounted using risk-free rates.

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

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

In order to derive collateral pool losses from the collateral pool defaults it has projected, the Company applies a loss severity. The loss severity is the amount of loss the transaction experiences on a defaulted loan after the application of net proceeds from the disposal of the underlying property. The Company projects loss severities by sector based on its experience to date. The Company continues to update its evaluation of these loss severities as new information becomes available.

The Company had been enforcing claims for breaches of R&W regarding the characteristics of the loans included in the collateral pools, but has now completed its active pursuit of significant R&W claims. The Company calculates a credit for R&W recoveries to include in its cash flow projections based on agreements it has with R&W providers, which are described in more detail under "Breaches of Representations and Warranties" below.

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

The Company's RMBS loss projection methodology assumes that the housing and mortgage markets will continue improving. Each period the Company makes a judgment as to whether to change the assumptions it uses to make RMBS loss projections based on its observation during the period of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, and, to the extent it observes changes, it makes a judgment as whether those changes are normal fluctuations or part of a trend.

Year-End 2015 Compared to Year-End 2014 U.S. RMBS Loss Projections

Based on its observation during the period of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general assumptions to project RMBS losses as of December 31, 2015 as it used as of December 31, 2014, except that, for its first lien RMBS loss projections for 2015, it shortened by twelve months the period it is projecting it will take in the base case to reach the final CDR as compared with December 31, 2014. The methodology and revised assumptions the Company used to project first lien RMBS losses and the scenarios it employed are described in more detail below under " - U.S. First Lien RMBS Loss Projections: Alt A First Lien, Option ARM and Subprime", and the methodology and assumptions the Company uses to project second lien RMBS losses and the scenarios it employs are described in more detail below under " - U.S. Second Lien RMBS Loss Projections."

Year-End 2014 Compared to Year-End 2013 U.S. RMBS Loss Projections

Based on its observations of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general methodology to project first lien RMBS losses as of December 31, 2014 as it used as of December 31, 2013, but it made a number of refinements to reflect its observations, notably:

- updated the liquidation rates it uses on delinquent loans based on observations and on an assumption that loan modifications (which improve liquidation rates) would over the next year be less frequent than they were over the most recent year

- updated the liquidation rate it uses for loans reported as current but that had been reported as modified over the previous twelve months, based on observed data

- established a liquidation rate assumption for loans reported as current and not modified in the past twelve months but that had been reported as delinquent in the previous twelve months

- established loss severity assumptions by vintage category as well as product type, rather than just product type as done previously

- beginning with the third quarter 2014, each quarter shortened by three months the period it is projecting it will take in the base case to reach the final CDR

The Company estimated the impact of all of the refinements to its first lien RMBS assumptions described above to be a decrease of expected losses (gross of reinsurance) of approximately $28 million (before adjustments for settlements or loss mitigation purchases) in 2014.

Based on its observations of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general methodology to project second lien RMBS losses as of December 31, 2014 as it used as of December 31, 2013, but it made a number of refinements to reflect its observations, notably with respect to most home equity lines of credit ("HELOC") projections to:

- reflect increased recoveries on newly defaulted loans as well as previously defaulted loans
- project incremental defaults associated with increased monthly payments that occur when interest-only periods end
- increase the assumed final conditional prepayment rate ("CPR") from 10% to 15%

The net impact of the refinements in the first two bullet points, which were implemented in the third quarter 2014, was an increase of $30 million in expected losses (gross of reinsurance) in the Company's base case as of September 30, 2014. The net impact of the refinements in the third bullet point was an increase of approximately $12 million in expected losses (gross of reinsurance) in the Company's base case as of December 31, 2014.

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

The majority of projected losses in first lien RMBS transactions are expected to come from non-performing mortgage loans (those that are or in the past twelve months have been two or more payments behind, have been modified, are in foreclosure, or have been foreclosed upon). Changes in the amount of non-performing loans from the amount projected in the previous period are one of the primary drivers of loss development in this portfolio. In order to determine the number of defaults resulting from these delinquent and foreclosed loans, the Company applies a liquidation rate assumption to loans in each of various non-performing categories. The Company arrived at its liquidation rates based on data purchased from a third party provider and assumptions about how delays in the foreclosure process and loan modifications may ultimately affect the rate at which loans are liquidated. Each quarter the Company reviews the most recent twelve months of this data and (if necessary) adjusts its liquidation rates based on its observations. The following table shows liquidation assumptions for various non-performing categories.

First Lien Liquidation Rates

	December 31, 2015	December 31, 2014
Current Loans Modified in the Previous 12 Months		
Alt-A	25%	25%
Option ARM	25	25
Subprime	25	25
Current Loans Delinquent in the Previous 12 Months		
Alt-A	25	25
Option ARM	25	25
Subprime	25	25
30 - 59 Days Delinquent		
Alt-A	35	35
Option ARM	40	40
Subprime	45	35
60 - 89 Days Delinquent		
Alt-A	45	50
Option ARM	50	55
Subprime	55	40
90 + Days Delinquent		
Alt-A	55	60
Option ARM	60	65
Subprime	60	55
Bankruptcy		
Alt-A	45	45
Option ARM	50	50
Subprime	40	40
Foreclosure		
Alt-A	65	75
Option ARM	70	80
Subprime	70	70
Real Estate Owned		
All	100	100

While the Company uses liquidation rates as described above to project defaults of non-performing loans (including current loans modified or delinquent within the last 12 months), it projects defaults on presently current loans by applying a CDR trend. The start of that CDR trend is based on the defaults the Company projects will emerge from currently nonperforming, recently nonperforming and modified loans. The total amount of expected defaults from the non-performing loans is translated into a constant CDR (*i.e.*, the CDR plateau), which, if applied for each of the next 36 months, would be sufficient to produce approximately the amount of defaults that were calculated to emerge from the various delinquency categories. The CDR thus calculated individually on the delinquent collateral pool for each RMBS is then used as the starting point for the CDR curve used to project defaults of the presently performing loans.

In the base case, after the initial 36-month CDR plateau period, each transaction's CDR is projected to improve over 12 months to an intermediate CDR (calculated as 20% of its CDR plateau); that intermediate CDR is held constant for 36 months and then trails off in steps to a final CDR of 5% of the CDR plateau. In the base case, the Company assumes the final CDR will be reached 7.5 years after the initial 36-month CDR plateau period, which is twelve months shorter than assumed at December 31, 2014. Under the Company's methodology, defaults projected to occur in the first 36 months represent defaults that can be attributed to loans that were modified or delinquent in the last 12 months or that are currently delinquent or in foreclosure, while the defaults projected to occur using the projected CDR trend after the first 36 month period represent defaults attributable to borrowers that are currently performing or are projected to reperform.

Another important driver of loss projections is loss severity, which is the amount of loss the transaction incurs on a loan after the application of net proceeds from the disposal of the underlying property. Loss severities experienced in first lien transactions have reached historically high levels, and the Company is assuming in the base case that these high levels generally will continue for another 18 months. The Company determines its initial loss severity based on actual recent experience. The Company then assumes that loss severities begin returning to levels consistent with underwriting assumptions beginning after the initial 18 month period, declining to 40% in the base case over 2.5 years. Beginning for December 31, 2014, the Company differentiated the loss severity assumptions depending on the vintage of the transaction, as shown in the table below.

The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions used in the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 first lien U.S. RMBS.

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

	As of December 31, 2015		As of December 31, 2014	
	Range	Weighted Average	Range	Weighted Average
Alt-A First Lien				
Plateau CDR	4.0% - 12.0%	7.7%	3.7% - 13.4%	9.3%
Intermediate CDR	0.8% - 2.4%	1.5%	0.7% - 2.7%	1.9%
Period until intermediate CDR	48 months		48 months	
Final CDR	0.2% - 0.6%	0.4%	0.2% - 0.7%	0.5%
Initial loss severity:				
2005 and prior	60.0%		60.0%	
2006	70.0%		70.0%	
2007	65.0%		65.0%	
Initial CPR	2.7% - 14.3%	6.2%	1.7% - 9.5%	5.1%
Final CPR(2)	15%		15%	
Option ARM				
Plateau CDR	3.5% - 10.3%	7.9%	4.3% - 14.2%	10.9%
Intermediate CDR	0.7% - 2.1%	1.6%	0.9% - 2.8%	2.2%
Period until intermediate CDR	48 months		48 months	
Final CDR	0.2% - 0.5%	0.4%	0.2% - 0.7%	0.5%
Initial loss severity:				
2005 and prior	60.0%		60.0%	
2006	70.0%		70.0%	
2007	65.0%		65.0%	
Initial CPR	1.5% - 6.5%	2.7%	2.3% - 6.2%	3.3%
Final CPR(2)	15%		15%	
Subprime				
Plateau CDR	5.4% - 13.2%	9.7%	6.0% - 15.0%	10.8%
Intermediate CDR	1.1% - 2.6%	1.9%	1.2% - 3.0%	2.2%
Period until intermediate CDR	48 months		48 months	
Final CDR	0.3% - 0.7%	0.5%	0.3% - 0.7%	0.5%
Initial loss severity:				
2005 and prior	75.0%		75.0%	
2006	90.0%		90.0%	
2007	90.0%		90.0%	
Initial CPR	0.0% - 6.7%	3.4%	0.1% - 5.3%	3.4%
Final CPR(2)	15%		15%	

____

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

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

The rate at which the principal amount of loans is voluntarily prepaid may impact both the amount of losses projected (since that amount is a function of the conditional default rate, the loss severity and the loan balance over time) as well as the amount of excess spread (the amount by which the interest paid by the borrowers on the underlying loan exceeds the amount of interest owed on the insured obligations). The assumption for the voluntary CPR follows a similar pattern to that of the conditional default rate. The current level of voluntary prepayments is assumed to continue for the plateau period before gradually increasing over 12 months to the final CPR, which is assumed to be 15% in the base case. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. These assumptions are the same as those the Company used for December 31, 2014.

In estimating expected losses, the Company modeled and probability weighted sensitivities for first lien transactions by varying its assumptions of how fast a recovery is expected to occur. One of the variables used to model sensitivities was how quickly the conditional default rate returned to its modeled equilibrium, which was defined as 5% of the initial conditional default rate. The Company also stressed CPR and the speed of recovery of loss severity rates. The Company probability weighted a total of five scenarios as of December 31, 2015. The Company used a similar approach to establish its pessimistic and optimistic scenarios as of December 31, 2015 as it used as of December 31, 2014, increasing and decreasing the periods of stress from those used in the base case.

In a somewhat more stressful environment than that of the base case, where the conditional default rate plateau was extended six months (to be 42 months long) before the same more gradual conditional default rate recovery and loss severities were assumed to recover over 4.5 rather than 2.5 years (and subprime loss severities were assumed to recover only to 60% and Option ARM and Alt A loss severities to only 45%), expected loss to be paid would increase from current projections by approximately $9 million for Alt-A first liens, $5 million for Option ARM and $38 million for subprime transactions.

In an even more stressful scenario where loss severities were assumed to rise and then recover over nine years and the initial ramp-down of the conditional default rate was assumed to occur over 15 months and other assumptions were the same as the other stress scenario, expected loss to be paid would increase from current projections by approximately $24 million for Alt-A first liens, $9 million for Option ARM and $53 million for subprime transactions.

In a scenario with a somewhat less stressful environment than the base case, where conditional default rate recovery was somewhat less gradual, expected loss to be paid would decrease from current projections by approximately $1 million for Alt-A first liens, $12 million for Option ARM and $9 million for subprime transactions.

In an even less stressful scenario where the conditional default rate plateau was six months shorter (30 months, effectively assuming that liquidation rates would improve) and the conditional default rate recovery was more pronounced, (including an initial ramp-down of the conditional default rate over nine months), expected loss to be paid would decrease from current projections by approximately $10 million for Alt-A first liens, $21 million for Option ARM and $31 million for subprime transactions.

U.S. Second Lien RMBS Loss Projections

Second lien RMBS transactions include both HELOC and closed end second lien. The Company believes the primary variable affecting its expected losses in second lien RMBS transactions is the amount and timing of future losses in the collateral pool supporting the transactions. Expected losses are also a function of the structure of the transaction; the voluntary prepayment rate (typically also referred to as CPR of the collateral); the interest rate environment; and assumptions about the draw rate and loss severity.

In second lien transactions the projection of near-term defaults from currently delinquent loans is relatively straightforward because loans in second lien transactions are generally “charged off” (treated as defaulted) by the securitization’s servicer once the loan is 180 days past due. Most second lien transactions report the amount of loans in five monthly delinquency categories (*i.e.*, 30-59 days past due, 60-89 days past due, 90-119 days past due, 120-149 days past due and 150-179 days past due). The Company estimates the amount of loans that will default over the next five months by calculating current representative liquidation rates. A liquidation rate is the percent of loans in a given cohort (in this instance, delinquency category) that ultimately default. Similar to first liens, the Company then calculates a CDR for six months, which is the period over which the currently delinquent collateral is expected to be liquidated. That CDR is then used as the basis for the plateau period that follows the embedded five months of losses. Liquidation rates assumed as of December 31, 2015, were from 10% to 100%.

For the base case scenario, the CDR (the “plateau CDR”) was held constant for six months. Once the plateau period has ended, the CDR is assumed to gradually trend down in uniform increments to its final long-term steady state CDR. (The

long-term steady state CDR is calculated as the constant CDR that would have yielded the amount of losses originally expected at underwriting.) In the base case scenario, the time over which the CDR trends down to its final CDR is 28 months. Therefore, the total stress period for second lien transactions is 34 months, comprising five months of delinquent data, a one month plateau period and 28 months of decrease to the steady state CDR, the same as of December 31, 2014.

HELOC loans generally permit the borrower to pay only interest for an initial period (often ten years) and, after that period, require the borrower to make both the monthly interest payment and a monthly principal payment, and so increase the borrower's aggregate monthly payment. Some of the HELOC loans underlying the Company's insured HELOC transactions have reached their principal amortization period. The Company has observed that the increase in monthly payments occurring when a loan reaches its principal amortization period, even if mitigated by borrower relief offered by the servicer, is associated with increased borrower defaults. Thus, most of the Company's HELOC projections incorporate an assumption that a percentage of loans reaching their amortization periods will default around the time of the payment increase. These projected defaults are in addition to those generated using the CDR curve as described above. This assumption is similar to the one used at December 31, 2014. For December 31, 2015 the Company used the approach it had refined in the third quarter of 2015 to calculate the number of additional delinquencies as a function of the number of modified loans in the transaction and the final steady state CDR but increased those additional resulting defaults. Under this refined approach, transactions that have worse than average expected experience will have higher defaults and transactions where borrowers are receiving modifications so that they will not default when their interest only period ends will have higher losses.

When a second lien loan defaults, there is generally a very low recovery. The Company had assumed as of December 31, 2015 that it will generally recover only 2% of the collateral defaulting in the future and declining additional amounts of post-default receipts on previously defaulted collateral. Based on experience, the Company changed this assumption from the assumption it had used as at December 31, 2014, when it assumed it would generally recover 10% or less of the collateral defaulting in the future and declining additional amounts of post-default receipts on previously defaulted collateral.

The rate at which the principal amount of loans is prepaid may impact both the amount of losses projected as well as the amount of excess spread. In the base case, an average CPR (based on experience of the most recent three quarters) is assumed to continue until the end of the plateau before gradually increasing to the final CPR over the same period the CDR decreases. The final CPR is assumed to be 15% for second lien transactions, which is lower than the historical average but reflects the Company’s continued uncertainty about the projected performance of the borrowers in these transactions. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. This pattern is generally consistent with how the Company modeled the CPR at December 31, 2014. To the extent that prepayments differ from projected levels it could materially change the Company’s projected excess spread and losses.

The Company uses a number of other variables in its second lien loss projections, including the spread between relevant interest rate indices. These variables have been relatively stable and in the relevant ranges have less impact on the projection results than the variables discussed above. However, in a number of HELOC transactions the servicers have been modifying poorly performing loans from floating to fixed rates, and, as a result, rising interest rates would negatively impact the excess spread available from these modified loans to support the transactions. The Company incorporated these modifications in its assumptions.

In estimating expected losses, the Company modeled and probability weighted five possible CDR curves applicable to the period preceding the return to the long-term steady state CDR. The Company used five scenarios at December 31, 2015 and three scenarios at December 31, 2014. The Company believes that the level of the elevated CDR and the length of time it will persist, the ultimate prepayment rate, and the amount of additional defaults because of the expiry of the interest only period, are the primary drivers behind the likely amount of losses the collateral will suffer. The Company continues to evaluate the assumptions affecting its modeling results.

Most of the Company's projected second lien RMBS losses are from HELOC transactions. The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions for the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 HELOCs.

Key Assumptions in Base Case Expected Loss Estimates
HELOCs(1)

	As of December 31, 2015		As of December 31, 2014	
	Range	Weighted Average	Range	Weighted Average
Plateau CDR	4.9% - 23.5%	11.0%	2.8% - 6.8%	4.1%
Final CDR trended down to	0.6% - 3.2%	1.2%	0.6% - 3.2%	1.2%
Period until final CDR	34 months		34 months	
Initial CPR	10.9%		6.9% - 21.8%	10.8%
Final CPR(2)	10.0% - 15.0%	13.3%	15.0% - 21.8%	15.6%
Loss severity	98.0%		90.0% - 98.0%	90.3%

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

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

The Company's base case assumed a six month CDR plateau and a 28 month ramp-down (for a total stress period of 34 months). The Company also modeled a scenario with a longer period of elevated defaults and another with a shorter period of elevated defaults. Increasing the CDR plateau to eight months and increasing the ramp-down by three months to 31-months (for a total stress period of 39 months), and doubling the defaults relating to the end of the interest only period would increase the expected loss by approximately $36 million for HELOC transactions. On the other hand, reducing the CDR plateau to four months and decreasing the length of the CDR ramp-down to 25 months (for a total stress period of 29 months) and lowering the ultimate prepayment rate to 10% would decrease the expected loss by approximately $22 million for HELOC transactions.

Breaches of Representations and Warranties

Generally, when mortgage loans were transferred into a securitization, the loan originator(s) and/or sponsor(s) provided R&W that the loans meet certain characteristics, and a breach of such R&W often requires that the loan be repurchased from the securitization. The Company has pursued such breaches of R&W on a loan-by-loan basis or in cases where a provider of R&W refused to honor its repurchase obligations, the Company sometimes chose to initiate litigation. The Company's success in pursuing these strategies permitted the Company to enter into agreements with R&W providers under which those providers made payments to the Company, agreed to make payments to the Company in the future, and / or repurchased loans from the transactions, all in return for releases of related liability by the Company.

Through December 31, 2015 the Company has caused entities providing R&Ws to pay, or agree to pay approximately $3.2 billion (gross of reinsurance) in respect of their R&W liabilities for transactions in which the Company has provided insurance.

The Company has included in its net expected loss estimates as of December 31, 2015 an estimated net benefit of $62 million (net of reinsurance), all of which is projected to be received pursuant to existing agreements with R&W providers or is otherwise collateralized. The Company is no longer actively pursuing R&W providers where it does not have such an agreement. Most of the amount projected to be received pursuant to existing agreements with R&W providers benefits from eligible assets placed in trusts to collateralize the R&W provider's future reimbursement obligation, with the amount of such collateral subject to increase or decrease from time to time as determined by rating agency requirements. Currently the Company has agreements with three counterparties where a future reimbursement obligation is collateralized by eligible assets held in trust:

- **Bank of America**. Under Assured Guaranty's agreement with Bank of America Corporation and certain of its subsidiaries ("Bank of America"), Bank of America agreed to reimburse Assured Guaranty for 80% of claims on the first lien transactions covered by the agreement that Assured Guaranty pays in the future, until the aggregate lifetime collateral losses (not insurance losses or claims) on those transactions reach $6.6 billion. As of December 31, 2015, aggregate lifetime collateral losses on those transactions was $4.4 billion ($4.0 billion for AGM and $0.4 billion for AGC), and Assured Guaranty was projecting in its base case that such collateral losses would eventually reach $5.2 billion ($4.73 billion for AGM and $0.42 billion for AGC). Bank of America's reimbursement obligation is secured by

$138 million of collateral held in trust for the AGM's benefit and $327 million of collateral held in trust that is available for either AGM or AGC.

- **Deutsche Bank.** Under Assured Guaranty's May 2012 agreement with Deutsche Bank AG and certain of its affiliates (collectively, “Deutsche Bank”), Deutsche Bank agreed to reimburse Assured Guaranty for certain claims it pays in the future on eight first and second lien transactions, including 80% of claims it pays on those transactions until the aggregate lifetime claims (before reimbursement) reach $319 million. As of December 31, 2015, Assured Guaranty was projecting in its base case that such aggregate lifetime claims would remain below $319 million. In the event aggregate lifetime claims paid exceed $389 million, Deutsche Bank must reimburse Assured Guaranty for 85% of such claims paid (in excess of $389 million) until such claims paid reach $600 million. Deutsche Bank's reimbursement obligation is secured by $55 million of collateral held in trust for AGM's benefit and $0.7 million of collateral held in trust that is available for either AGM or AGC.

- **UBS.** On May 6, 2013, Assured Guaranty entered into an agreement with UBS Real Estate Securities Inc. and affiliates ("UBS") and a third party resolving Assured Guaranty’s claims and liabilities related to specified RMBS transactions that were issued, underwritten or sponsored by UBS and insured by AGM or AGC under financial guaranty insurance policies. Under the agreement, UBS agreed to reimburse the Company for 85% of future losses on three first lien RMBS transactions, and such reimbursement obligation is secured by $54 million of collateral held in trust for the Company's benefit.

The Company uses the same RMBS projection scenarios and weightings to project its future R&W benefit as it uses to project RMBS losses on its portfolio. To the extent the Company increases its loss projections, the R&W benefit generally will also increase, subject to the agreement limits and thresholds described above. Similarly, to the extent the Company decreases its loss projections, the R&W benefit generally will also decrease, subject to the agreement limits and thresholds described above.

Other structured finance

The Company's other structured finance includes $544 million net par rated BIG, including transactions backed by manufactured housing loans. The Company has expected loss to be paid of $23 million as of December 31, 2015. The economic benefit during 2015 was $1 million.

Recovery Litigation

Public Finance Transactions

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

5. Financial Guaranty Insurance

Financial Guaranty Insurance Premiums

The portfolio of outstanding exposures discussed in Note 3, Outstanding Exposure, includes financial guaranty contracts that meet the definition of insurance contracts as well as those that meet the definition of a derivative under GAAP. Amounts presented in this note relate only to financial guaranty insurance contracts. See Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives for amounts that relate to CDS and Note 8, Consolidated Variable Interest Entities for amounts that relate to FG VIEs.

Accounting Policies

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 the contract was written on a direct basis, assumed from another financial guarantor under a reinsurance treaty, ceded to another insurer under a reinsurance treaty, or acquired in a business combination.

Premium receivables comprise the present value of contractual or expected future premium collections discounted using the risk-free rate. Unearned premium reserve represents deferred premium revenue, less claim payments and recoveries received that have not yet been recognized in the statement of operations (“contra-paid”). The following discussion relates to the deferred premium revenue component of the unearned premium reserve, while the contra-paid is discussed below under "Financial Guaranty Insurance Losses."

The amount of deferred premium revenue at contract inception is determined as follows:

- For premiums received upfront on financial guaranty insurance contracts that were originally underwritten by the Company, deferred premium revenue 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 that were originally underwritten by the Company, deferred premium revenue is the present value of either (1) contractual premiums due or (2) in cases where the underlying collateral is comprised of homogeneous pools of assets, the expected premiums to be collected over the life of the contract. To be considered a homogeneous pool of assets, prepayments must be contractually prepayable, the amount of prepayments must be probable, and the timing and amount of prepayments must be reasonably estimable. When the Company adjusts prepayment assumptions or expected premium collections, an adjustment is recorded to the deferred premium revenue, with a corresponding adjustment to the premium receivable, and prospective changes are recognized in premium revenues. 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. 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.

- For financial guaranty insurance contracts acquired in a business combination, deferred premium revenue is equal to the fair value of the Company's stand-ready obligation portion of the insurance contract at the date of acquisition based on what a hypothetical similarly rated financial guaranty insurer would have charged for the contract at that date and not the actual cash flows under the insurance contract. The amount of deferred premium revenue may differ significantly from cash collections due primarily to fair value adjustments recorded in connection with a business combination.

The Company recognizes deferred premium revenue as earned premium over the contractual period or expected period of the contract in proportion to the amount of insurance protection provided. As premium revenue is recognized, a corresponding decrease to the deferred premium revenue is recorded. The amount of insurance protection provided is a function of the insured principal 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 principal amounts outstanding in the reporting period compared with the sum of each of the insured principal amounts outstanding for all periods. When an insured financial obligation is retired before its maturity, the financial guaranty insurance contract is extinguished. Any nonrefundable deferred premium revenue 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.

Deferred premium revenue ceded to reinsurers (ceded unearned premium reserve) is recorded as an asset. Direct, assumed and ceded earned premium revenue are presented together as net earned premiums in the statement of operations. Net earned premiums comprise the following:

Net Earned Premiums

	Year Ended December 31,	
	2015	2014
	(in millions)	
Scheduled net earned premiums	$ 243	$ 278
Acceleration of net earned premiums (1)	151	88
Accretion of discount on net premiums receivable	10	8
Net earned premiums(2)	$ 404	$ 374

(1) Reflects the unscheduled refunding or termination of the insurance on an insured obligation as well as changes in scheduled earnings due to changes in the expected lives of the insured obligations.

(2) Excludes $19 million and $31 million for the year ended December 31, 2015 and 2014, respectively, related to consolidated FG VIEs.

Components of Unearned Premium Reserve

	As of December 31, 2015			As of December 31, 2014		
	Gross	Ceded	Net(1)	Gross	Ceded	Net(1)
	(in millions)					
Deferred premium revenue	$ 2,943	$ 853	$ 2,090	$ 3,331	$ 966	$ 2,365
Contra-paid(2)	(10)	(8)	(2)	94	(8)	102
Unearned premium reserve	$ 2,933	$ 845	$ 2,088	$ 3,425	$ 958	$ 2,467

(1) Excludes $97 million and $114 million of deferred premium revenue, and $30 million and $42 million of contra-paid related to FG VIEs as of December 31, 2015 and December 31, 2014, respectively.

(2) See "Financial Guaranty Insurance Losses" below for an explanation of "contra-paid".

Gross Premium Receivable
Roll Forward

	Year Ended December 31,	
	2015	2014
	(in millions)	
Beginning of period, December 31	$ 450	$ 578
Gross premium written	169	136
Gross premiums received	(171)	(192)
Adjustments:		
Changes in the expected term	(7)	(47)
Accretion of discount	13	3
Foreign exchange translation	(25)	(28)
Consolidation/deconsolidation of FG VIEs	(4)	0
End of period, December 31(1)	$ 425	$ 450

(1) Excludes $5 million and $6 million as of December 31, 2015 and 2014, respectively, related to consolidated FG VIEs.

Foreign exchange translation relates to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 82% and 78% of installment premiums at December 31, 2015 and 2014, respectively, are denominated in currencies other than the U.S. dollar, primarily the Euro and British Pound Sterling.

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

**Expected Collections of
Financial Guaranty Gross Premiums Receivable
(Undiscounted)**

	As of December 31, 2015
	(in millions)
2016 (January 1 – March 31)	$ 23
2016 (April 1 – June 30)	15
2016 (July 1 – September 30)	11
2016 (October 1 – December 31)	9
2017	40
2018	35
2019	33
2020	32
2021-2025	133
2026-2030	96
2031-2035	69
After 2035	64
Total (1)	$ 560

(1) Excludes expected cash collections on FG VIEs of $6 million.

Scheduled Financial Guaranty Net Earned Premiums

	As of December 31, 2015
	(in millions)
2016 (January 1 – March 31)	$ 59
2016 (April 1 – June 30)	57
2016 (July 1 – September 30)	55
2016 (October 1 – December 31)	53
Subtotal 2016	224
2017	191
2018	169
2019	152
2020	138
2021-2025	528
2026-2030	327
2031-2035	196
After 2035	165
Net deferred premium revenue(1)	2,090
Future accretion	92
Total future net earned premiums	$ 2,182

____

(1) Excludes scheduled net earned premiums on consolidated FG VIEs of $97 million.

Selected Information for Financial Guaranty Policies Paid in Installments

	As of December 31, 2015	As of December 31, 2014
	(dollars in millions)	
Premiums receivable	$ 425	$ 450
Gross deferred premium revenue	966	1,097
Weighted-average risk-free rate used to discount premiums	3.2%	3.6%
Weighted-average period of premiums receivable (in years)	10.0	10.1

Financial Guaranty Insurance Acquisition Costs

Accounting Policy

Policy acquisition costs that are directly related and essential to successful insurance contract acquisition and ceding commission income on ceded reinsurance contracts are deferred for contracts accounted for as insurance and reported net. Amortization of deferred ceding commissions includes the accretion of discount on ceding commission income and expense.

Capitalized policy acquisition costs include expenses such as the cost of underwriting personnel attributable to successful underwriting efforts. 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 deferred acquisition costs ("DAC"), with a corresponding offset to net premiums receivable or reinsurance balances payable. Management uses its judgment in determining the type and amount of costs to be deferred. The Company conducts an annual study to determine which operating costs qualify for deferral. 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. DAC, net of deferred ceding commission income, is amortized in proportion to net earned

premiums. When an insured obligation is retired early, the remaining related DAC, net of ceding commission income is recognized at that time.

Expected losses, which include 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 Ceding Commissions,
Net of DAC(1)

	Year Ended December 31,	
	2015	2014
	(in millions)	
Beginning of period	$ (78)	$ (86)
Costs deferred during the period:		
Commissions on ceded business	(19)	(7)
Premium taxes	1	3
Compensation and other acquisition costs	8	7
Total	(10)	3
Costs amortized during the period	13	5
End of period	$ (75)	$ (78)

____
(1) The balances are included in other liabilities on the consolidated balance sheets.

Financial Guaranty Insurance Losses

Accounting Policies

Loss and LAE Reserve

Loss and LAE reserve reported on the balance sheet relates only to direct and assumed reinsurance contracts that are accounted for as insurance, all of which are financial guaranty insurance contracts. The corresponding reserve ceded to reinsurers is reported as reinsurance recoverable on unpaid losses. As discussed in Note 6, Fair Value Measurement, contracts that meet the definition of a derivative, as well as consolidated FG VIE assets and liabilities, are recorded separately at fair value. Any expected losses related to consolidated FG VIEs are eliminated upon consolidation. Any expected losses on credit derivatives are not recorded as loss and LAE reserve on the consolidated balance sheet.

Under financial guaranty insurance accounting, the sum of unearned premium reserve and loss and LAE reserve represents the Company's stand-ready obligation. Unearned premium reserve is deferred premium revenue, less claim payments and recoveries received that have not yet been recognized in the statement of operations ("contra-paid"). At contract inception, the entire stand-ready obligation is represented by unearned premium reserve. A loss and LAE reserve for an insurance contract is recorded only to the extent, and for the amount, that expected loss to be paid net of contra-paid ("total losses") exceed the deferred premium revenue, on a contract by contract basis. As a result, the Company has expected loss to be paid that has not yet been expensed. Such amounts will be recognized in future periods as deferred premium revenue amortizes into income.

When a claim or LAE payment is made on a contract, it first reduces any recorded loss and LAE reserve. To the extent there is no loss and LAE reserve on a contract, then such claim payment is recorded as "contra-paid," which reduces the unearned premium reserve. The contra-paid is recognized in the line item "loss and LAE" in the consolidated statement of operations when and for the amount that total losses exceed the remaining deferred premium revenue on the insurance contract. Loss and LAE in the consolidated statement of operations is presented net of cessions to reinsurers.

Salvage and Subrogation Recoverable

When the Company becomes entitled to the cash flow from the underlying collateral of an insured credit under salvage and subrogation rights as a result of a claim payment or estimated future claim payment, it reduces the expected loss to be paid on the contract. Such reduction in expected loss to be paid can result in one of the following:

- a reduction in the corresponding loss and LAE reserve with a benefit to the income statement,
- no entry recorded, if "total loss" is not in excess of deferred premium revenue, or
- the recording of a salvage asset with a benefit to the income statement if the transaction is in a net recovery position at the reporting date.

The Company recognizes the expected recovery of claim payments (including recoveries from settlement with R&W providers) made by the Company prior to the date of its acquisition by AGL consistent with its policy for recognizing recoveries on all financial guaranty insurance contracts. To the extent that the estimated amount of recoveries increases or decreases, due to changes in facts and circumstances, the Company would recognize a benefit or expense consistent with how changes in the expected recovery of all other claim payments are recorded. The ceded component of salvage and subrogation recoverable is recorded in the line item reinsurance balances payable.

Expected Loss to be Expensed

Expected loss to be expensed represents past or expected future net claim payments that have not yet been expensed. Such amounts will be expensed in future periods as deferred premium revenue 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.

Insurance Contracts' Loss Information

The following table provides information on loss and LAE reserves and salvage and subrogation recoverable, net of reinsurance. The Company used weighted average risk-free rates for U.S. dollar denominated financial guaranty insurance obligations that ranged from 0.0% to 3.25% as of December 31, 2015 and 0.0% to 2.95% as of December 31, 2014. Financial guaranty insurance expected LAE reserve was $3 million as of December 31, 2015 and $4 million as of December 31, 2014.

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

	As of December 31, 2015			As of December 31, 2014		
	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)
			(in millions)			
Public Finance:						
U.S. public finance	$ 178	$ 0	$ 178	$ 119	$ —	$ 119
Non-U.S. public finance	15	—	15	21	—	21
Public Finance	193	—	193	140	—	140
Structured Finance:						
U.S. RMBS:						
First lien:						
Alt-A first lien	13	—	13	22	—	22
Option ARM	7	40	(33)	11	39	(28)
Subprime	159	15	144	156	7	149
First lien	179	55	124	189	46	143
Second lien	15	47	(32)	0	73	(73)
Total U.S. RMBS	194	102	92	189	119	70
Other structured finance	19	1	18	20	—	20
Structured Finance	213	103	110	209	119	90
Subtotal	406	103	303	349	119	230
Effect of consolidating FG VIEs	(72)	0	(72)	(78)	(1)	(77)
Total (1)	$ 334	$ 103	$ 231	$ 271	$ 118	$ 153

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

Components of Net Reserves (Salvage)

	As of December 31, 2015	As of December 31, 2014
	(in millions)	
Loss and LAE reserve	$ 488	$ 404
Reinsurance recoverable on unpaid losses	(154)	(133)
Loss and LAE reserve, net	334	271
Salvage and subrogation recoverable	(109)	(130)
Salvage and subrogation payable(1)	6	12
Salvage and subrogation recoverable, net	(103)	(118)
Net reserves (salvage)	$ 231	$ 153

____

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

The table below provides a reconciliation of net expected loss to be paid to net expected loss to be expensed. Expected loss to be paid differs from expected loss to be expensed due to: (1) the contra-paid which represent the claim payments made and recoveries received that have not yet been recognized in the statement of operations, (2) salvage and subrogation recoverable for transactions that are in a net recovery position where the Company has not yet received recoveries on claims previously paid (having the effect of reducing net expected loss to be paid by the amount of the previously paid claim and the expected recovery), but will have no future income effect (because the previously paid claims and the corresponding recovery of those claims will offset in income in future periods), and (3) loss reserves that have already been established (and therefore expensed but not yet paid).

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

	As of December 31, 2015
	(in millions)
Net expected loss to be paid	$ 558
Less: net expected loss to be paid for FG VIEs	114
Total	444
Contra-paid, net	2
Salvage and subrogation recoverable, net of reinsurance	103
Loss and LAE reserve, net of reinsurance	(334)
Net expected loss to be expensed (present value)(1)	$ 215

____

(1) Excludes $72 million as of December 31, 2015 related to consolidated FG VIEs.

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

Net Expected Loss to be Expensed
Financial Guaranty Insurance Contracts

	As of December 31, 2015
	(in millions)
2016 (January 1 – March 31)	$ 9
2016 (April 1 – June 30)	8
2016 (July 1 – September 30)	6
2016 (October 1 – December 31)	6
Subtotal 2016	29
2017	22
2018	20
2019	19
2020	16
2021-2025	56
2026-2030	29
2031-2035	16
After 2035	8
Net expected loss to be expensed	215
Discount	121
Total expected future loss and LAE	$ 336

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

	Year Ended December 31,	
	2015	2014
	(in millions)	
Public Finance:		
U.S. public finance	$ 78	$ 96
Non-U.S. public finance	0	(1)
Public finance	78	95
Structured Finance:		
U.S. RMBS:		
First lien:		
Alt-A first lien	(15)	(39)
Option ARM	(8)	(24)
Subprime	31	4
First lien	8	(59)
Second lien	51	(31)
Total U.S. RMBS	59	(90)
Other structured finance	0	1
Structured finance	59	(89)
Loss and LAE on insurance contracts before FG VIE consolidation	137	6
Effect of consolidating FG VIEs	(27)	(31)
Loss and LAE	$ 110	$ (25)

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

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

	BIG Categories								
	BIG 1		BIG 2		BIG 3				
	Gross	Ceded	Gross	Ceded	Gross	Ceded	Total BIG, Net	Effect of Consolidating VIEs	Total
	(dollars in millions)								
Number of risks(1)	59	(52)	14	(14)	43	(43)	116	—	116
Remaining weighted-average contract period (in years)	10.2	9.8	10.0	8.7	6.8	7.1	9.3	—	9.3
Outstanding exposure:									
Principal	$ 4,718	$ (1,763)	$ 1,923	$ (544)	$ 2,325	$ (325)	$ 6,334	$ —	$ 6,334
Interest	2,665	(952)	983	(234)	786	(101)	3,147	—	3,147
Total(2)	$ 7,383	$ (2,715)	$ 2,906	$ (778)	$ 3,111	$ (426)	$ 9,481	$ —	$ 9,481
Expected cash outflows (inflows)	$ 274	$ (84)	$ 531	$ (136)	$ 1,044	$ (115)	$ 1,514	$ (290)	$ 1,224
Potential recoveries									
Undiscounted R&W	72	(2)	(47)	3	(77)	7	(44)	—	(44)
Other(3)	(409)	21	(87)	14	(364)	64	(761)	146	(615)
Total potential recoveries	(337)	19	(134)	17	(441)	71	(805)	146	(659)
Subtotal	(63)	(65)	397	(119)	603	(44)	709	(144)	565
Discount	103	7	(109)	24	(175)	(1)	(151)	30	(121)
Present value of expected cash flows	$ 40	$ (58)	$ 288	$ (95)	$ 428	$ (45)	$ 558	$ (114)	$ 444
Deferred premium revenue	$ 168	$ (44)	$ 69	$ (8)	$ 343	$ (47)	$ 481	$ (95)	$ 386
Reserves (salvage)(4)	$ (13)	$ (37)	$ 240	$ (90)	$ 224	$ (21)	$ 303	$ (72)	$ 231

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of December 31, 2014

	BIG Categories								
	BIG 1		BIG 2		BIG 3			Effect of Consolidating VIEs	
	Gross	Ceded	Gross	Ceded	Gross	Ceded	Total BIG, Net		Total
	(dollars in millions)								
Number of risks(1)	71	(65)	14	(14)	38	(38)	123	—	123
Remaining weighted-average contract period (in years)	8.4	8.1	7.9	8.8	7.6	8.1	8.2	—	8.2
Outstanding exposure:									
Principal	$ 8,281	$ (3,341)	$ 1,594	$ (468)	$ 2,013	$ (279)	$ 7,800	$ —	$ 7,800
Interest	3,693	(1,435)	616	(187)	784	(105)	3,366	—	3,366
Total(2)	$ 11,974	$ (4,776)	$ 2,210	$ (655)	$ 2,797	$ (384)	$ 11,166	$ —	$ 11,166
Expected cash outflows (inflows)	$ 1,538	$ (796)	$ 621	$ (128)	$ 1,101	$ (101)	$ 2,235	$ (298)	$ 1,937
Potential recoveries									
Undiscounted R&W	(12)	0	(46)	2	(160)	11	(205)	—	(205)
Other(3)	(1,526)	767	(197)	6	(326)	44	(1,232)	149	(1,083)
Total potential recoveries	(1,538)	767	(243)	8	(486)	55	(1,437)	149	(1,288)
Subtotal	0	(29)	378	(120)	615	(46)	798	(149)	649
Discount	11	0	(67)	18	(150)	3	(185)	30	(155)
Present value of expected cash flows	$ 11	$ (29)	$ 311	$ (102)	$ 465	$ (43)	$ 613	$ (119)	$ 494
Deferred premium revenue	$ 324	$ (100)	$ 107	$ (9)	$ 287	$ (43)	$ 566	$ (111)	$ 455
Reserves (salvage)(4)	$ (41)	$ (9)	$ 207	$ (92)	$ 185	$ (20)	$ 230	$ (77)	$ 153

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

(2) Includes BIG amounts related to FG VIEs.

(3) Includes excess spread and draws on HELOCs.

(4) See table "Components of net reserves (salvage)."

Ratings Impact on Financial Guaranty Business

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

For example, AGM has issued financial guaranty insurance policies in respect of the obligations of municipal obligors under interest rate swaps. AGM insures periodic payments owed by the municipal obligors to the bank counterparties. In certain cases, AGM also insures termination payments that may be owed by the municipal obligors to the bank counterparties. If (i) AGM has been downgraded below the rating trigger set forth in a swap under which it has insured the termination payment, which rating trigger varies on a transaction by transaction basis; (ii) the municipal obligor has the right to cure by, but has failed in, posting collateral, replacing AGM or otherwise curing the downgrade of AGM; (iii) the transaction documents include as a condition that an event of default or termination event with respect to the municipal obligor has occurred, such as the rating of the municipal obligor being downgraded past a specified level, and such condition has been met; (iv) the bank counterparty has elected to terminate the swap; (v) a termination payment is payable by the municipal obligor; and (vi) the municipal obligor has failed to make the termination payment payable by it, then AGM would be required to pay the termination payment due by the municipal obligor, in an amount not to exceed the policy limit set forth in the financial

guaranty insurance policy. At AGM's current financial strength ratings, if the other conditions giving rise to the obligation of AGM to make a termination payment under the swap termination policies were all satisfied, then AGM could pay claims in an amount not exceeding approximately $150 million in respect of such termination payments. Taking into consideration whether the rating of the municipal obligor is below any applicable specified trigger, if the financial strength ratings of AGM were further downgraded below "A" by S&P or below "A2" by Moody's, and the other conditions giving rise to the obligation of AGM to make a payment under the swap policies were all satisfied, then AGM could pay claims in an additional amount not exceeding approximately $377 million in respect of such termination payments.

As another example, with respect to variable rate demand obligations ("VRDOs") for which a bank has agreed to provide a liquidity facility, a downgrade of AGM may provide the bank with the right to give notice to bondholders that the bank will terminate the liquidity facility, causing the bondholders to tender their bonds to the bank. Bonds held by the bank accrue interest at a “bank bond rate” that is higher than the rate otherwise borne by the bond (typically the prime rate plus 2.00% - 3.00%, and capped at the lesser of 25% and the maximum legal limit). In the event the bank holds such bonds for longer than a specified period of time, usually 90-180 days, the bank has the right to demand accelerated repayment of bond principal, usually through payment of equal installments over a period of not less than five years. In the event that a municipal obligor is unable to pay interest accruing at the bank bond rate or to pay principal during the shortened amortization period, a claim could be submitted to AGM under its financial guaranty policy. As of December 31, 2015, the Company had insured approximately $4.8 billion net par of VRDOs, of which approximately $0.2 billion of net par constituted VRDOs issued by municipal obligors rated BBB- or lower pursuant to the Company’s internal rating. The specific terms relating to the rating levels that trigger the bank’s termination right, and whether it is triggered by a downgrade by one rating agency or a downgrade by all rating agencies then rating the insurer, vary depending on the transaction.

In addition, AGM may be required to pay claims in respect of AGMH’s former financial products business if Dexia SA and its affiliates, from which Assured Guaranty had purchased AGMH and its subsidiaries, do not comply with their obligations following a downgrade of the financial strength rating of AGM. Most of the guaranteed investment contracts ("GICs") insured by AGM allow the GIC holder to terminate the GIC and withdraw the funds in the event of a downgrade of AGM below A3 or A-, with no right of the GIC issuer to avoid such withdrawal by posting collateral or otherwise enhancing its credit. Each GIC contract stipulates the thresholds below which the GIC issuer must post eligible collateral, along with the types of securities eligible for posting and the collateralization percentage applicable to each security type. These collateralization percentages range from 100% of the GIC balance for cash posted as collateral to, typically, 108% for asset-backed securities. If the entire aggregate accreted GIC balance of approximately $1.8 billion as of December 31, 2015 were terminated, the assets of the GIC issuers (which had an aggregate market value which exceed the liabilities by $0.8 billion) would be sufficient to fund the withdrawal of the GIC funds.

6. Fair Value Measurement

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

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

Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments include amounts to reflect counterparty credit quality, the Company’s creditworthiness and constraints on liquidity. As markets and products develop and the pricing for certain products becomes more or less transparent, the Company may refine its methodologies and assumptions. During 2015, 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 fair value hierarchy is determined based on whether the inputs to valuation techniques used to measure fair value are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Company estimates of market assumptions. The fair value hierarchy prioritizes model inputs into three broad levels as follows, with Level 1 being the highest and Level 3 the lowest. An asset or liability's categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation.

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

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

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

In May 2015, the FASB issued ASU No. 2015-07, Fair Value Measurement *(Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share*, which removes the requirement to make certain disclosures and categorize within the fair value hierarchy certain investments for which fair value is measured using net asset value ("NAV") per share as a practical expedient. Effective December 31, 2015, the Company retrospectively adopted this accounting guidance that no longer requires investments measured at fair value using the NAV per share practical expedient to be categorized within the fair value hierarchy. Therefore, the Company no longer includes its investments in partially-owned investment companies, investment funds, and limited partnerships within the fair value hierarchy and the Level 3 rollforward tables disclosed below. Prior period amounts within the fair value hierarchy disclosures contained in this section have been revised to conform to the current period presentation. This guidance requires a change in disclosure only and adoption of this guidance did not have an impact on our financial condition or results of operations.

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

Measured and Carried at Fair Value

Fixed-Maturity Securities and Short-Term Investments

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

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

where at least one significant model assumption or input is unobservable, are considered to be Level 3 in the fair value hierarchy.

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

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

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

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

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

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

As of December 31, 2015, the Company used models to price 27 fixed-maturity securities and short-term investments (which were purchased or obtained for loss mitigation or other risk management purposes), which was 12.5% or $793 million of the Company's fixed-maturity securities and short-term investments at fair value. Most Level 3 securities were priced with the assistance of an independent third-party. The pricing is based on a discounted cash flow approach using the third-party's proprietary pricing models. The models use inputs such as projected prepayment speeds; severity assumptions; recovery lag assumptions; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); home price depreciation/appreciation rates based on macroeconomic forecasts and recent trading activity. The yield used to discount the projected cash flows is determined by reviewing various attributes of the bond including collateral type, weighted average life, sensitivity to losses, vintage, and convexity, in conjunction with market data on comparable securities. Significant changes to any of these inputs could materially change the expected timing of cash flows within these securities which is a significant factor in determining the fair value of the securities.

Other Invested Assets

As of December 31, 2015 and December 31, 2014, other invested assets include investments carried and measured at fair value on a recurring basis of $51 million and $94 million, respectively, and include primarily an investment in the global property catastrophe risk market and an investment in a fund that invests primarily in senior loans and bonds. Fair values for the majority of these investments are based on their respective NAV per share or equivalent, as a practical expedient, and are excluded from the fair value hierarchy table below. Other invested assets also include fixed-maturity securities classified as trading carried as Level 2.

Other Assets

Committed Capital Securities

The fair value of AGM Committed Preferred Trust Securities (the "AGM CPS"), which is recorded in "other assets" on the consolidated balance sheets, represents the difference between the present value of remaining expected put option premium payments under AGM CPS agreements, and the estimated present value that the Company would hypothetically have to pay currently for a comparable security (see Note 16, Notes Payable and Credit Facilities). The AGM CPS are carried at fair value with changes in fair value recorded in the consolidated statement of operations. The estimated current cost of the AGM CPS is based on several factors, including broker-dealer quotes for the outstanding securities, AGM CDS spreads, the U.S. dollar forward swap curve, London Interbank Offered Rate ("LIBOR") curve projections and the term the securities are estimated to remain outstanding.

Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company's credit derivatives consist primarily of insured CDS contracts, and also include interest rate swaps that fall under derivative accounting standards requiring fair value accounting through the statement of operations. The Company did not enter into CDS with the intent to trade these contracts and the Company may not unilaterally terminate a CDS contract absent an event of default or termination event that entitles the Company to terminate such contracts; however, the Company has mutually agreed with various counterparties to terminate certain CDS transactions. Such terminations generally are not completed at fair value but instead for an amount that approximates the present value of future premiums or for a negotiated amount.

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

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

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

The fair value of the Company's credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay and the estimated present value of premiums that a financial guarantor of comparable credit-worthiness would hypothetically charge or pay at the reporting date for the same protection. The fair value of the Company's credit derivatives depends on a number of factors, including notional amount of the contract, expected term, credit spreads, changes in interest rates, the credit ratings of referenced entities, the Company's own credit risk and remaining contractual cash flows. The expected remaining contractual premium cash flows are the most readily observable inputs since they are based on the CDS contractual terms. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. Consistent with previous years, market conditions at December 31, 2015 were such that market prices of the Company's CDS contracts were not available.

Management considers factors such as current prices charged for similar agreements, when available, performance of underlying assets, life of the instrument, and the nature and extent of activity in the financial guaranty credit derivative marketplace. The assumptions that management uses to determine the fair value may change in the future due to market conditions. Due to the inherent uncertainties of the assumptions used in the valuation models, actual experience may differ from the estimates reflected in the Company's consolidated financial statements and the differences may be material.

Assumptions and Inputs

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

- Gross spread.

- The allocation of gross spread among:

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

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

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

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

The rates used to discount future expected premium cash flows ranged from 0.54% to 2.38% at December 31, 2015 and 0.26% to 2.66% at December 31, 2014.

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

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

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

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

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

- Credit spreads interpolated based upon market indices.

- Credit spreads provided by the counterparty of the CDS.

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

Information by Credit Spread Type (1)

	As of December 31, 2015	As of December 31, 2014
Based on actual collateral specific spreads	—%	0.1%
Based on market indices	100.0%	99.9%
Total	100%	100%

____

(1) Based on par.

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

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

The premium the Company receives is referred to as the "net spread." The Company's pricing model takes into account not only how credit spreads on risks that it assumes affect pricing, but also how the Company's own credit spread affects the pricing of its deals. The Company's own credit risk is factored into the determination of net spread based on the impact of changes in the quoted market price for credit protection bought on the Company, as reflected by quoted market prices on CDS referencing AGM. For credit spreads on the Company's name the Company obtains the quoted price of CDS contracts traded on AGM from market data sources published by third parties. The cost to acquire CDS protection referencing AGM affects the amount of spread on CDS deals that the Company retains and, hence, their fair value. As the cost to acquire CDS protection referencing AGM increases, the amount of premium the Company retains on a deal generally decreases. As the cost to acquire CDS protection referencing AGM decreases, the amount of premium the Company retains on a deal generally increases. In the Company's valuation model, the premium the Company captures is not permitted to go below the minimum rate that the Company would currently charge to assume similar risks. This assumption can have the effect of mitigating the amount of unrealized gains that are recognized on certain CDS contracts. Given the current market conditions and the Company's own credit spreads, approximately 14%, and 19%, based on number of deals, of the Company's CDS contracts are fair valued using this minimum premium as of December 31, 2015 and December 31, 2014, respectively. The percentage of deals that price using the minimum premiums fluctuates due to changes in AGM's credit spreads. In general when AGM's credit spreads narrow, the cost to hedge AGM's name declines and more transactions price above previously established floor levels. Meanwhile, when AGM's credit spreads widen, the cost to hedge AGM's name increases causing more transactions to price at previously established floor levels. The Company corroborates the assumptions in its fair value model, including the portion of exposure to AGM hedged by its counterparties, with independent third parties each reporting period. The current level of AGM's own credit spread has resulted in the bank or deal originator hedging a significant portion of its exposure to AGM. This reduces the amount of contractual cash flows AGM can capture as premium for selling its protection.

The amount of premium a financial guaranty insurance market participant can demand is inversely related to the cost of credit protection on the insurance company as measured by market credit spreads assuming all other assumptions remain constant. This is because the buyers of credit protection typically hedge a portion of their risk to the financial guarantor, due to the fact that the contractual terms of the Company's contracts typically do not require the posting of collateral by the guarantor. The extent of the hedge depends on the types of instruments insured and the current market conditions.

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

Example

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

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

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

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

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

Strengths and Weaknesses of Model

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

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

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

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

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

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

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

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

- At December 31, 2015 and 2014, the markets for the inputs to the model were highly illiquid, which impacts their reliability.

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

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

Fair Value Option on FG VIEs' Assets and Liabilities

The Company elected the fair value option for all the FG VIEs' assets and liabilities. See Note 8, Consolidated Variable Interest Entities.

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

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

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

Not Carried at Fair Value

Financial Guaranty Insurance Contracts

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

Notes Payable

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

Other Invested Assets

Other invested assets primarily consist of a surplus note issued by AGC to AGM. The fair value of the surplus note was determined by calculating the effect of changes in U.S. Treasury yield adjusted for a credit factor at the end of each reporting period. The fair value measurement of the surplus note was classified as Level 3.

Other Assets and Other Liabilities

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

Financial Instruments Carried at Fair Value

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

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2015

	Fair Value	Fair Value Hierarchy Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$ 4,041	$ —	$ 4,033	$ 8
U.S. government and agencies	51	—	51	—
Corporate securities	668	—	597	71
Mortgage-backed securities:				
RMBS	532	—	208	324
Commercial mortgage-backed securities ("CMBS")	223	—	223	—
Asset-backed securities	394	—	64	330
Foreign government securities	181	—	181	—
Total fixed-maturity securities	6,090	—	5,357	733
Short-term investments	257	176	21	60
Other invested assets (1)	10	—	5	5
Credit derivative assets	63	—	—	63
FG VIEs' assets, at fair value	735	—	—	735
Other assets	29	—	—	29
Total assets carried at fair value	$ 7,184	$ 176	$ 5,383	$ 1,625
Liabilities:				
Credit derivative liabilities	$ 154	$ —	$ —	$ 154
FG VIEs' liabilities with recourse, at fair value	713	—	—	713
FG VIEs' liabilities without recourse, at fair value	121	—	—	121
Total liabilities carried at fair value	$ 988	$ —	$ —	$ 988

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2014

	Fair Value	Fair Value Hierarchy Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$ 4,189	$ —	$ 4,181	$ 8
U.S. government and agencies	69	—	69	—
Corporate securities	643	—	564	79
Mortgage-backed securities:				
RMBS	661	—	262	399
CMBS	266	—	266	—
Asset-backed securities	193	—	98	95
Foreign government securities	191	—	191	—
Total fixed-maturity securities	6,212	—	5,631	581
Short-term investments	377	197	180	—
Other invested assets (1)	23	—	16	7
Credit derivative assets	79	—	—	79
FG VIEs' assets, at fair value	823	—	—	823
Other assets	17	—	—	17
Total assets carried at fair value	$ 7,531	$ 197	$ 5,827	$ 1,507
Liabilities:				
Credit derivative liabilities	$ 287	$ —	$ —	$ 287
FG VIEs' liabilities with recourse, at fair value	830	—	—	830
FG VIEs' liabilities without recourse, at fair value	114	—	—	114
Total liabilities carried at fair value	$ 1,231	$ —	$ —	$ 1,231

(1) Excluded from the table above are investment funds of $45 million and $76 million as of December 31, 2015 and December 31, 2014, respectively, measured using the NAV per share practical expedient. Includes Level 3 mortgage loans that are recorded at fair value on a non-recurring basis.

Changes in Level 3 Fair Value Measurements

The table below presents a roll forward of the Company's Level 3 financial instruments carried at fair value on a recurring basis during the years ended December 31, 2015 and 2014.

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2015

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Short-Term Investments	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)									
Fair value as of December 31, 2014	$ 8	$ 79	$ 399	$ 95	$ —	$ 823	$ 19	$ (208)	$ (830)	$ (114)
Total pretax realized and unrealized gains/(losses) recorded in:(1)										
Net income (loss)	1 (2)	3 (2)	16 (2)	6 (2)	24 (2)	61 (3)	11 (4)	134 (6)	93 (3)	(18) (3)
Other comprehensive income (loss)	0	(11)	(8)	(17)	0	—	—	—	—	—
Purchases	—	—	46	278	52 (7)	—	—	—	—	—
Settlements	(1)	—	(129)	(32)	(16)	(253)	0	(17)	155	11
FG VIE consolidations	—	—	—	—	—	104	—	—	(131)	—
FG VIE deconsolidations	—	—	—	—	—	—	—	—	—	—
Fair value as of December 31, 2015	$ 8	$ 71	$ 324	$ 330	$ 60	$ 735	$ 30	$ (91)	$ (713)	$ (121)
Change in unrealized gains/(losses) related to financial instruments held as of December 31, 2015	$ 0	$ (11)	$ (6)	$ (17)	$ 0	$ 107	$ 12	$ 18	$ (15)	$ (8)

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2014

	Fixed-Maturity Securities								
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
					(in millions)				
Fair value as of December 31, 2013	$ 8	$ 136	$ 238	$ 141	$ 1,691	$ 23	$ (228)	$ (1,275)	$ (686)
Total pretax realized and unrealized gains/(losses) recorded in: (1)									
Net income (loss)	1 (2)	(46) (2)	16 (2)	12 (2)	144 (3)	(4) (4)	41 (6)	(30) (3)	(48) (3)
Other comprehensive income (loss)	0	(6)	25	2	—	—	—	—	—
Purchases	—	—	160	—	—	—	—	—	—
Settlements	(1)	(5)	(41)	(60)	(360)	0	(21)	351	14
FG VIE consolidations	—	—	—	—	46	—	—	(25)	(21)
FG VIE deconsolidations	—	—	1	—	(698)	—	—	149	627
Fair value as of December 31, 2014	$ 8	$ 79	$ 399	$ 95	$ 823	$ 19	$ (208)	$ (830)	$ (114)
Change in unrealized gains/(losses) related to financial instruments held as of December 31, 2014	$ 0	$ (6)	$ 22	$ 1	$ 110	$ (4)	$ 19	$ (14)	$ (10)

____

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

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

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

(4) Recorded in fair value gains (losses) on committed capital securities ("CCS"), net realized investment gains (losses) and net investment income.

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

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

(7) Primarily non-cash transaction.

(8) Includes CCS and other invested assets.

Level 3 Fair Value Disclosures

Quantitative Information About Level 3 Fair Value Inputs
At December 31, 2015

Financial Instrument Description (1)	Fair Value at December 31, 2015 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets (2):				
Fixed-maturity securities (3):				
Corporate securities	$ 71	Yield	21.8%	
RMBS	324	CPR	0.3% - 9.0%	2.2%
		CDR	4.2% - 9.3%	7.1%
		Loss severity	60.0% - 100.0%	74.5%
		Yield	4.7% - 8.2%	5.9%
Asset-backed securities:				
Investor owned utility	69	Cash flow receipts	100.0%	
		Collateral recovery period	2.9 years	
		Discount factor	7.0%	
Triple-X life insurance transactions	261	Yield	4.8%	
Short-term investments	60	Yield	17.0%	
FG VIEs' assets, at fair value	735	CPR	2.3% - 8.3%	3.9%
		CDR	2.3% - 16.0%	4.9%
		Loss severity	40.0% - 100.0%	83.7%
		Yield	3.1% - 20.0%	6.7%
Other assets	29	Quotes from third party pricing	$45	
		Term (years)	5 years	

Financial Instrument Description (1)	Fair Value at December 31, 2015 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Liabilities:				
Credit derivative liabilities, net	(91)	Hedge cost (in bps)	32.8 - 274.5	37.8
		Bank profit (in bps)	3.9 - 1,017.5	74.4
		Internal floor (in bps)	7.0 - 100.0	34.9
		Internal credit rating	AAA - CCC	AAA
FG VIEs' liabilities, at fair value	(834)	CPR	2.3% - 8.3%	3.9%
		CDR	2.3% - 16.0%	4.9%
		Loss severity	40.0% - 100.0%	83.7%
		Yield	3.1% - 20.0%	5.7%

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

(2) Excludes several investments recorded in other invested assets with fair value of $4 million.

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

Quantitative Information About Level 3 Fair Value Inputs
At December 31, 2014

Financial Instrument Description (1)	Fair Value at December 31, 2014 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets:				
Fixed-maturity securities:				
Obligations of state and political subdivisions	$ 8	Rate of inflation	1.0% - 3.0%	2.0%
		Cash flow receipts	0.5% - 22.4%	22.1%
		Yield	4.6%	
		Collateral recovery period	1 month - 9 years	8.4 years
Corporate securities	79	Yield	17.8%	
RMBS	399	CPR	0.3% - 8.1%	3.1%
		CDR	3.1% - 10.6%	5.4%
		Loss severity	52.6% - 100.0%	75.7%
		Yield	4.6% - 11.7%	6.4%
Asset-backed securities:				
Investor owned utility	95	Cash flow receipts	100%	
		Collateral recovery period	4 years	
		Discount factor	7.0%	
Other invested assets	7	Discount for lack of liquidity	20%	
		Recovery on delinquent loans	40%	
		Default rates	0.0% - 7.0%	5.8%
		Loss severity	40.0% - 75.0%	68.3%
		Prepayment speeds	5.0% - 15.0%	12.3%
FG VIEs’ assets, at fair value	823	CPR	0.3% - 7.0%	3.2%
		CDR	1.6% - 11.8%	4.4%
		Loss severity	40.0% - 100.0%	81.4%
		Yield	2.7% - 17.7%	7.9%
Other assets	17	Quotes from third party pricing	$ 52 - $57	$54.5
		Term (years)	5 years	

Financial Instrument Description (1)	Fair Value at December 31, 2014 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Liabilities:				
Credit derivative liabilities, net	(208)	Hedge cost (in bps)	21.2 - 243.8	38.6
		Bank profit (in bps)	1.0 - 916.9	48.6
		Internal floor (in bps)	7.0 - 100.0	9.2
		Internal credit rating	AAA - CCC	AAA
FG VIEs' liabilities, at fair value	(944)	CPR	0.3% - 7.0%	3.2%
		CDR	1.6% - 11.8%	4.4%
		Loss severity	40.0% - 100.0%	81.4%
		Yield	2.7% - 17.7%	6.2%

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

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

Fair Value of Financial Instruments

	As of December 31, 2015		As of December 31, 2014	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in millions)			
Assets:				
Fixed-maturity securities	$ 6,090	$ 6,090	$ 6,212	$ 6,212
Short-term investments	257	257	377	377
Other invested assets(1)	360	428	407	491
Credit derivative assets	63	63	79	79
FG VIEs' assets, at fair value	735	735	823	823
Other assets	91	91	89	89
Liabilities:				
Financial guaranty insurance contracts (2)	2,016	3,528	2,325	3,279
Notes payable	13	12	19	16
Credit derivative liabilities	154	154	287	287
FG VIEs' liabilities with recourse, at fair value	713	713	830	830
FG VIEs' liabilities without recourse, at fair value	121	121	114	114
Other liabilities	2	2	21	21

(1) Includes investments not carried at fair value with a carrying value of $305 million and $308 million as of December 31, 2015 and 2014, respectively.

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

7. Financial Guaranty Contracts Accounted for as Credit Derivatives

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

Accounting Policy

Credit derivatives are recorded at fair value. Changes in fair value are recorded in “net change in fair value of credit derivatives” on the consolidated statement of operations. Realized gains (losses) and other settlements on credit derivatives include credit derivative premiums received and receivable for credit protection the Company has sold under its insured CDS contracts, premiums paid and payable for credit protection the Company has purchased, claims paid and payable and received and receivable related to insured credit events under these contracts, ceding commission expense or income and realized gains or losses related to their early termination. Fair value of credit derivatives is reflected as either net assets or net liabilities determined on a contract by contract basis in the Company's consolidated balance sheets. See Note 6, Fair Value Measurement, for a discussion on the fair value methodology for credit derivatives.

Credit Derivative Net Par Outstanding by Sector

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

The estimated remaining weighted average life of credit derivatives was 2.3 years at December 31, 2015 and 2.5 years at December 31, 2014. The components of the Company's credit derivative net par outstanding are presented below.

Credit Derivatives
Subordination and Ratings

Asset Type	As of December 31, 2015				As of December 31, 2014			
	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating
				(dollars in millions)				
Pooled corporate obligations:								
Collateralized loan obligations/ collateralized bond obligations	$ 3,980	29.1%	40.6%	AAA	$ 7,375	29.6%	33.6%	AAA
Synthetic investment grade pooled corporate	4,859	21.8	19.4	AAA	7,354	22.3	20.3	AAA
Trust preferred securities collateralized debt obligations ("TruPS CDOs")	2	56.0	96.9	AAA	9	56.0	86.4	AAA
Market value CDOs of corporate obligations	946	17.0	30.1	AAA	946	17.0	20.1	AAA
Total pooled corporate obligations	9,787	24.3	29.1	AAA	15,684	25.5	26.6	AAA
U.S. RMBS:								
Subprime first lien	47	—	—	AAA	55	—	—	AAA
Closed-end second lien	51	—	—	BBB+	61	—	—	BBB+
Total U.S. RMBS	98	—	—	AA-	116	—	—	AA-
Other	1,756	—	—	A-	2,393	—	—	A-
Total	$ 11,641			AAA	$ 18,193			AAA

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

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

The $1.8 billion of exposure in "Other" CDS contracts as of December 31, 2015 comprises numerous deals typically structured with significant underlying credit enhancement and spread across various asset classes, such as commercial receivables, international RMBS, infrastructure, regulated utilities and healthcare.

Distribution of Credit Derivative Net Par Outstanding by Internal Rating

Ratings	As of December 31, 2015 Net Par Outstanding	As of December 31, 2015 % of Total	As of December 31, 2014 Net Par Outstanding	As of December 31, 2014 % of Total
	(dollars in millions)			
AAA	$ 9,089	78.1%	$ 14,471	79.5%
AA	985	8.5	1,843	10.1
A	853	7.3	920	5.1
BBB	607	5.2	830	4.6
BIG	107	0.9	129	0.7
Credit derivative net par outstanding	$ 11,641	100.0%	$ 18,193	100.0%

Fair Value of Credit Derivatives

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

	Year Ended December 31, 2015	Year Ended December 31, 2014
	(in millions)	
Realized gains on credit derivatives	$ 32	$ 33
Net credit derivative losses (paid and payable) recovered and recoverable and other settlements	(15)	(11)
Realized gains (losses) and other settlements on credit derivatives	17	22
Net change in unrealized gains (losses) on credit derivatives:		
Pooled corporate obligations	(17)	13
U.S. RMBS	1	3
Other	133	3
Net change in unrealized gains (losses) on credit derivatives	117	19
Net change in fair value of credit derivatives	$ 134	$ 41

Net Par and Realized Gain from Terminations of Credit Derivative Contracts

	Year Ended December 31, 2015	Year Ended December 31, 2014
	(in millions)	
Net par of terminated credit derivative contracts	$ 485	$ 565
Realized gains on credit derivatives	11	1

During 2015, unrealized fair value gains were generated primarily as a result of a CDS termination. The Company terminated a Triple-X life insurance securitization transaction during the period and recognized unrealized fair value gains of $99 million. This was the primary driver of the unrealized fair value gains in the Other sector during the period. The remainder of the fair value gains for the period were a result of tighter implied net spreads across the Other and U.S. RMBS sectors. The tighter implied net spreads were primarily a result of the increased cost to buy protection in AGM's name, particularly for the one year CDS spread. These transactions were pricing at or above their floor levels, therefore when the cost of purchasing CDS protection on AGM increased, the implied spreads that the Company would expect to receive on these transactions decreased. The unrealized fair value gains were partially offset by unrealized fair value losses in the pooled corporate sector where the Company's transactions are quickly approaching maturity. The majority of transactions in this sector are marked in an asset

position as they are AAA rated and performing well. As these transactions approach maturity the positive marks on these transactions will naturally revert to zero, leading to unrealized fair value losses.

During 2014, unrealized fair value gains were generated primarily in the pooled corporate obligations and Other sectors. The unrealized gains were a result of the run-off of outstanding exposure as the transactions in these sectors approach maturity, as well as the expiration of several large synthetic high yield pooled corporate transactions. These unrealized gains were partially offset by unrealized losses resulting from the decreased cost to buy protection in AGM's name as the market cost of AGM's credit protection decreased during the period. Several transactions were pricing above their floor levels (or the minimum rate at which the Company would consider assuming these risks based on historical experience); therefore when the cost of purchasing CDS protection on AGM decreased, which management refers to as the CDS spread on AGM, the implied spreads that the Company would expect to receive on these transactions increased.

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

CDS Spread on AGM
Quoted price of CDS contract (in basis points)

	As of December 31,		
	2015	2014	2013
Five-year CDS spread	366	325	525
One-year CDS spread	131	85	220

Fair Value of Credit Derivatives Assets (Liabilities)
and Effect of AGM
Credit Spreads

	As of December 31, 2015	As of December 31, 2014
	(in millions)	
Fair value of credit derivatives before effect of AGM credit spread	$ (145)	$ (344)
Plus: Effect of AGM credit spread	54	136
Net fair value of credit derivatives	$ (91)	$ (208)

The fair value of CDS contracts at December 31, 2015, before considering the implications of AGM's credit spreads, is a direct result of continued wide credit spreads in the fixed income security markets and ratings downgrades. The asset classes that remain most affected are pooled corporate obligations. Comparing December 31, 2015 with December 31, 2014, there was large runoff of par outstanding and termination of CDS contracts, which resulted in a gain of approximately $199 million, before taking into account AGM's credit spreads.

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

The following table presents the fair value and the present value of expected claim payments or recoveries (i.e. net expected loss to be paid as described in Note 4) for contracts accounted for as derivatives.

Net Fair Value and Expected Losses
Credit Derivatives by Sector

Asset Type	Fair Value of Credit Derivative Asset (Liability), net As of December 31, 2015	Fair Value of Credit Derivative Asset (Liability), net As of December 31, 2014	Expected Loss to be (Paid) Recovered (1) As of December 31, 2015	Expected Loss to be (Paid) Recovered (1) As of December 31, 2014
		(in millions)		
Pooled corporate obligations	$ (7)	$ 10	$ —	$ —
U.S. RMBS	(6)	(7)	(4)	(4)
Other	(78)	(211)	(3)	(2)
Total	$ (91)	$ (208)	$ (7)	$ (6)

Sensitivity to Changes in Credit Spread

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

Effect of Changes in Credit Spread
As of December 31, 2015

Credit Spreads(1)	Estimated Net Fair Value (Pre-Tax)	Estimated Change in Gain/(Loss) (Pre-Tax)
	(in millions)	
100% widening in spreads	$ (165)	$ (74)
50% widening in spreads	(128)	(37)
25% widening in spreads	(110)	(19)
10% widening in spreads	(99)	(8)
Base Scenario	(91)	—
10% narrowing in spreads	(84)	7
25% narrowing in spreads	(76)	15
50% narrowing in spreads	(59)	32

___

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

8. Consolidated Variable Interest Entities

Background

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

AGM is not primarily liable for the debt obligations issued by the VIEs it insures and would only be required to make payments on those insured debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due and only for the amount of the shortfall. AGM’s creditors do not have any rights with regard to the collateral supporting the debt issued by the FG VIEs. Proceeds from sales, maturities, prepayments and interest from such underlying collateral may only be used to pay Debt Service on VIE liabilities. Net fair value gains and losses on FG VIEs are expected to reverse to zero at maturity of the VIE debt, except for net premiums received and net claims paid by AGM under the financial guaranty insurance contract. The Company’s estimate of expected loss to be paid for FG VIEs is included in Note 4, Expected Loss to be Paid.

Accounting Policy

The Company evaluates whether it is the primary beneficiary of its VIEs. If the Company concludes that it is the primary beneficiary, it is required to consolidate the entire VIE in the Company's financial statements and eliminate the effects of the financial guaranty insurance contracts issued by AGM on the consolidated FG VIEs debt obligations.

The primary beneficiary of a VIE is the enterprise that has both 1) the power to direct the activities of a VIE that most significantly impact the entity's economic performance; and 2) the obligation to absorb losses of the entity that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE.

As part of the terms of its financial guaranty contracts, the Company obtains certain protective rights with respect to the VIE that are triggered by the occurrence of certain events, such as failure to be in compliance with a covenant due to poor deal performance or a deterioration in a servicer or collateral manager's financial condition. At deal inception, the Company typically is not deemed to control a VIE; however, once a trigger event occurs, the Company's control of the VIE typically increases. The Company continuously evaluates its power to direct the activities that most significantly impact the economic performance of VIEs that have debt obligations insured by the Company and, accordingly, where the Company is obligated to absorb VIE losses or receive benefits that could potentially be significant to the VIE. The Company obtains protective rights under its insurance contracts that give the Company additional controls over a VIE if there is either deterioration of deal performance or in the financial health of the deal servicer. The Company is deemed to be the control party for certain VIEs under GAAP, typically when its protective rights give it the power to both terminate and replace the deal servicer, which are characteristics specific to the Company's financial guaranty contracts. If the protective rights that could make the Company the control party have not been triggered, then the VIE is not consolidated. If the Company is deemed no longer to have those protective rights, the transaction is deconsolidated.

The FG VIEs' liabilities that are insured by the Company are considered to be with recourse, because the Company guarantees the payment of principal and interest regardless of the performance of the related FG VIEs' assets. FG VIEs' liabilities that are not insured by the Company are considered to be without recourse, because the payment of principal and interest of these liabilities is wholly dependent on the performance of the FG VIEs' assets.

The Company has limited contractual rights to obtain the financial records of its consolidated FG VIEs. The FG VIEs do not prepare separate GAAP financial statements; therefore, the Company compiles GAAP financial information for them based on trustee reports prepared by and received from third parties. Such trustee reports are not available to the Company until approximately 30 days after the end of any given period. The time required to perform adequate reconciliations and analyses of the information in these trustee reports results in a one quarter lag in reporting the FG VIEs' activities. The Company records the fair value of FG VIE assets and liabilities based on modeled prices. The Company updates the model assumptions each reporting period for the most recent available information, which incorporates the impact of material events that may have occurred since the quarter lag date. The net change in the fair value of consolidated FG VIE assets and liabilities is recorded in "fair value gains (losses) on FG VIEs" in the consolidated statements of operations. Interest income and interest expense are derived from the trustee reports and also included in “fair value gains (losses) on FG VIEs.” The Company has elected the fair value option for assets and liabilities classified as FG VIEs' assets and liabilities because the carrying amount transition method was not practical.

The cash flows generated by the FG VIE assets, including R&W recoveries, are classified as cash flows from investing activities. Paydowns of FG liabilities are supported by the cash flows generated by FG VIE assets, and for liabilities with recourse, possibly claim payments made by AGM under its financial guaranty insurance contracts. Paydowns of FG liabilities both with and without recourse are classified as cash flows used in financing activities by the Company. Interest income, interest expense and other expenses of the FG VIE assets and liabilities are classified as operating cash flows. Claim payments made by AGM under the financial guaranty contracts issued to the FG VIEs are eliminated upon consolidation and

therefore such claim payments are treated as paydowns of FG VIE liabilities as a financing activity as opposed to an operating activity of AGM.

Consolidated FG VIEs

Number of FG VIEs Consolidated

	Year Ended December 31,	
	2015	2014
Beginning of the period, December 31	25	32
Consolidated(1)	1	1
Deconsolidated(1)	—	(6)
Matured	(2)	(2)
End of the period, December 31	24	25

(1) Net loss on consolidation was $26 million in 2015 and net gain on deconsolidation was $102 million in 2014 and recorded in "fair value gains (losses) on FG VIEs" in the consolidated statement of operations.

The total unpaid principal balance for the FG VIEs' assets that were over 90 days or more past due was approximately $136 million at December 31, 2015 and $177 million at December 31, 2014. The aggregate unpaid principal of the FG VIEs' assets was approximately $610 million greater than the aggregate fair value at December 31, 2015. The aggregate unpaid principal of the FG VIEs' assets was approximately $670 million greater than the aggregate fair value at December 31, 2014.

The change in the instrument-specific credit risk of the FG VIEs' assets held as of December 31, 2015 that was recorded in the consolidated statements of operations for 2015 were gains of $23 million. The change in the instrument-specific credit risk of the FG VIEs' assets held as of December 31, 2014 that was recorded in the consolidated statements of operations for 2014 were gains of $171 million. To calculate the instrument specific credit risk, the changes in the fair value of the FG VIE assets are allocated between those changes that are due to the instrument specific credit risk and those are due to other factors, including interest rates. The instrument specific credit risk amount is determined by using expected contractual cash flows versus current expected cash flows discounted at original contractual rate. The net present value is calculated by discounting the expected cash flows of the underlying security, excluding the Company's financial guaranty insurance, at the relevant effective interest rate.

The unpaid principal for FG VIE liabilities with recourse was $802 million and $1,132 million as of December 31, 2015 and December 31, 2014, respectively. FG VIE liabilities with recourse will mature at various dates ranging from 2025 to 2038. The aggregate unpaid principal balance of the FG VIE liabilities with and without recourse was approximately $285 million greater than the aggregate fair value of the FG VIEs' liabilities as of December 31, 2015. The aggregate unpaid principal balance was approximately $548 million greater than the aggregate fair value of the FG VIEs' liabilities as of December 31, 2014.

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

Consolidated FG VIEs
By Type of Collateral

	As of December 31, 2015		As of December 31, 2014	
	Assets	Liabilities	Assets	Liabilities
	(in millions)			
With recourse:				
U.S. RMBS first lien	$ 449	$ 494	$ 498	$ 570
U.S. RMBS second lien	159	219	193	260
Total with recourse	608	713	691	830
Without recourse	127	121	132	114
Total	$ 735	$ 834	$ 823	$ 944

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

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

	Year Ended December 31,	
	2015	2014
	(in millions)	
Net earned premiums	$ (19)	$ (31)
Net investment income	(18)	(9)
Net realized investment gains (losses)	2	(5)
Fair value gains (losses) on FG VIEs	32	234
Other income (loss)	0	(2)
Loss and LAE	27	31
Effect on net income before tax	24	218
Less: tax provision (benefit)	8	77
Effect on net income (loss)	$ 16	$ 141
Effect on cash flows from operating activities	$ 44	$ 62

	As of December 31, 2015	As of December 31, 2014
	(in millions)	
Effect on shareholders' equity (decrease) increase	$ (9)	$ (25)

In 2015, the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of $32 million which was primarily driven by price appreciation on the Company's FG VIE assets during the year that resulted from improvements in the underlying collateral, as well as large principal paydowns made on the Company's FG VIEs.

In 2014, the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of $234 million. The primary driver of this gain, $102 million, was a result of the deconsolidation of five VIEs. In addition, there was a gain of $37 million resulting from the Company exercising its option to accelerate two second lien RMBS bonds. The remainder of the gain for the period was driven by the price appreciation on the Company's FG VIE assets during the year resulting from improvements in the underlying collateral, as well as large principal paydowns made on the Company's FG VIEs.

Non-Consolidated VIEs

As of December 31, 2015 and December 31, 2014 the Company had financial guaranty contracts outstanding for approximately 360 and 430 VIEs, respectively, that it did not consolidate. To date, the Company's analyses have indicated that it does not have a controlling financial interest in any other VIEs and, as a result, they are not consolidated in the consolidated financial statements. The Company's exposure provided through its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 3, Outstanding Exposure.

9. Investments and Cash

Accounting Policy

The vast majority of the Company's investment portfolio is composed of fixed-maturity and short-term investments, classified as available-for-sale at the time of purchase (approximately 94.6% based on fair value as of December 31, 2015), and therefore carried at fair value. Changes in fair value for other-than-temporarily-impaired ("OTTI") securities are bifurcated between credit losses and non-credit changes in fair value. The credit loss on OTTI securities is recorded in the statement of operations and the non-credit component of the change in fair value of securities, whether OTTI or not, is recorded in other comprehensive income ("OCI"). For securities 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, declines in fair value are 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 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.

Loss mitigation securities are generally purchased at a discount and are accounted for based on their underlying investment type and exclude the effects of the Company’s insurance. Interest income on loss mitigation securities is recognized on a level yield basis over the life of the security.

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.

Other invested assets primarily include:

- a surplus note issued by AGC to AGM (see Note 14, Related Party Transactions). The surplus note is being held to maturity,

- preferred stocks, which are carried at fair value with changes in unrealized gains and losses recorded in OCI.

Cash consists of cash on hand and demand deposits. As a result of the lag in reporting FG VIEs, cash and short-term investments do not reflect cash outflow to the holders of the debt issued by the FG VIEs for claim payments made by the Company to the consolidated FG VIEs until the subsequent reporting period.

Assessment for Other-Than-Temporary Impairments

The amount of other-than-temporary-impairment recognized in earnings depends on whether (1) an entity intends to sell the security or (2) it is more-likely-than-not that the entity will be required to sell the security before recovery of its amortized cost basis.

If an entity does not intend to sell the security and it is not more-likely-than-not that the Company will be required to sell the security before recovery of its amortized cost basis, the other-than-temporary-impairment is separated into (1) the amount representing the credit loss and (2) the amount related to all other factors.

The Company has a formal review process to determine other-than-temporary-impairment 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;
- the impact of foreign exchange rates; 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 other-than-temporary impairment 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 including default rates, recoveries and changes in value. The assumptions used in these projections require the use of significant management judgment.

The Company's assessment of a decline in value included management's current assessment of the factors noted above. The Company also seeks advice from its outside investment managers. If that assessment changes in the future, the Company may ultimately record a loss after having originally concluded that the decline in value was temporary.

Net Investment Income and Realized Gains (Losses)

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. Accrued investment income, which is recorded in Other Assets, was $62 million and $63 million as of December 31, 2015 and December 31, 2014, respectively.

Net Investment Income

	Year Ended December 31,	
	2015	2014
	(in millions)	
Income from fixed-maturity securities managed by third parties	$ 190	$ 185
Income from internally managed securities:		
Fixed maturities	46	58
Other	51	29
Gross investment income	287	272
Investment expenses	(5)	(5)
Net investment income	$ 282	$ 267

Net Realized Investment Gains (Losses)

	Year Ended December 31,	
	2015	2014
	(in millions)	
Gross realized gains on available-for-sale securities	$ 16	$ 7
Gross realized gains on other assets in investment portfolio	1	7
Gross realized losses on available-for-sale securities	(3)	(1)
Gross realized losses on other assets in investment portfolio	(10)	(2)
Other-than-temporary impairment	(31)	(70)
Net realized investment gains (losses)	$ (27)	$ (59)

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

Roll Forward of Credit Losses in the Investment Portfolio

	Year Ended December 31,	
	2015	2014
	(in millions)	
Balance, beginning of period	$ 104	$ 34
Reductions for securities sold during the period	(17)	—
Additions for credit losses on securities for which an other-than-temporary-impairment was not previously recognized	3	63
Additions for credit losses on securities for which an other-than-temporary-impairment was previously recognized	7	6
Other	—	1
Balance, end of period	$ 97	$ 104

Investment Portfolio

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

Investment Category	Percent of Total (1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI (2) Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Rating (3)
	(dollars in millions)						
Fixed-maturity securities:							
Obligations of state and political subdivisions	62%	$ 3,820	$ 222	$ (1)	$ 4,041	$ 1	AA
U.S. government and agencies	1	47	4	0	51	—	AA+
Corporate securities	11	675	11	(18)	668	(13)	BBB+
Mortgage-backed securities(4):							
RMBS	9	538	11	(17)	532	(7)	BBB-
CMBS	3	219	4	0	223	—	AAA
Asset-backed securities	7	410	1	(17)	394	(16)	AA-
Foreign government securities	3	192	0	(11)	181	—	AA+
Total fixed-maturity securities	96	5,901	253	(64)	6,090	(35)	AA-
Short-term investments	4	257	0	—	257	—	A+
Total investment portfolio	100%	$ 6,158	$ 253	$ (64)	$ 6,347	$ (35)	AA-

Fixed-Maturity Securities and Short-Term Investments
by Security Type
As of December 31, 2014

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Rating (3)
				(dollars in millions)			
Fixed-maturity securities:							
Obligations of state and political subdivisions	63%	$ 3,928	$ 261	$ 0	$ 4,189	$ 1	AA
U.S. government and agencies	1	64	5	0	69	—	AA+
Corporate securities	10	632	15	(4)	643	(2)	A-
Mortgage-backed securities(4):							
RMBS	10	656	24	(19)	661	(3)	BIG
CMBS	4	258	8	0	266	—	AAA
Asset-backed securities	3	191	2	0	193	1	A
Foreign government securities	3	191	3	(3)	191	—	AA+
Total fixed-maturity securities	94	5,920	318	(26)	6,212	(3)	AA-
Short-term investments	6	377	0	0	377	—	AAA
Total investment portfolio	100%	$ 6,297	$ 318	$ (26)	$ 6,589	$ (3)	AA-

(1) Based on amortized cost.

(2) Accumulated OCI ("AOCI"). See also Note 18, Other Comprehensive Income.

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

(4) Government-agency obligations were approximately 29% of mortgage backed securities as of December 31, 2015 and 24% as of December 31, 2014 based on fair value.

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

The 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, 2015 and December 31, 2014 by state.

Fair Value of Available-for-Sale Portfolio of Obligations of State and Political Subdivisions As of December 31, 2015 (1)

State	State General Obligation	Local General Obligation	Revenue Bonds	Fair Value	Amortized Cost	Average Credit Rating
			(in millions)			
Fixed-maturity securities:						
New York	$ 13	$ 21	$ 356	$ 390	$ 370	AA
California	36	50	255	341	311	AA-
Texas	4	119	202	325	307	AA
Florida	6	—	218	224	209	AA-
Washington	27	39	146	212	202	AA
Massachusetts	44	—	110	154	142	AA
Illinois	4	44	100	148	139	A+
Arizona	—	7	123	130	123	AA
Pennsylvania	37	26	37	100	95	A
Georgia	1	7	89	97	91	A+
All others	104	116	821	1,041	987	AA-
Subtotal	276	429	2,457	3,162	2,976	AA-
Short-term investments (2)	—	—	60	60	60	CC
Total	$ 276	$ 429	$ 2,517	$ 3,222	$ 3,036	AA-

Fair Value of Available-for-Sale Portfolio of
Obligations of State and Political Subdivisions
As of December 31, 2014 (1)

State	State General Obligation	Local General Obligation	Revenue Bonds	Fair Value	Amortized Cost	Average Credit Rating
			(in millions)			
Fixed-maturity securities:						
New York	$ 14	$ 18	$ 407	$ 439	$ 416	AA
Texas	26	174	206	406	383	AA
California	36	46	267	349	318	AA-
Florida	39	21	223	283	260	AA-
Illinois	4	61	133	198	183	A+
Washington	31	27	120	178	167	AA
Massachusetts	44	—	124	168	155	AA
Arizona	—	7	134	141	132	AA
Michigan	—	—	105	105	96	A+
Ohio	6	23	65	94	88	AA
All others	186	184	770	1,140	1,077	AA-
Total	$ 386	$ 561	$ 2,554	$ 3,501	$ 3,275	AA-

(1) Excludes $879 million and $688 million as of December 31, 2015 and 2014, 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.

(2) Matured in the first quarter of 2016.

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

Revenue Bonds
Sources of Funds

Type	As of December 31, 2015 Fair Value	As of December 31, 2015 Amortized Cost	As of December 31, 2014 Fair Value	As of December 31, 2014 Amortized Cost
		(in millions)		
Fixed-maturity securities:				
Transportation	$ 614	$ 573	$ 643	$ 593
Tax backed	416	394	397	374
Water and sewer	388	365	365	343
Higher education	362	342	372	350
Municipal utilities	325	309	388	363
Healthcare	259	239	272	245
All others	93	89	117	111
Subtotal	2,457	2,311	2,554	2,379
Short-term investments (1)	60	60	—	—
Total	$ 2,517	$ 2,371	$ 2,554	$ 2,379

(1) Matured in the first quarter of 2016.

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

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

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2015

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
			(dollars in millions)			
Obligations of state and political subdivisions	$ 90	$ (1)	$ 3	$ 0	$ 93	$ (1)
U.S. government and agencies	3	0	—	—	3	0
Corporate securities	153	(4)	90	(14)	243	(18)
Mortgage-backed securities:						
RMBS	150	(3)	74	(14)	224	(17)
CMBS	49	0	—	—	49	0
Asset-backed securities	269	(17)	—	—	269	(17)
Foreign government securities	92	(4)	82	(7)	174	(11)
Total	$ 806	$ (29)	$ 249	$ (35)	$ 1,055	$ (64)
Number of securities (1)		116		32		139
Number of securities with other-than-temporary impairment		6		4		10

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2014

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
			(dollars in millions)			
Obligations of state and political subdivisions	$ 61	$ 0	$ 7	$ 0	$ 68	$ 0
U.S. government and agencies	2	0	12	0	14	0
Corporate securities	151	(3)	48	(1)	199	(4)
Mortgage-backed securities:						
RMBS	172	(3)	85	(16)	257	(19)
CMBS	22	0	—	—	22	0
Asset-backed securities	24	0	—	—	24	0
Foreign government securities	108	(3)	—	—	108	(3)
Total	$ 540	$ (9)	$ 152	$ (17)	$ 692	$ (26)
Number of securities		79		34		113
Number of securities with other-than-temporary impairment		3		5		8

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

Of the securities in an unrealized loss position for 12 months or more as of December 31, 2015, nine securities had unrealized losses greater than 10% of book value. The total unrealized loss for these securities as of December 31, 2015 was $26 million. The Company has determined that the unrealized losses recorded as of December 31, 2015 are yield related and not the result of other-than-temporary-impairment.

The amortized cost and estimated fair value of available-for-sale fixed-maturity securities by contractual maturity as of December 31, 2015 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, 2015

	Amortized Cost	Estimated Fair Value
	(in millions)	
Due within one year	$ 91	$ 89
Due after one year through five years	960	978
Due after five years through 10 years	1,320	1,380
Due after 10 years	2,773	2,888
Mortgage-backed securities:		
RMBS	538	532
CMBS	219	223
Total	$ 5,901	$ 6,090

The investment portfolio contains securities and cash that are either held in trust for the benefit of third party reinsurers in accordance with statutory requirements, placed on deposit to fulfill state licensing requirements, or otherwise restricted in the amount of $33 million and $50 million as of December 31, 2015 and December 31, 2014, respectively, based on fair value. In addition, the total collateral required to be funded into a reinsurance trust account by AGM for the benefit of AGE as of December 31, 2015 and December 31, 2014 was approximately $244 million and $238 million, respectively, based on fair value.

No material investments of the Company were non-income producing for years ended December 31, 2015 and 2014, respectively.

Internally Managed Portfolio

The investment portfolio tables shown above include both assets managed externally and internally. In the table below, more detailed information is provided for the component of the total investment portfolio that is internally managed (excluding short-term investments and surplus note from affiliate). The internally managed portfolio, as defined below, represents approximately 14% and 11% of the investment portfolio, on a fair value basis as of December 31, 2015 and December 31, 2014, respectively. The internally managed portfolio consists primarily of the Company's investments in securities for (i) loss mitigation purposes, (ii) other risk management purposes and (iii) where the Company believes a particular security presents an attractive investment opportunity.

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

Internally Managed Portfolio
Carrying Value

	As of December 31, 2015	As of December 31, 2014
	(in millions)	
Assets purchased for loss mitigation and other risk management purposes:		
Fixed maturity securities, at fair value	$ 870	$ 634
Other invested assets	15	28
Other	45	79
Total	$ 930	$ 741

10. Investment in MAC Holdings

On July 16, 2013, subsidiaries of Assured Guaranty Ltd. completed a series of transactions that increased the capitalization of its subsidiary, MAC, to $800 million on a statutory basis. The Company does not currently anticipate that MAC will distribute any dividends.

AGM and its subsidiaries Assured Guaranty Municipal Insurance Company ("AGMIC") and Assured Guaranty (Bermuda) Ltd. ("AGBM") terminated the reinsurance pooling agreement pursuant to which AGMIC and AGBM had assumed a quota share percentage of the financial guaranty insurance policies issued by AGM, and AGM reassumed such ceded business. Subsequently, AGMIC was merged into AGM, with AGM as the surviving company.

AGBM, which had made a loan of $82.5 million to Assured Guaranty US Holdings Inc. ("AGUS"), an indirect parent holding company of AGM, received all of the outstanding shares of MAC held by AGUS and cash, in full satisfaction of the principal of and interest on such loan. After AGBM distributed substantially all of its assets, including the MAC shares, to AGM as a dividend, AGM sold AGBM to its affiliate Assured Guaranty Re Ltd. (“AG Re”). Subsequently, AGBM and AG Re merged, with AG Re as the surviving company. The sale of AGBM to, and subsequent merger with, AG Re were each effective as of July 17, 2013.

MAC Holdings, was formed to own 100% of the outstanding stock of MAC. AGM and its affiliate AGC subscribed for approximately 61% and 39% of the outstanding MAC Holdings common stock, respectively, for which AGM paid $425 million and AGM's affiliate AGC paid $275 million, as consideration. The consideration consisted of all of MAC's outstanding common stock (in the case of AGM), cash and marketable securities.

MAC Holdings then contributed cash and marketable securities having a fair market value sufficient to increase MAC's policyholders' surplus to approximately $400 million, and purchased a surplus note issued by MAC in the principal amount of $300 million. In addition, AGM purchased a surplus note issued by MAC in the principal amount of $100 million.

Following the increase in MAC's capitalization, AGM ceded par exposure of approximately $87 billion and unearned premiums of approximately $468 million to MAC, and AGC ceded par exposure of approximately $24 billion and unearned premiums of approximately $249 million to MAC.

11. Insurance Company Regulatory Requirements

The Company's ability to pay dividends depends, among other things, upon their 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 their state of domicile and other states. Financial statements prepared in accordance with accounting practices prescribed or permitted by local insurance regulatory authorities differ in certain respects from GAAP.

The Company's U.S. domiciled insurance companies prepare statutory financial statements in accordance with accounting practices prescribed or permitted by the National Association of Insurance Commissioners ("NAIC") and their respective insurance departments. Prescribed statutory accounting practices are set forth in the NAIC Accounting Practices and Procedures Manual. The Company has no permitted accounting practices on a statutory basis.

GAAP differs in certain significant respects from U.S. insurance companies' statutory accounting practices prescribed or permitted by insurance regulatory authorities. The principal differences result from the following statutory accounting practices:

- upfront premiums are earned when related principal and interest have expired rather than earned over the expected period of coverage;
- acquisition costs are charged to expense as incurred rather than over the period that related premiums are earned;
- a contingency reserve is computed based on statutory requirements, whereas no such reserve is required under GAAP;
- certain assets designated as "non-admitted assets" are charged directly to statutory surplus, rather than reflected as assets under GAAP;
- investments in subsidiaries are carried on the balance sheet on the equity basis, to the extent admissible, rather than consolidated with the parent;
- the amount of deferred tax assets that may be admitted is subject to an adjusted surplus threshold and is generally limited to the lesser of those assets the Company expects to realize within three years of the balance sheet date or fifteen percent of the Company's adjusted surplus. This realization period and surplus percentage is subject to change based on the amount of adjusted surplus. Under GAAP there is no non-admitted asset determination, rather a valuation allowance is recorded to reduce the deferred tax asset to an amount that is more likely than not to be realized;
- insured credit derivatives are accounted for as insurance contracts rather than as derivative contracts measured at fair value;
- bonds are generally carried at amortized cost rather than fair value;
- VIEs and refinancing vehicles are not consolidated;

- payment of principal and interest on surplus notes is recorded only upon approval of the insurance regulator rather than periodic accrual of interest;
- push-down acquisition accounting is not applicable under statutory accounting practices, as it is under GAAP;
- expected losses are discounted at a rate of 5%, recorded when the loss is deemed probable and without consideration of the deferred premium revenue rather than discounted at the risk free rate at the end of each reporting period and only to the extent they exceed deferred premium revenue;
- the present value of installment premiums and commissions are not recorded on the balance sheet as they are under GAAP.

Insurance Regulatory Amounts Reported

	Policyholders' Surplus		Net Income (Loss)	
	As of December 31,		Year Ended December 31,	
	2015	2014	2015	2014
	(in millions)			
AGM(1)	$ 2,441	$ 2,267	$ 217	$ 304
MAC	730	612	102	75

____

(1) Policyholders' surplus of AGM includes its indirect share of MAC. AGM owns approximately 61% of the outstanding stock of MAC Holdings, which owns 100% of the outstanding common stock of MAC.

Contingency Reserves

On July 15, 2013, AGM and its wholly-owned subsidiary AGE (together, the "AGM Group"), were notified that the New York State Department of Financial Services ("NYDFS") does not object to the AGM Group reassuming all of the outstanding contingency reserves that the AGM Group had ceded to AG Re and electing to cease ceding future contingency reserves to AG Re. The insurance regulator permitted the AGM Group to reassume the contingency reserves in increments over three years. In the third quarter of 2015, the AGM Group reassumed its final installment and as of December 31, 2015, the AGM Group had collectively reassumed an aggregate of approximately $255 million.

From time to time, AGM has obtained the approval of its regulator to release contingency reserves based on losses or because the accumulated reserve is deemed excessive in relation to the insurer's outstanding insured obligations. In 2015, on the latter basis, AGM obtained the NYDFS's approval for a contingency reserve release of approximately $253 million. In addition, MAC also released approximately $56 million of contingency reserves, which consisted of the assumed contingency reserves maintained by MAC, as reinsurer of AGM, in respect of the same obligations that were the subject of AGM's $253 million release.

With respect to the regular, quarterly contributions to contingency reserves required by New York laws and regulations, such laws and regulations permit the discontinuation of such quarterly contributions to a company’s contingency reserves when such company’s aggregate contingency reserves for a particular line of business (i.e., municipal or non-municipal) exceed the sum of the company’s outstanding principal for each specified category of obligations within the particular line of business multiplied by the specified contingency reserve factor for each such category. In accordance with such laws and regulations, and with the approval of the NYDFS, AGM ceased making quarterly contributions to its contingency reserves for non-municipal business, beginning in the fourth quarter of 2014. Such cessations are expected to continue for as long as AGM satisfies the foregoing condition for its applicable line of business.

Dividend Restrictions and Capital Requirements

Under New York insurance law, AGM may only pay dividends out of "earned surplus," which is the portion of the company's surplus that represents the net earnings, gains or profits (after deduction of all losses) that have not been distributed to shareholders as dividends or transferred to stated capital or capital surplus, or applied to other purposes permitted by law, but does not include unrealized appreciation of assets. AGM may pay dividends without the prior approval of the New York Superintendent of Financial Services ("New York Superintendent") that, together with all dividends declared or distributed by it during the preceding 12 months, does not exceed the lesser of 10% of its policyholders' surplus (as of its last annual or quarterly statement filed with the New York Superintendent) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGM to distribute as dividends without regulatory approval, is estimated to be approximately $244 million, of which approximately $95 million is estimated to be available for distribution in the first quarter of 2016.

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

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

Dividends and Surplus Note
By Insurance Company

	Year Ended December 31,	
	2015	2014
	(in millions)	
Dividends paid by AGM to AGMH	$ 215	$ 160
Repayment of surplus note by AGM to AGMH	25	50

12. 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.

Non-interest-bearing tax and loss bonds are purchased in the amount of the tax benefit that results from deducting contingency reserves as provided under Internal Revenue Code Section 832(e). The Company records the purchase of tax and loss bonds in deferred taxes.

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

Overview

The Company files its US federal tax return as a part of the consolidated group for AGUS, an indirect parent holding company. Each member of the AGUS consolidated tax group is part of a tax sharing agreement and pays or receives its proportionate share of the consolidated regular federal tax liability for the group as if each company filed on a separate return basis.

Provision for Income Taxes

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

Effective Tax Rate Reconciliation

	Year Ended December 31,	
	2015	2014
	(in millions)	
Expected tax provision (benefit) at statutory rate	$ 229	$ 270
Tax-exempt interest	(41)	(44)
Change in liability for uncertain tax position	8	6
Other	(10)	(3)
Total provision (benefit) for income taxes	$ 186	$ 229
Effective tax rate	28.4%	29.6%

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

Components of Net Deferred Tax Assets

	As of December 31,	
	2015	2014
	(in millions)	
Deferred tax assets:		
Unrealized losses on credit derivative financial instruments, net	$ 28	$ 79
Unearned premium reserves, net	122	86
Loss and LAE reserve	—	47
Tax and loss bonds	39	39
Deferred ceding commission income	25	31
FG VIEs	29	9
Deferred compensation	12	15
Investment basis difference	51	66
Other	14	9
Total deferred income tax assets	320	381
Deferred tax liabilities:		
Contingency reserves	64	64
Loss and LAE reserve	50	—
Unrealized appreciation on committed capital securities	10	16
Unrealized appreciation on investments	66	106
Market discount	21	23
Other	6	11
Total deferred income tax liabilities	217	220
Net deferred income tax asset	$ 103	$ 161

Valuation Allowance

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

Audits

AGUS has open tax years with the U.S. Internal Revenue Service ("IRS") for 2009 forward and is currently under audit for the 2009 - 2012 tax years. The Company's U.K. subsidiary, AGE, is not currently under examination and has open tax years of 2014 forward.

Uncertain Tax Positions

The following table provides a reconciliation of the beginning and ending balances of the total liability for unrecognized tax benefits. The Company does not believe it is reasonably possible that this amount will change significantly in the next twelve months.

	2015	2014
	(in millions)	
Balance as of January 1,	$ 11	$ 5
True-up from tax return filings	7	6
Balance as of December 31,	$ 18	$ 11

The Company's policy is to recognize interest and penalties related to uncertain tax positions in income tax expense and has accrued $0.5 million for 2015 and $0.5 million for 2014. As of December 31, 2015 and December 31, 2014, the Company has accrued $2.8 million and $2.3 million of interest, respectively.

The total amount of unrecognized tax benefits as of December 31, 2015 would affect the effective tax rate, if recognized.

Tax Treatment of CDS

The Company treats the guaranty it provides on CDS as an insurance contract for tax purposes and as such a taxable loss does not occur until the Company expects to make a loss payment to the buyer of credit protection based upon the occurrence of one or more specified credit events with respect to the contractually referenced obligation or entity. The Company holds its CDS to maturity, at which time any unrealized fair value loss in excess of credit-related losses would revert to zero. The tax treatment of CDS is an unsettled area of the law. The uncertainty relates to the IRS determination of the income or potential loss associated with CDS as either subject to capital gain (loss) or ordinary income (loss) treatment. In treating CDS as insurance contracts the Company treats both the receipt of premium and payment of losses as ordinary income and believes it is more likely than not that any CDS credit related losses will be treated as ordinary by the IRS. To the extent the IRS takes the view that the losses are capital losses in the future and the Company incurred actual losses associated with the CDS, the Company would need sufficient taxable income of the same character within the carryback and carryforward period available under the tax law.

13. Reinsurance and Other Monoline Exposures

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

Accounting Policy

For business assumed and ceded, the accounting model of the underlying direct financial guaranty contract dictates the accounting model used for the reinsurance contract (except for those eliminated as FG VIEs). For any assumed or ceded financial guaranty insurance premiums and financial guaranty insurance losses, the accounting models described in Note 5 are followed. For any ceded credit derivative contracts, the accounting model in Note 7 is followed.

Ceded and Assumed Business

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

AGM is also party to reinsurance agreements as a reinsurer to its affiliated financial guaranty insurance companies. In 2013, MAC assumed a book of U.S. public finance business from AGM and AGC.

The Company has assumed business primarily from its affiliate, AGC. Under this relationship, the Company assumes a portion of the ceding company's insured risk in exchange for a premium. The Company may be exposed to risk in this portfolio in that the Company may be required to pay losses without a corresponding premium in circumstances where the ceding company is experiencing financial distress and is unable to pay premiums. The Company's agreement with AGC is generally subject to termination at the option of the ceding company if the Company fails to meet certain financial and regulatory criteria or to maintain a specified minimum financial strength rating. Upon termination under these conditions, the Company may be required to return to the ceding company unearned premiums and loss reserves calculated on a statutory basis of accounting, attributable to the reinsurance assumed, after which the Company would be released from liability with respect to the Assumed Business. Upon the occurrence of the conditions set forth above, whether or not an agreement is terminated, the Company may be obligated to increase the level of ceding commission paid.

Over the past several years, the Company has entered into several commutations in order to reassume previously ceded books of business from its reinsurers.

Net Effect of Commutations of Ceded Reinsurance Contracts

	Year Ended December 31,	
	2015	2014
	(in millions)	
Increase (decrease) in net unearned premium reserve	$ 23	$ 20
Increase (decrease) in net par outstanding	855	1,091
Commutation gains recorded in other income	28	23

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

Effect of Reinsurance on Statement of Operations

	Year Ended December 31,	
	2015	2014
	(in millions)	
Premiums Written:		
Direct	$ 146	$ 89
Assumed	16	0
Ceded	(47)	(31)
Net	$ 115	$ 58
Premiums Earned:		
Direct	$ 521	$ 476
Assumed	37	26
Ceded	(154)	(128)
Net	$ 404	$ 374
Loss and LAE:		
Direct	$ 157	$ 48
Ceded	(47)	(73)
Net	$ 110	$ (25)

Other Monoline Exposures

In addition to assumed and ceded reinsurance arrangements, the Company may also have exposure to some financial guaranty reinsurers (i.e., monolines) in other areas. Second-to-pay insured par outstanding represents transactions the Company has insured that were previously insured by other monolines. The Company underwrites such transactions based on the underlying insured obligation without regard to the primary insurer. Another area of exposure is in the investment portfolio where the Company holds fixed-maturity securities that are wrapped by monolines and whose value may change based on the rating of the monoline. As of December 31, 2015, based on fair value, the Company had fixed-maturity securities in its investment portfolio consisting of $164 million insured by National Public Finance Guarantee Corporation ("National"), $141 million insured by Ambac, $68 million insured by AGC, $260 million insured by the Company's affiliate Assured Guaranty (UK) Ltd., and $8 million insured by other guarantors. In addition, the Company acquired bonds for loss mitigation or other risk management purposes in the amount of $123 million insured by FGIC UK Limited.

In accordance with U.S. statutory accounting requirements and U.S. insurance laws and regulations, in order for the Company to receive credit for liabilities ceded to reinsurers domiciled outside of the U.S., such reinsurers must secure their liabilities to the Company. All of the unauthorized reinsurers in the tables below are required to post collateral for the benefit of the Company in an amount at least equal to the sum of their ceded unearned premium reserve, loss reserves and contingency reserves all calculated on a statutory basis of accounting. In addition, certain authorized reinsurers in the tables below post collateral on terms negotiated with the Company.

Exposure by Reinsurer

Reinsurer	Ratings at March 28, 2016		Par Outstanding (1) As of December 31, 2015		
	Moody's Reinsurer Rating	S&P Reinsurer Rating	Ceded Par Outstanding	Second-to-Pay Insured Par Outstanding	Assumed Par Outstanding
			(dollars in millions)		
Affiliated Companies: (3)					
AGC (2)	A3	AA	$ 3,349	$ 163	$ 19,836
AG Re (2)	WR (4)	AA	56,985	—	—
Affiliated Companies			60,334	163	19,836
Non-Affiliated Companies:					
American Overseas Reinsurance Company Limited (f/k/a Ram Re) (2)	WR	WR	4,320	—	30
Tokio Marine & Nichido Fire Insurance Co., Ltd. ("Tokio") (2)	Aa3 (5)	A+ (5)	4,219	—	—
Syncora Guarantee Inc. (2)	WR	WR	2,450	545	567
Mitsui Sumitomo Insurance Co. Ltd.(2)	A1	A+ (5)	1,819	—	—
ACA Financial Guaranty Corp.	NR (6)	WR	714	1	—
National (7)	A3	AA-	—	3,634	—
Ambac	WR	WR	—	2,126	—
MBIA	(8)	(8)	—	1,241	—
FGIC	(9)	(9)	—	798	—
Ambac Assurance Corp. Segregated Account	NR	NR	—	88	—
CIFG Assurance North America Inc.	WR	WR	—	21	—
Other	Various	Various	24	—	1
Non-Affiliated Companies			13,546	8,454	598
Total			$ 73,880	$ 8,617	$ 20,434

(1) Includes par related to insured credit derivatives.

(2) The total collateral posted by all affiliated and non-affiliated reinsurers required or agreeing to post collateral as of December 31, 2015, is approximately $1.2 billion. The collateral excludes amounts for the benefit of AGE, See Note 14.

(3) MAC is rated AA+ (stable outlook) from KBRA and of AA (stable outlook) from S&P. Assumed par outstanding includes $19,807 million assumed by MAC from AGC.

(4) Represents "Withdrawn Rating."

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

(6) Represents "Not Rated."

(7) National is rated AA+ by KBRA.

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

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

Ceded Par Outstanding by Reinsurer and Credit Rating
As of December 31, 2015

Reinsurer	Internal Credit Rating AAA	AA	A	BBB	BIG	Total
	(in millions)					
Affiliated Companies	$ 936	$ 11,620	$ 29,504	$ 16,762	$ 1,512	$ 60,334
American Overseas Reinsurance Company Limited (f/k/a Ram Re)	235	1,514	1,328	992	251	4,320
Tokio	565	532	1,131	1,364	627	4,219
Syncora Guarantee Inc.	—	132	429	1,766	123	2,450
Mitsui Sumitomo Insurance Co. Ltd.	131	551	591	372	174	1,819
ACA Financial Guaranty Corp.	—	449	246	19	—	714
Other	—	—	0	24	—	24
Total	$ 1,867	$ 14,798	$ 33,229	$ 21,299	$ 2,687	$ 73,880

Second-to-Pay
Insured Par Outstanding by Internal Rating
As of December 31, 2015(1)

	Public Finance AAA	AA	A	BBB	BIG	Structured Finance AAA	AA	BBB	BIG	Total
	(in millions)									
Affiliated Companies	$ —	$ 97	$ —	$ —	$ —	$ —	$ 66	$ —	$ —	$ 163
Non-Affiliated Companies:										
Syncora Guarantee Inc.	—	38	75	273	159	—	—	—	—	545
ACA Financial Guaranty Corp.	—	—	—	1	—	—	—	—	—	1
National	30	1,221	2,383	—	—	—	—	—	—	3,634
Ambac	9	706	977	396	—	—	—	32	6	2,126
MBIA	—	47	240	48	—	—	745	66	95	1,241
FGIC	—	6	531	25	65	149	—	—	22	798
Ambac Assurance Corp. Segregated Account	—	—	—	—	—	—	23	—	65	88
CIFG Assurance North America Inc.	—	—	—	1	20	—	—	—	—	21
Non-Affiliated Companies	39	2,018	4,206	744	244	149	768	98	188	8,454
Total	$ 39	$ 2,115	$ 4,206	$ 744	$ 244	$ 149	$ 834	$ 98	$ 188	$ 8,617

(1) Assured Guaranty's internal rating.

Amounts Due (To) From Reinsurers
As of December 31, 2015

	Assumed Premium	Ceded Premium, net of Commissions	Ceded Expected Loss to be Paid
		(in millions)	
AGC	$ 2	$ (13)	$ 31
AG Re	—	(53)	79
American Overseas Reinsurance Company Limited (f/k/a Ram Re)	—	(5)	24
Tokio	—	(12)	43
Syncora Guarantee Inc.	14	(22)	5
Mitsui Sumitomo Insurance Co. Ltd.	—	(3)	17
Swiss Reinsurance Co.	—	(3)	—
Total	$ 16	$ (111)	$ 199

Excess of Loss Reinsurance Facility

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

14. Related Party Transactions

Guarantees or Contingencies for Related Parties

AGM currently provides support to its subsidiary AGE through a quota share and excess of loss reinsurance agreement (the "Reinsurance Agreement") and a net worth maintenance agreement (the "Net Worth Agreement"). Such agreements replace and supersede the second amended and restated quota share and stop loss reinsurance agreement and the second amended and restated net worth maintenance agreement, respectively, previously in place between the parties. For transactions closed prior to 2011, AGE typically guaranteed all of the guaranteed obligations directly and AGM reinsured under the quota share cover of the Reinsurance Agreement approximately 92% of AGE's retention after cessions to other reinsurers. In 2011, AGE and AGM implemented a co-guarantee structure pursuant to which (i) AGE directly guarantees a portion of the guaranteed obligations in an amount equal to what would have been AGE's pro rata retention percentage under the quota share cover, (ii) AGM directly guarantees the balance of the guaranteed obligations, and (iii) AGM also provides a second-to-pay guarantee for AGE's portion of the guaranteed obligations.

Under the excess of loss cover of the Reinsurance Agreement, AGM will pay AGE quarterly the amount by which (i) the sum of (a) AGE's incurred losses calculated in accordance with UK GAAP as reported by AGE in its financial returns filed with the Prudential Regulation Authority ("PRA") and (b) AGE's paid losses and LAE, in both cases net of all other performing reinsurance, including the reinsurance provided by AGM under the quota share cover of the Reinsurance Agreement, exceeds (ii) an amount equal to (a) AGE's capital resources under U.K. law minus (b) the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K. In addition, the Reinsurance Agreement permits AGE to terminate the Reinsurance Agreement upon the following events: a downgrade of AGM's ratings by Moody's below Aa3 or by S&P below AA- if the company fails to restore its rating(s) to the required level within a prescribed period of time; AGM's insolvency; failure by AGM to maintain the minimum capital required by its domiciliary jurisdiction; or AGM filing a petition in bankruptcy, going into liquidation or rehabilitation or having a receiver appointed. The Reinsurance Agreement also provides that no amounts are owing under the excess of loss cover (or the stop loss cover of the second amended and restated quota share and stop loss reinsurance agreement previously in place between the parties) with respect to any quarter ending prior to April 1, 2014.

The quota share and excess loss covers each exclude transactions guaranteed by AGE on or after July 1, 2009 that are not municipal, utility, project finance or infrastructure risks or similar types of risks.

The Reinsurance Agreement also contemplates the establishment of collateral by AGM to support its reinsurance obligations to AGE. In December 2014, to satisfy a new PRA requirement that AGM post collateral to support its reinsurance obligations to AGE, AGM and AGE amended the Reinsurance Agreement to incorporate the PRA's requirement. Pursuant to such amended Reinsurance Agreement, AGM's collateral requirement will be measured as of the end of each calendar quarter by (i) using the PRA's FG Benchmark Model to calculate at the 99.5% confidence interval the losses expected to be borne collectively by AGE's three affiliated reinsurers, AGM, AG Re and Assured Guaranty Re Overseas Ltd. ("AGRO"); (ii) deducting from such calculation AGE's capital resources under such model; and (iii) requiring AGM, AG Re and AGRO collectively to maintain collateral equal to fifty percent (50%) of such difference, i.e., the excess of AGM's, AG Re's and AGRO's assumed modeled losses over AGE's capital resources. As of January 1, 2016, the FG Benchmark Model is no longer applicable and the PRA has agreed to allow AGM's collateral requirement to be determined using AGE's internal capital requirement model under the same formula described above. This change is subject to approval by the NYDFS. In December 2014, AGM and AGE also entered into a related trust agreement pursuant to which AGM, prior to year-end, established, and deposited assets into, a reinsurance trust account for the benefit of AGE to satisfy the PRA's collateral requirement as of September 30, 2014, as measured in accordance with such amended Reinsurance Agreement. The total collateral required to be funded into such reinsurance trust account by AGM as of December 31, 2015 was approximately $244 million.

Pursuant to the Net Worth Agreement, AGM is obligated to cause AGE to maintain capital resources equal to 110% of the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K., provided that AGM's contributions (a) do not exceed 35% of its policyholders' surplus on an accumulated basis as determined by the laws of the State of New York, and (b) are in compliance with Section 1505 of the New York Insurance Law. AGM has never been required to make any contributions to AGE's capital under the current Net Worth Agreement or the prior net worth maintenance agreement.

Management, Service Contracts or Cost Sharing Arrangements

In 2010, the Company entered into a service agreement with various of its affiliates, including AGC, which agreement was amended and restated, effective as of April 1, 2015. Pursuant to such service agreement, AGC makes available to it certain equipment, insurance, reinsurance and such other services, including underwriting, actuarial, surveillance, marketing, claims handling, legal, information technologies, corporate secretarial, human resources, accounting, tax, financial reporting and investment planning services. In addition, under the agreement the Company makes available to AGC and the other affiliate parties the use of certain equipment and office space owned by the Company. Expenses are allocated directly where appropriate and, where not appropriate, based upon an allocation of employee time and corresponding office overhead. The agreement provides for quarterly settlements and an express right of offset with regard to amounts owing between parties under this Agreement and other agreements between such parties.

See Note 17, Employee Benefit Plans for expenses related to Long-Term Compensation Plans of AGL which are allocated to AGM.

The following table summarizes the allocated expenses from (to) affiliate companies under the expense sharing agreements.

Expenses Allocated From (To) Affiliated Companies

	Year Ended December 31,	
	2015	2014
	(in millions)	
Affiliated companies:		
AGC	$ 68	$ 79
Assured Guaranty Finance Overseas Ltd.	9	8
AGL	6	6
Assured Guaranty (UK) Services Limited	5	5
Total	$ 88	$ 98

The following table summarizes the amounts due (to) from affiliate companies under the expense sharing agreements.

Amounts Due (To) From Affiliated Companies

	As of December 31,	
	2015	2014
	(in millions)	
Affiliated companies:		
AGC	$ (36)	$ (47)
AGL	(5)	(4)
Assured Guaranty Finance Overseas Ltd.	(2)	(2)
Other	(3)	(4)
Total	$ (46)	$ (57)

Reinsurance Agreements

The Company cedes to and assumes business from affiliated entities under certain reinsurance agreements. See below for material balance sheet and statement of operations items related to insurance transactions.

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

	As of December 31,	
	2015	2014
	(in millions)	
Assets:		
Premium receivable		
AGC	$ 2	$ 2
Ceded unearned premium reserve (1)		
AG Re (1)	564	591
AGC	56	—
Reinsurance recoverable on unpaid losses		
AG Re	62	55
AGC	24	—
Reinsurance recoverable on paid losses (2)		
AG Re	0	1
AGC	0	—
Profit commission receivable (2)		
AG Re	0	1
Net credit derivative assets		
AG Re	18	24
AGC	0	—
Liabilities:		
Unearned premium reserve		
AGC	172	209
Ceded premium payable, net of ceding commission (3)		
AG Re	53	55
AGC	13	—
Ceded salvage and subrogation recoverable (3)		
AG Re	1	2
AGC	1	—
Ceded funds held (4)		
AG Re	35	30
AGC	25	—
Deferred ceding commissions (4)		
AG Re	113	111
AGC	1	—
Other liabilities		
AG Re	6	—
AGC	5	—
Other information:		
Exposure		
Assumed par outstanding		
AGC	19,836	22,018
Ceded par outstanding		
AG Re	56,985	58,891
AGC	3,349	—

(1) Includes $1 million and $3 million of ceded contra-paid on losses at December 31, 2015 and December 31, 2014, respectively.
(2) Included in other assets on the consolidated balance sheets.
(3) Included in reinsurance balances payable, net on the consolidated balance sheets.
(4) Included in other liabilities on the consolidated balance sheets.

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

	Year Ended December 31, 2015	Year Ended December 31, 2014
	(in millions)	
Revenues:		
Net earned premiums		
AG Re	$ (80)	$ (75)
AGC	25	26
Profit commission income		
AG Re	0	1
Realized gains and other settlements on credit derivatives		
AG Re	0	(1)
AGC	4	—
Net unrealized gains (losses) on credit derivatives		
AG Re	(5)	(7)
Expenses:		
Loss and loss adjustment expenses (recoveries)		
AG Re	(15)	(30)
AGC	(12)	—
Commissions incurred (earned)		
AG Re	(15)	(13)
AGC	0	—

Other Invested Assets

Surplus Note from AGC

On December 18, 2009, AGC issued a surplus note with a principal amount of $300 million to AGM. This note carries a simple interest rate of 5.0% per annum and matures on December 31, 2029. Principal is payable at the option of AGC prior to the final maturity of the note in 2029 and interest is payable on the note annually in arrears as of December 31 of each year, commencing December 31, 2010. Payments of principal and interest are subject to AGC having policyholders' surplus in excess of statutory minimum requirements after such payment and to prior written approval by the Maryland Insurance Administration. AGM recognized $15 million and $15 million of interest income in each of the years ended December 31, 2015 and 2014. AGM also received $15 million and $15 million of interest from AGC in each of the years ended December 31, 2015 and 2014. There was no principal paydown on the surplus note by AGC.

Capital Contributions from AGMH

In the third quarter of 2008, AGM issued a non-interest bearing surplus note with no term to AGMH in exchange for $300 million which, due to the terms of the agreement, is recorded as capital. Principal on the surplus note may be paid at any time at the option of the Company, subject to prior approval of the New York Superintendent and in compliance with the conditions to such payments as contained in the New York Insurance Laws. The Company repaid $25 million in principal on this surplus note in 2015 and $50 million in 2014. AGM fully repaid the surplus note in March 2015 after obtaining approval from the New York Department of Financial Services.

15. Commitments and Contingencies

Leases

AGM and AGE are party to various lease agreements accounted for as operating leases. The Company leases and occupies space in New York City through 2032. In addition, AGM and AGE lease additional office space in various locations under non-cancelable operating leases which expire at various dates through 2029. Total rent expense allocated to the Company for all premises was $4.7 million in 2015 and $4.6 million in 2014.

AGM entered into an operating lease effective January 1, 2016, for new office space comprising one full floor and one partial floor at 1633 Broadway in New York City. Assured Guaranty plans to move the principal place of business of AGM, AGC, MAC and AGL's other U.S. based subsidiaries from 31 West 52nd Street in New York City to this new location during the summer of 2016. The new lease is for approximately 88,000 square feet and runs until 2032, with an option, subject to certain conditions, to renew for five years at a fair market rent. The fixed annual rent, which commences after an initial rent holiday, begins at $6.2 million, rising in two steps to $7.3 million for the last five years of the initial term. In connection with the move and in return for rent abatement and certain other concessions, AGM agreed to terminate, eight months after its new space is delivered, its lease on its existing office space at 31 West 52nd Street, which had been scheduled to run until 2026.

Future Minimum Rental Payments

Year	(in millions)
2016	$ 3
2017	5
2018	7
2019	7
2020	7
Thereafter	76
Total	$ 105

Legal Proceedings

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

In addition, in the ordinary course of their respective businesses, certain of the Company's subsidiaries assert claims in legal proceedings against third parties to recover losses paid in prior periods or prevent losses in the future. For example, as described in the "Recovery Litigation" section of Note 4, Expected Loss to be Paid, in January 2016 the Company commenced an action for declaratory judgment and injunctive relief in the U.S. District Court for the District of Puerto Rico to invalidate executive orders issued by the Governor of Puerto Rico directing the retention or transfer of certain taxes and revenues pledged to secure the payment of certain bonds insured by the Company. The amounts, if any, the Company will recover in proceedings to recover losses are uncertain, and recoveries, or failure to obtain recoveries, in any one or more of these proceedings during any quarter or year could be material to the Company's results of operations in that particular quarter or year.

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, including matters discussed below. The Company reviews relevant information with respect to its litigation and regulatory matters on a quarterly, and annual basis and updates its accruals, disclosures and estimates of reasonably possible loss based on such reviews.

Litigation

Proceedings Relating to the Company's Financial Guaranty Business

AGM and AGMH receive subpoenas *duces tecum* and interrogatories from regulators from time to time.

On September 25, 2013, Wells Fargo Bank, N.A., as trust administrator of the MASTR Adjustable Rate Mortgages Trust 2007-3, filed an interpleader complaint in the U.S. District Court for the Southern District of New York against AGM, among others, relating to the right of AGM to be reimbursed from certain cashflows for principal claims paid in respect of

insured certificates. The Company estimates that an adverse outcome to the interpleader proceeding could increase losses on the transaction by approximately $10 - $20 million, net of expected settlement payments and reinsurance in force.

Proceedings Related to AGMH's Former Financial Products Business

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

Governmental Investigations into Former Financial Products Business

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

Lawsuits Relating to Former Financial Products Business

During 2008, nine putative class action lawsuits were filed in federal court alleging federal antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. These cases have been coordinated and consolidated for pretrial proceedings in the U.S. District Court for the Southern District of New York as *MDL 1950, In re Municipal Derivatives Antitrust Litigation,* Case No. 1:08-cv-2516 ("MDL 1950"). Five of these cases named both AGMH and AGM: (a) *Hinds County, Mississippi v. Wachovia Bank, N.A.*; (b) *Fairfax County, Virginia v. Wachovia Bank, N.A.*; (c) *Central Bucks School District, Pennsylvania v. Wachovia Bank, N.A.*; (d) *Mayor and City Council of Baltimore, Maryland v. Wachovia Bank, N.A.*; and (e) *Washington County, Tennessee v. Wachovia Bank, N.A.* In April 2009, the MDL 1950 court granted the defendants' motion to dismiss on the federal claims for these five cases, but granted leave for the plaintiffs to file an amended complaint. The Corrected Third Consolidated Amended Class Action Complaint, filed on October 9, 2013, lists neither AGM nor AGMH as a named defendant or a co-conspirator. The complaint generally seeks unspecified monetary damages, interest, attorneys' fees and other costs. The other four cases named AGMH (but not AGM) and also alleged that the defendants violated California state antitrust law and common law by engaging in illegal bid-rigging and market allocation, thereby depriving the cities or municipalities of competition in the awarding of GICs and ultimately resulting in the cities paying higher fees for these products: (f) *City of Oakland, California v. AIG Financial Products Corp.*; (g) *County of Alameda, California v. AIG Financial Products Corp.*; (h) *City of Fresno, California v. AIG Financial Products Corp.*; and (i) *Fresno County Financing Authority v. AIG Financial Products Corp*. When the four plaintiffs filed a consolidated complaint in September 2009, the plaintiffs did not name AGMH as a defendant. However, the complaint does describe some of AGMH's and AGM's activities. The consolidated complaint generally seeks unspecified monetary damages, interest, attorneys' fees and other costs. In April 2010, the MDL 1950 court granted in part and denied in part the named defendants' motions to dismiss this consolidated complaint. On September 22, 2015, the remaining parties to the putative class action reported to the MDL 1950 Court that settlements in principle had been reached and a motion for preliminary approval of those putative class claims was filed on February 24, 2016. The parties have reported that final settlement with those remaining defendants would resolve the putative class case. The settlement fairness hearing for those putative class cases is scheduled for July 8, 2016. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from these lawsuits.

In 2008, AGMH and AGM also were named in five non-class action lawsuits originally filed in the California Superior Courts alleging violations of California law related to the municipal derivatives industry: (a) *City of Los Angeles, California v. Bank of America, N.A.*; (b) *City of Stockton, California v. Bank of America, N.A.*; (c) *County of San Diego, California v. Bank of America, N.A.*; (d) *County of San Mateo, California v. Bank of America, N.A.*; and (e) *County of Contra Costa, California v. Bank of America, N.A.* Amended complaints in these actions were filed in September 2009, adding a federal antitrust claim and naming AGM (but not AGMH) and AGUS, among other defendants. These cases have been transferred to the Southern District

of New York and consolidated with MDL 1950 for pretrial proceedings. In late 2009, AGM and AGUS, among other defendants, were named in six additional non-class action cases filed in federal court, which also have been coordinated and consolidated for pretrial proceedings with MDL 1950; one was voluntarily dismissed with prejudice in October 2010, leaving five that are currently pending: (f) *City of Riverside, California v. Bank of America, N.A.*; (g) *Los Angeles World Airports v. Bank of America, N.A.*; (h) *Redevelopment Agency of the City of Stockton v. Bank of America, N.A.*; (i) *Sacramento Suburban Water District v. Bank of America, N.A.*; and (j) *County of Tulare, California v. Bank of America, N.A.* The MDL 1950 court denied AGM and AGUS's motions to dismiss the eleven complaints that were pending as of April 2010. Amended complaints were filed in May 2010. The complaints in these lawsuits generally seek or sought unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from the remaining lawsuits.

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

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

In September 2009, the Attorney General of the State of West Virginia filed a lawsuit (Circuit Ct. Mason County, W. Va.) against Bank of America, N.A. alleging West Virginia state antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. An amended complaint in this action was filed in June 2010, adding a federal antitrust claim and naming AGM (but not AGMH) and AGUS, among other defendants. This case has been removed to federal court as well as transferred to the S.D.N.Y. and consolidated with MDL 1950 for pretrial proceedings. AGM and AGUS answered West Virginia's Second Amended Complaint on November 11, 2013. The complaint in this lawsuit generally seeks civil penalties, unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from this lawsuit.

16. Notes Payable and Credit Facilities

Notes Payable

Notes Payable represents debt issued by VIEs consolidated by AGM to one of the Financial Products Companies that were transferred to Dexia Holdings prior to the acquisition of AGMH. The funds borrowed were used to finance the purchase of the underlying obligations of AGM-insured obligations which had breached triggers allowing AGM to exercise its right to accelerate payment of a claim in order to mitigate loss. The assets purchased are classified as assets acquired in refinancing transactions and recorded in "other invested assets." The terms of the notes payable match the terms of the assets acquired in refinancing transactions.

The principal and carrying values of the Company's notes payable are presented in the table below.

Principal and Carrying Amounts of Notes Payable

	As of December 31,			
	2015		2014	
	Principal	Carrying Value	Principal	Carrying Value
	(in millions)			
Notes Payable	$ 12	$ 13	$ 16	$ 19

Principal payments due under the notes payable are as follows:

Expected Maturity Schedule of Notes Payable

Expected Withdrawal Date	Principal Amount
	(in millions)
2016	$ 4
2017	4
2018	2
2019	1
2020	0
Thereafter	1
Total	$ 12

Recourse Credit Facilities

2009 Strip Coverage Facility

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

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

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

Currently, all the leveraged lease transactions in which AGM acts as strip coverage provider are breaching a rating trigger related to AGM and are subject to early termination. However, early termination of a lease does not result in a draw on the AGM policy if the tax-exempt entity makes the required termination payment. If all the leases were to terminate early and the tax-exempt entities do not make the required early termination payments, then AGM would be exposed to possible liquidity claims on gross exposure of approximately $1.1 billion as of December 31, 2015. To date, none of the leveraged lease transactions that involve AGM has experienced an early termination due to a lease default and a claim on the AGM policy. It is difficult to determine the probability that AGM will have to pay strip provider claims or the likely aggregate amount of such claims. At December 31, 2015, approximately $1.4 billion of cumulative strip par exposure had been terminated since 2008 on a consensual basis. The consensual terminations have resulted in no claims on AGM.

On July 1, 2009, AGM and Dexia Crédit Local S.A., acting through its New York Branch ("Dexia Crédit Local (NY)"), entered into a credit facility (the "Strip Coverage Facility"). Under the Strip Coverage Facility, Dexia Crédit Local (NY) agreed to make loans to AGM to finance all draws made by lessors on AGM strip policies that were outstanding as of November 13, 2008, up to the commitment amount. The commitment amount of the Strip Coverage Facility was $1 billion at closing of the Company's acquisition of AGMH. AGM has reduced the maximum commitment amount from time to time, after taking into account its experience with its exposure to leveraged lease transactions. Most recently, as of June 30, 2014, AGM reduced the maximum commitment amount to $495 million and agreed with Dexia Crédit Local (NY) that the commitment amount would no longer amortize on a scheduled monthly basis.

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

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

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

The Company was in compliance with all financial covenants as of December 31, 2015.

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

As of December 31, 2015, no amounts were outstanding under this facility, nor have there been any borrowings during the life of this facility.

AGM CPS Securities

In June 2003, $200 million of "AGM CPS", money market preferred trust securities, were issued by trusts created for the primary purpose of issuing the AGM CPS, investing the proceeds in high-quality commercial paper and selling put options to AGM, allowing AGM to issue the trusts non-cumulative redeemable perpetual preferred stock (the "AGM Preferred Stock") of AGM in exchange for cash. There are four trusts, each with an initial aggregate face amount of $50 million. These trusts hold auctions every 28 days, at which time investors submit bid orders to purchase AGM CPS. If AGM were to exercise a put option, the applicable trust would transfer the portion of the proceeds attributable to principal received upon maturity of its assets, net of expenses, to AGM in exchange for AGM Preferred Stock. AGM pays a floating put premium to the trusts, which represents the difference between the commercial paper yield and the winning auction rate (plus all fees and expenses of the trust). If an auction does not attract sufficient clearing bids, however, the auction rate is subject to a maximum rate of one-month LIBOR plus 200 basis points for the next succeeding distribution period. Beginning in August 2007, the AGM CPS required the maximum rate for each of the relevant trusts. AGM continues to have the ability to exercise its put option and cause the related trusts to purchase AGM Preferred Stock. The trusts provide AGM access to new capital at its sole discretion through the exercise of the put options. As of December 31, 2015 the put option had not been exercised. The Company does not consider itself to be the primary beneficiary of the trusts. See Note 6, Fair Value Measurement, –Other Assets–Committed Capital Securities, for a fair value measurement discussion.

17. Employee Benefit Plans

Accounting Policy

AGM 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 all compensation expense based on time studies conducted annually.

Assured Guaranty Ltd. 2004 Long-Term Incentive Plan

Under the Assured Guaranty Ltd. 2004 Long-Term Incentive Plan, as amended (the "Incentive Plan"), the number of AGL common shares that may be delivered under the Incentive Plan may not exceed 18,670,000. In the event of certain transactions affecting AGL's common shares, the number or type of shares subject to the Incentive Plan, the number and type of shares subject to outstanding awards under the Incentive Plan, and the exercise price of awards under the Incentive Plan, may be adjusted.

The Incentive Plan authorizes the grant of incentive stock options, non-qualified stock options, stock appreciation rights, and full value awards that are based on AGL's common shares. The grant of full value awards may be in return for a participant's previously performed services, or in return for the participant surrendering other compensation that may be due, or may be contingent on the achievement of performance or other objectives during a specified period, or may be subject to a risk of forfeiture or other restrictions that will lapse upon the achievement of one or more goals relating to completion of service by the participant, or achievement of performance or other objectives. Awards under the Incentive Plan may accelerate and become vested upon a change in control of AGL.

The Incentive Plan is administered by the Compensation Committee of the Board of Directors of AGL, except as otherwise determined by the Board. The Board may amend or terminate the Incentive Plan. As of December 31, 2015, 10,367,163 common shares of AGL were available for grant under the Incentive Plan.

The Company recognized expenses of $4 million and $4 million for the years ended December 31, 2015 and 2014, respectively, under the Incentive Plan.

Time Vested Stock Options

Stock options are generally granted once a year with exercise prices equal to the closing price on the date of grant. To date, AGL has only issued non-qualified stock options. All stock options, except for performance stock options, granted to employees vest in equal annual installments over a three-year period and expire seven years or ten years from the date of grant. None of AGL's options, except for performance stock options, have a performance or market condition.

Performance Stock Options

Assured Guaranty grants performance stock options under the Incentive Plan. These awards are non-qualified stock options with exercise prices equal to the closing price of an AGL common share on the applicable date of grant. These awards vest 35%, 50% or 100%, if the price of AGL's common shares using the highest 40-day average share price during the relevant three-year performance period reaches certain hurdles. If the share price is between the specified levels, the vesting level will be interpolated accordingly. These awards expire seven years from the date of grant.

Restricted Stock Awards

Restricted stock awards are valued based on the closing price of the underlying shares at the date of grant. These restricted stock awards to employees generally vest in equal annual installments over a four-year period.

Restricted Stock Units

Restricted stock units are valued based on the closing price of the underlying shares at the date of grant. Restricted stock units generally vest in equal annual installments over a four-year period or fully vest after a three-year period.

Performance Restricted Stock Units

Assured Guaranty has granted performance restricted stock units under the Incentive Plan. These awards vest 35%, 50%, 100%, or 200%, if the price of AGL's common shares using the highest 40-day average share price during the relevant three-year performance period reaches certain hurdles. If the share price is between the specified levels, the vesting level will be interpolated accordingly.

Employee Stock Purchase Plan

Assured Guaranty established the AGL Employee Stock Purchase Plan ("Stock Purchase Plan") in accordance with Internal Revenue Code Section 423, and participation is available to all eligible employees. Maximum annual purchases by participants are limited to the number of whole shares that can be purchased by an amount equal to 10% of the participant's compensation or, if less, shares having a value of $25,000. Participants may purchase shares at a purchase price equal to 85% of the lesser of the fair market value of the stock on the first day or the last day of the subscription period. The Company recorded $0.1 million and $0.1 million in share-based compensation, after the effects of DAC, under the Stock Purchase Plan during the years ended December 31, 2015 and 2014, respectively.

Defined Contribution Plan

Employees receive employer contributions into the AGC Employee Retirement Plan (“AGC ERP”) based on a fixed percentage of the employee's compensation and are eligible to make employee contributions and to receive matching employer contributions based on a percentage of compensation up to limits prescribed by Internal Revenue Code Section 401(k). The Company recognized defined contribution expenses of $5 million and $5 million for the years ended December 31, 2015 and 2014, respectively.

Cash-Based Compensation Plans

Assured Guaranty Ltd. maintains a Performance Retention Plan (“PRP”) that permits the grant of deferred cash based awards to selected employees. Generally, each PRP award is divided into three installments, that vest over four years. The cash payment depends on growth in adjusted book value per share and on operating return on equity, which are defined in each PRP award agreement. The Company recognized performance retention plan expenses of $5 million and $7 million for the years ended December 31, 2015 and 2014, respectively, representing its proportionate share of the Assured Guaranty expense.

Assured Guaranty's executive officers are eligible to receive compensation under a non-equity incentive plan. The amount of compensation payable is subject to a performance goal being met. AGL's Compensation Committee then uses discretion to determine the actual amount of cash incentive compensation payable to each executive officer for such performance year based on factors and criteria as determined by the Compensation Committee of AGL, provided that such discretion cannot be used to increase the amount that was determined to be payable to each executive officer. For an applicable performance year, the Compensation Committee of AGL establishes target financial performance measures for AGL and individual non-financial objectives for the executive officers.

18. Other Comprehensive Income

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

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2015

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, December 31, 2014	$ 186	$ (2)	$ 184
Other comprehensive income (loss) attributable to AGM before reclassifications	(48)	(37)	(85)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	1	25	26
Net investment income	(9)	—	(9)
Tax (provision) benefit	3	(9)	(6)
Total amount reclassified from AOCI, net of tax	(5)	16	11
Net current period other comprehensive income (loss) attributable to AGM	(53)	(21)	(74)
Balance, December 31, 2015	$ 133	$ (23)	$ 110

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2014

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, December 31, 2013	$ 105	$ (19)	$ 86
Other comprehensive income (loss) attributable to AGM before reclassifications	86	(28)	58
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(9)	70	61
Tax (provision) benefit	4	(25)	(21)
Total amount reclassified from AOCI, net of tax	(5)	45	40
Net current period other comprehensive income (loss) attributable to AGM	81	17	98
Balance, December 31, 2014	$ 186	$ (2)	$ 184

19. Subsequent Events

Subsequent events have been considered through March 30, 2016, the date on which these financial statements were issued.

APPENDIX 4

2014 FINANCIAL STATEMENTS OF ASSURED GUARANTY MUNICIPAL CORP.

Exhibit 99.1

Assured Guaranty Municipal Corp.

Consolidated Financial Statements

December 31, 2014 and 2013

ASSURED GUARANTY MUNICIPAL CORP.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Independent Auditor's Report

To the Board of Directors of Assured Guaranty Municipal Corp.:

We have audited the accompanying consolidated financial statements of Assured Guaranty Municipal Corp. and its subsidiaries (the “Company”), which comprise the consolidated balance sheets as of December 31, 2014 and December 31, 2013, and the related consolidated statements of operations, of comprehensive income, 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.

Auditor's 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 Municipal Corp. and its subsidiaries at December 31, 2014 and December 31, 2013, 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
March 30, 2015

Assured Guaranty Municipal Corp.

Consolidated Balance Sheets

(dollars in millions except per share and share amounts)

	As of December 31, 2014	As of December 31, 2013
Assets		
Investment portfolio:		
Fixed-maturity securities, available-for-sale, at fair value (amortized cost of $5,920 and $5,394)	$ 6,212	$ 5,522
Short-term investments, at fair value	377	667
Other invested assets (includes Surplus Note from affiliate of $300 and $300)	406	406
Total investment portfolio	6,995	6,595
Cash	23	53
Premiums receivable	450	578
Ceded unearned premium reserve	958	1,047
Reinsurance recoverable on unpaid losses	133	66
Salvage and subrogation recoverable	130	140
Credit derivative assets	79	98
Deferred tax asset, net	161	331
Financial guaranty variable interest entities' assets, at fair value	823	1,691
Other assets	154	190
Total assets	**$ 9,906**	**$ 10,789**
Liabilities and shareholder's equity		
Unearned premium reserve	$ 3,425	$ 3,652
Loss and loss adjustment expense reserve	404	273
Reinsurance balances payable, net	158	217
Notes payable	19	39
Credit derivative liabilities	287	326
Current income tax payable	57	114
Financial guaranty variable interest entities' liabilities with recourse, at fair value	830	1,275
Financial guaranty variable interest entities' liabilities without recourse, at fair value	114	686
Other liabilities	322	366
Total liabilities	**5,616**	**6,948**
Commitments and contingencies (See Note 17)		
Preferred stock ($1,000 par value, 5,000.1 shares authorized; 0 shares issued and outstanding)	—	—
Common stock ($45,455 par value, 330 shares authorized; issued and outstanding)	15	15
Additional paid-in capital	1,000	1,051
Retained earnings	2,752	2,400
Accumulated other comprehensive income, net of tax of $107 and $45	184	86
Total shareholder's equity attributable to Assured Guaranty Municipal Corp.	**3,951**	**3,552**
Noncontrolling interest	339	289
Total shareholder's equity	**4,290**	**3,841**
Total liabilities and shareholder's equity	**$ 9,906**	**$ 10,789**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Operations

(in millions)

	Year Ended December 31,	
	2014	2013
Revenues		
Net earned premiums	$ 374	$ 508
Net investment income	267	246
Net realized investment gains (losses):		
Other-than-temporary impairment losses	(69)	(19)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	1	2
Net impairment loss	(70)	(21)
Other net realized investment gains (losses)	11	44
Net realized investment gains (losses)	(59)	23
Net change in fair value of credit derivatives:		
Realized gains (losses) and other settlements	22	41
Net unrealized gains (losses)	19	57
Net change in fair value of credit derivatives	41	98
Fair value gains (losses) on committed capital securities	(4)	7
Fair value gains (losses) on financial guaranty variable interest entities	234	343
Other income (loss)	4	(23)
Total revenues	857	1,202
Expenses		
Loss and loss adjustment expenses	(25)	92
Amortization of deferred ceding commissions	(4)	(28)
Interest expense	2	6
Other operating expenses	111	107
Total expenses	84	177
Income (loss) before income taxes	773	1,025
Provision (benefit) for income taxes:		
Current	102	157
Deferred	127	165
Total provision (benefit) for income taxes	229	322
Net income (loss)	**544**	**703**
Less: Noncontrolling interest	32	20
Net income (loss) attributable to Assured Guaranty Municipal Corp.	**$ 512**	**$ 683**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Comprehensive Income

(in millions)

	Year Ended December 31,	
	2014	2013
Net income (loss)	**$ 544**	**$ 703**
Unrealized holding gains (losses) arising during the period on:		
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $56 and $(57)	103	(105)
Investments with other-than-temporary impairment, net of tax provision (benefit) of $(15) and $(15)	(28)	(27)
Unrealized holding gains (losses) arising during the period, net of tax	75	(132)
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $(21) and $8	(40)	16
Other comprehensive income (loss)	115	(148)
Comprehensive income (loss)	**659**	**555**
Less: Comprehensive income (loss) attributable to noncontrolling interest	49	18
Comprehensive income (loss) of Assured Guaranty Municipal Corp.	**$ 610**	**$ 537**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Shareholder’s Equity

(dollars in millions, except share data)

	Common Shares Outstanding	Common Stock Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholder's Equity Attributable to Assured Guaranty Municipal Corp.	Noncontrolling Interest	Total Shareholder's Equity
Balance at December 31, 2012	**330**	**15**	**1,092**	**1,880**	**232**	**$ 3,219**	**$ —**	**$ 3,219**
Net income	—	—	—	683	—	683	20	703
Capital contribution	—	—	13	—	—	13	—	13
Investment in Municipal Assurance Holdings Inc.	—	—	—	—	—	—	271	271
Dividends	—	—	—	(163)	—	(163)	—	(163)
Other comprehensive income (loss)	—	—	—	—	(146)	(146)	(2)	(148)
Return of capital:								
Repayment of Surplus Notes	—	—	(50)	—	—	(50)	—	(50)
Other	—	—	(4)	—	—	(4)	—	(4)
Balance at December 31, 2013	**330**	**15**	**1,051**	**2,400**	**86**	**3,552**	**289**	**3,841**
Net income	—	—	—	512	—	512	32	544
Dividends	—	—	—	(160)	—	(160)	—	(160)
Other comprehensive income (loss)	—	—	—	—	98	98	17	115
Return of capital:								
Repayment of Surplus Notes	—	—	(50)	—	—	(50)	—	(50)
Other	—	—	(1)	—	—	(1)	1	0
Balance at December 31, 2014	**330**	**$ 15**	**$ 1,000**	**$ 2,752**	**$ 184**	**$ 3,951**	**$ 339**	**$ 4,290**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Cash Flows

(in millions)

	Year Ended December 31, 2014	Year Ended December 31, 2013
Operating Activities:		
Net Income	$ 544	$ 703
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Net amortization of premium (discount) on investments	(15)	(15)
Provision (benefit) for deferred income taxes	127	165
Net realized investment losses (gains)	59	(23)
Net unrealized losses (gains) on credit derivatives	(19)	(57)
Fair value losses (gains) on committed capital securities	4	(7)
Change in deferred ceding commissions, net	(8)	(25)
Change in premiums receivable, net of premiums payable and commissions	75	36
Change in deferred premium revenue net of ceded deferred premium revenue	(138)	(320)
Change in loss and loss adjustment expense reserve and salvage and subrogation, net	66	118
Change in current income tax	(76)	99
Change in financial guaranty variable interest entities' assets and liabilities, net	(145)	(305)
(Purchases) sales of trading securities, net	37	3
Other	(49)	19
Net cash flows provided by (used in) operating activities	462	391
Investing activities		
Fixed-maturity securities:		
Purchases	(1,387)	(926)
Sales	362	287
Maturities	459	480
Net sales (purchases) of short-term investments	312	(182)
Net proceeds from paydowns on financial guaranty variable interest entities’ assets	360	587
Loan to affiliate	—	7
Other	(1)	28
Net cash flows provided by (used in) investing activities	**105**	**281**
Financing activities		
Dividends paid	(160)	(163)
Repayment of notes payable	(19)	(27)
Net paydowns of financial guaranty variable interest entities' liabilities	(365)	(425)
Repayment of Surplus Notes	(50)	(50)
Net cash flows provided by (used in) financing activities	**(594)**	**(665)**
Effect of foreign exchange rate changes	(3)	(1)
Increase (decrease) in cash	**(30)**	**6**
Cash at beginning of period	53	47
Cash at end of period	**$ 23**	**$ 53**
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$ 155	$ 40
Interest	$ 3	$ 6

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

Assured Guaranty Municipal Corp.

Notes to Consolidated Financial Statements

December 31, 2014 and 2013

1. Business and Basis of Presentation

Business

Assured Guaranty Municipal Corp. (“AGM,” or together with its direct and indirect subsidiaries, the “Company”), a New York domiciled insurance company, is a wholly owned subsidiary of Assured Guaranty Municipal Holdings Inc. (“AGMH”). AGMH is an indirect and wholly owned subsidiary of Assured Guaranty Ltd. (“AGL” and, together with its subsidiaries, “Assured Guaranty”). AGL is a Bermuda-based holding company that provides, through its operating subsidiaries, credit protection products to the United States (“U.S.”) and international public finance (including infrastructure) and structured finance markets. AGM formerly was known as Financial Security Assurance Inc.

The Company applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guaranty insurance that protects holders of debt instruments and other monetary obligations from defaults in scheduled payments. If an obligor defaults on a scheduled payment due on an obligation, including a scheduled principal or interest payment (“Debt Service”), the Company is required under its unconditional and irrevocable financial guaranty to pay the amount of the shortfall to the holder of the obligation. Obligations insured by the Company include bonds issued by U.S. state or municipal governmental authorities and notes issued to finance international infrastructure projects. AGM had previously offered insurance and reinsurance in the global structured finance market, but has not done so since mid-2008. The Company markets its financial guaranty insurance directly to issuers and underwriters of public finance bonds as well as to investors in such obligations. The Company guarantees obligations issued principally in the U.S. and the United Kingdom (the "U.K."), and has also guaranteed obligations issued in other countries and regions, including Australia and Western Europe. While AGM has ceased insuring new originations of asset-backed securities, a significant portfolio of such obligations remains outstanding. AGM's wholly owned subsidiary Assured Guaranty (Europe) Ltd. (“AGE”) provides financial guarantees in the international public finance market and intends to provide such guarantees in the international structured finance market, subject to regulatory approval.

In the past, the Company sold credit protection by issuing policies that guaranteed payment obligations under credit derivatives, primarily credit default swaps (“CDS”). Financial guaranty contracts accounted for as credit derivatives are generally structured such that the circumstances giving rise to the Company’s obligation to make loss payments are similar to those for financial guaranty insurance contracts. The Company’s credit derivative transactions are governed by International Swaps and Derivative Association, Inc. (“ISDA”) documentation. The Company has not entered into any new CDS in order to sell credit protection since 2008. Regulatory guidelines issued in 2009 limiting the terms under which such protection could be sold as well as the capital and margin requirements applicable under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) contributed to the Company choosing not to enter into any such new CDS since 2009. The Company actively pursues opportunities to terminate existing CDS, which have the effect of reducing future fair value volatility in income and/or reducing rating agency capital charges.

Basis of Presentation

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) and, in the opinion of management, reflect all adjustments that are of a normal recurring nature, necessary for a fair statement of the financial condition, results of operations and cash flows of the Company and its consolidated financial guaranty variable interest entities (“FG VIEs”) for the periods presented. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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

AGM's direct and indirect subsidiaries are as follows:

- AGE, organized in the United Kingdom ("U.K.") and 100% owned by AGM;
- Municipal Assurance Holdings Inc. ("MAC Holdings"), incorporated in Delaware and 60.7% owned by AGM and 39.3% owned by AGM's affiliate, Assured Guaranty Corp. ("AGC"); and
- Municipal Assurance Corp. ("MAC"), domiciled in New York and 100% owned by MAC Holdings.

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 AGM's foreign currency transactions are reported in the consolidated statement of operations.

The chief operating decision maker manages the operations of the Company at a consolidated level. Therefore, all results of operations are reported as one segment.

Other significant accounting policies are included in the following notes.

Significant Accounting Policies

Premium revenue recognition	Note 4
Policy acquisition cost	Note 5
Expected loss to be paid (Insurance, Credit Derivatives and FG VIE contracts)	Note 6
Loss and loss adjustment expense (Insurance Contracts)	Note 7
Fair value measurement	Note 8
Credit derivatives	Note 9
Variable interest entities	Note 10
Investments and Cash	Note 11
Income Taxes	Note 14
Reinsurance and Other Monoline Exposures	Note 15

2. Rating Actions

Rating Actions

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

In the last several years, Standard & Poor's Ratings Services ("S&P") and Moody's Investors Service, Inc. ("Moody's") have changed, multiple times, their financial strength ratings of AGM and AGE, or changed the outlook on such ratings. More recently, Kroll Bond Rating Agency ("KBRA") has assigned financial strength ratings to MAC and AGM. The rating agencies' most recent actions and proposals related to AGM and its subsidiaries are:

- On March 18, 2014, S&P upgraded the financial strength ratings of AGM, AGE and MAC to AA (stable outlook) from AA- (stable outlook); it affirmed such ratings in a credit analysis issued on July 2, 2014.

- On July 2, 2014, Moody's affirmed AGM's and AGE's A2 (stable outlook) financial strength ratings.

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

- On November 13, 2014, KBRA assigned a financial strength rating of AA+ (stable outlook) to AGM.

- On January 20, 2015, Moody's adopted changes to its credit methodology for financial guaranty insurance companies, and on February 18, 2015 Moody's published a credit opinion maintaining its existing ratings of AGM and AGE under that new methodology.

There can be no assurance that any of the rating agencies will not take negative action on the financial strength ratings of AGM or its insurance subsidiaries in the future.

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

- Note 7, Financial Guaranty Insurance Losses

- Note 15, Reinsurance and Other Monoline Exposures

- Note 18, Notes Payable and Credit Facilities (regarding the impact on AGM's insured leveraged lease transactions)

3. Outstanding Exposure

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

The Company has issued financial guaranty insurance policies on public finance obligations and, prior to mid-2008, structured finance obligations. Public finance obligations insured by the Company consist primarily of general obligation bonds supported by the taxing powers of U.S. state or municipal governmental authorities, as well as tax-supported bonds, revenue bonds and other obligations supported by covenants from state or municipal governmental authorities or other municipal obligors to impose and collect fees and charges for public services or specific infrastructure projects. The Company also includes within public finance obligations those obligations backed by the cash flow from leases or other revenues from projects serving substantial public purposes, including utilities, toll roads, health care facilities and government office buildings.

Structured finance obligations insured by the Company are generally issued by special purpose entities including variable interest entities ("VIEs"), and backed by pools of assets having an ascertainable cash flow or market value or other specialized financial obligations. Some of these VIEs are consolidated as described in Note 10, Consolidated Variable Interest Entities. Unless otherwise specified, the outstanding par and Debt Service amounts presented in this note include outstanding exposures on VIEs whether or not they are consolidated. While AGM has ceased writing new originations of asset-backed securities, a significant portfolio of such obligations remains outstanding and AGE may, subject to regulatory approval, provide guarantees on structured finance obligations outside the U.S.

Debt Service and par outstanding exposures presented in these financial statements are presented on a consolidated basis. That is, amounts presented include 100% of the exposures of AGM, AGE and MAC, despite the fact that AGM indirectly owns only 60.7% of MAC.

Significant Risk Management Activities

Assured Guaranty's Portfolio Risk Management Committee, which includes members of senior management and senior credit and surveillance officers of the Company, sets specific risk policies and limits and is responsible for enterprise risk management, establishing the Company's risk appetite, credit underwriting of new business, surveillance and work-out.

Surveillance personnel are responsible for monitoring and reporting on all transactions in the insured portfolio. The primary objective of the surveillance process is to monitor trends and changes in transaction credit quality, detect any deterioration in credit quality, and recommend to management such remedial actions as may be necessary or appropriate. All transactions in the insured portfolio are assigned internal credit ratings, and surveillance personnel are responsible for recommending adjustments to those ratings to reflect changes in transaction credit quality.

Work-out personnel are responsible for managing work-out and loss mitigation situations, working with surveillance and legal personnel (as well as outside vendors) as appropriate. They develop strategies for the Company to enforce its contractual rights and remedies and to mitigate its losses, engage in negotiation discussions with transaction participants and, when necessary, manage (along with legal personnel) the Company's litigation proceedings.

Surveillance Categories

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

The Company monitors its investment grade credits to determine whether any new credits need to be internally downgraded to BIG and refreshes its internal credit ratings on individual credits in quarterly, semi-annual or annual cycles based on the Company's view of the credit's quality, loss potential, volatility and sector. Ratings on credits in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter. The Company's credit ratings on assumed credits are based on the Company's reviews of low-rated credits or credits in volatile sectors, unless such information is not available, in which case, the ceding company's credit rating of the transactions are used. The Company models the performance of many of its structured finance transactions as part of its periodic internal credit rating review of them.

Credits identified as BIG are subjected to further review to determine the probability of a loss. See Note 6, Expected Loss to be Paid for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. For surveillance purposes, the Company calculates present value using a constant discount rate of 5%. (A risk-free curve rate is used for calculating the expected loss for financial statement measurement purposes.)

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

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

Components of Outstanding Exposure

Unless otherwise noted, ratings disclosed herein on the Company's insured portfolio reflect the Company's internal ratings. The Company classifies those portions of risks benefiting from reimbursement obligations collateralized by eligible assets held in trust in acceptable reimbursement structures as the higher of 'AA' or their current internal rating. The Company excludes amounts attributable to loss mitigation securities (unless otherwise indicated) from par and Debt Service outstanding, because it manages such securities as investments and not insurance exposure.

Financial Guaranty
Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding(1)	
	December 31, 2014	December 31, 2013	December 31, 2014	December 31, 2013
	(in millions)			
Public finance	$ 473,492	$ 522,777	$ 348,905	$ 386,897
Structured finance	33,196	48,250	29,756	42,354
Total financial guaranty	$ 506,688	$ 571,027	$ 378,661	$ 429,251

(1) Includes $132.0 billion and $153.3 billion of net debt service outstanding, as of December 31, 2014 and 2013, respectively, from MAC, which represents 100% of MAC's net debt service outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2014

	Public Finance U.S.		Public Finance Non-U.S.		Structured Finance U.S.		Structured Finance Non-U.S.		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
					(dollars in millions)					
AAA	$ 3,254	1.6%	$ 541	2.7%	$ 13,185	61.3%	$ 3,311	73.1%	$ 20,291	8.0%
AA	62,175	30.1	348	1.7	4,883	22.7	312	6.9	67,718	26.8
A	112,119	54.3	5,488	27.1	45	0.2	175	3.9	117,827	46.6
BBB	25,604	12.4	12,891	63.5	266	1.2	226	5.0	38,987	15.5
BIG	3,274	1.6	1,024	5.0	3,130	14.6	501	11.1	7,929	3.1
Total net par outstanding (1) (2)	$ 206,426	100.0%	$ 20,292	100.0%	$ 21,509	100.0%	$ 4,525	100.0%	$ 252,752	100.0%

(1) Excludes $675 million of loss mitigation securities insured and held by the Company as of December 31, 2014, which are primarily in the BIG category.

(2) Includes $90.6 billion of net par outstanding as of December 31, 2014, from MAC, which represents 100% of MAC's net par outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

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

	Public Finance U.S.		Public Finance Non-U.S.		Structured Finance U.S.		Structured Finance Non-U.S.		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
					(dollars in millions)					
AAA	$ 4,012	1.8%	$ 524	2.4%	$ 20,283	66.7%	$ 5,551	78.0%	$ 30,370	10.6%
AA	74,478	32.7	378	1.8	5,718	18.8	343	4.8	80,917	28.2
A	123,389	54.2	5,611	25.8	198	0.7	193	2.8	129,391	45.1
BBB	22,091	9.7	14,025	64.6	382	1.2	397	5.6	36,895	12.9
BIG	3,648	1.6	1,171	5.4	3,836	12.6	629	8.8	9,284	3.2
Total net par outstanding (1) (2)	$ 227,618	100.0%	$ 21,709	100.0%	$ 30,417	100.0%	$ 7,113	100.0%	$ 286,857	100.0%

(1) Excludes $627 million of loss mitigation securities insured and held by the Company as of December 31, 2013, which are primarily in the BIG category.

(2) Includes $104.2 billion of net par outstanding as of December 31, 2013, from MAC, which represents 100% of MAC's net par outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

Financial Guaranty Portfolio
by Sector

Sector	Gross Par Outstanding As of December 31, 2014	Gross Par Outstanding As of December 31, 2013	Ceded Par Outstanding As of December 31, 2014	Ceded Par Outstanding As of December 31, 2013	Net Par Outstanding As of December 31, 2014	Net Par Outstanding As of December 31, 2013
			(in millions)			
Public finance:						
U.S.:						
General obligation	$ 124,967	$ 138,342	$ 29,979	$ 32,314	$ 94,988	$ 106,028
Tax backed	51,522	54,982	12,510	12,909	39,012	42,073
Municipal utilities	45,468	48,835	9,045	9,302	36,423	39,533
Transportation	20,632	23,798	4,528	5,502	16,104	18,296
Healthcare	11,184	11,777	3,828	4,073	7,356	7,704
Higher education	9,693	10,313	2,449	2,508	7,244	7,805
Housing	2,677	3,368	509	582	2,168	2,786
Infrastructure finance	2,606	2,508	1,284	1,219	1,322	1,289
Other public finance-U.S.	1,998	2,390	189	286	1,809	2,104
Total public finance-U.S.	270,747	296,313	64,321	68,695	206,426	227,618
Non-U.S.:						
Infrastructure finance	14,242	16,021	4,794	5,347	9,448	10,674
Regulated utilities	12,996	13,685	6,705	7,501	6,291	6,184
Other public finance-non-U.S.	6,115	6,532	1,562	1,681	4,553	4,851
Total public finance-non-U.S.	33,353	36,238	13,061	14,529	20,292	21,709
Total public finance obligations	$ 304,100	$ 332,551	$ 77,382	$ 83,224	$ 226,718	$ 249,327
Structured finance:						
U.S.:						
Pooled corporate obligations	14,517	$ 22,112	$ 943	$ 1,359	13,574	$ 20,753
Residential Mortgage-Backed Security ("RMBS")	5,777	7,017	810	932	4,967	6,085
Financial products	2,276	2,709	—	—	2,276	2,709
Insurance securitizations	383	383	55	77	328	306
Consumer receivables	170	198	10	11	160	187
Commercial receivables	40	47	2	3	38	44
Structured credit	8	8	2	2	6	6
Other structured finance-U.S.	282	1,422	122	1,095	160	327
Total structured finance-U.S.	23,453	33,896	1,944	3,479	21,509	30,417
Non-U.S.:						
Pooled corporate obligations	4,310	6,839	881	1,226	3,429	5,613
RMBS	837	1,182	113	138	724	1,044
Structured credit	—	104	—	21	—	83
Other structured finance- non-U.S.	400	401	28	28	372	373
Total structured finance- non-U.S.	5,547	8,526	1,022	1,413	4,525	7,113
Total structured finance obligations	$ 29,000	$ 42,422	$ 2,966	4,892	$ 26,034	$ 37,530
Total	$ 333,100	$ 374,973	$ 80,348	88,116	$ 252,752	$ 286,857

In addition to amounts shown in the tables above, at December 31, 2014, AGM had outstanding commitments to provide guaranties of $248 million for public finance obligations, of which up to $124 million can be used together with AGC,

an affiliate of the Company. The expiration dates for the public finance commitments range between January 1, 2015 and February 25, 2017, with $124 million expiring prior to December 31, 2015. The commitments are contingent on the satisfaction of all conditions set forth in them and may expire unused or be canceled at the counterparty's request. Therefore, the total commitment amount does not necessarily reflect actual future guaranteed amounts.

Actual maturities of insured obligations could differ from contractual maturities because borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties. The expected maturities of structured finance obligations are, in general, considerably shorter than the contractual maturities for such obligations.

**Expected Amortization of
Net Par Outstanding
As of December 31, 2014**

	Public Finance	Structured Finance	Total
		(in millions)	
0 to 5 years	$ 68,967	$ 20,897	$ 89,864
5 to 10 years	49,220	1,820	51,040
10 to 15 years	43,459	1,077	44,536
15 to 20 years	30,996	1,298	32,294
20 years and above	34,076	942	35,018
Total net par outstanding	$ 226,718	$ 26,034	$ 252,752

Components of BIG Portfolio

**Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of December 31, 2014**

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
First lien U.S. RMBS:					
Prime first lien	$ —	$ —	$ —	$ —	$ 57
Alt-A first lien	27	98	523	648	819
Option ARM	4	—	56	60	175
Subprime	46	483	573	1,102	2,487
Second lien U.S. RMBS:					
Closed-end second lien	—	19	61	80	181
Home equity lines of credit ("HELOCs")	636	—	434	1,070	1,248
Total U.S. RMBS	713	600	1,647	2,960	4,967
Trust preferred securities ("TruPS")	—	—	—	—	44
Other structured finance	565	62	44	671	21,023
U.S. public finance	2,748	464	62	3,274	206,426
Non-U.S. public finance	1,024	—	—	1,024	20,292
Total	$ 5,050	$ 1,126	$ 1,753	$ 7,929	$ 252,752

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

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
First lien U.S. RMBS:					
Prime first lien	$ —	$ —	$ —	$ —	$ 66
Alt-A first lien	—	259	450	709	900
Option ARM	7	—	141	148	359
Subprime	49	708	555	1,312	2,853
Second lien U.S. RMBS:					
Closed-end second lien	8	20	57	85	204
HELOCs	1,239	—	102	1,341	1,703
Total U.S. RMBS	1,303	987	1,305	3,595	6,085
TruPS	—	—	—	—	56
Other structured finance	752	118	—	870	31,389
U.S. public finance	3,535	—	113	3,648	227,618
Non-U.S. public finance	780	391	—	1,171	21,709
Total	$ 6,370	$ 1,496	$ 1,418	$ 9,284	$ 286,857

BIG Net Par Outstanding
and Number of Risks
As of December 31, 2014

	Net Par Outstanding			Number of Risks(2)		
Description	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
			(dollars in millions)			
BIG:						
Category 1	$ 4,940	$ 110	$ 5,050	71	2	73
Category 2	1,126	—	1,126	14	—	14
Category 3	1,734	19	1,753	38	2	40
Total BIG	$ 7,800	$ 129	$ 7,929	123	4	127

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

Description	Net Par Outstanding			Number of Risks(2)		
	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
	(dollars in millions)					
BIG:						
Category 1	$ 6,095	$ 275	$ 6,370	91	8	99
Category 2	1,496	—	1,496	23	—	23
Category 3	1,403	15	1,418	33	7	40
Total BIG	$ 8,994	$ 290	$ 9,284	147	15	162

(1) Includes net par outstanding for FG VIEs.

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

Geographic Distribution of Net Par Outstanding

The Company seeks to maintain a diversified portfolio of insured obligations designed to spread its risk across a number of geographic areas.

Geographic Distribution of Net Par Outstanding
As of December 31, 2014

	Number of Risks	Net Par Outstanding	Percent of Total Net Par Outstanding
		(dollars in millions)	
U.S.:			
U.S. public finance:			
California	1,270	$ 33,308	13.2%
Pennsylvania	968	17,387	6.9
New York	935	16,029	6.3
Texas	1,165	15,690	6.2
Illinois	749	15,437	6.1
Florida	286	11,459	4.5
Michigan	620	9,003	3.6
New Jersey	555	8,904	3.5
Georgia	159	5,626	2.2
Ohio	464	5,254	2.1
Other states and U.S. territories	3,700	68,329	27.1
Total U.S. public finance	10,871	206,426	81.7
U.S. structured finance (multiple states)	257	21,509	8.5
Total U.S.	11,128	227,935	90.2
Non-U.S.:			
United Kingdom	80	11,478	4.5
Canada	10	3,160	1.3
Australia	17	2,766	1.1
France	12	1,443	0.6
Italy	8	1,131	0.4
Other	42	4,839	1.9
Total non-U.S.	169	24,817	9.8
Total	11,297	$ 252,752	100.0%

Exposure to the Selected European Countries

Several European countries continue to experience significant economic, fiscal and/or political strains such that the likelihood of default on obligations with a nexus to those countries may be higher than the Company anticipated when such factors did not exist. The European countries where the Company believes heightened uncertainties exist are: Hungary, Italy, Portugal and Spain (collectively, the “Selected European Countries”). The Company is closely monitoring its exposures in the Selected European Countries where it believes heightened uncertainties exist. Previously, the Company had included Ireland on this list but removed it during the third quarter of 2014 because of Ireland's strengthening economic performance and improving prospects; in 2014, Ireland's long-term foreign currency rating was upgraded one notch by S&P (to ‘A-’) and three notches by Moody’s (to ‘Baa1’). The Company’s direct economic exposure to the Selected European Countries (based on par for financial guaranty contracts and notional amount for financial guaranty contracts accounted for as derivatives) is shown in the following table, net of ceded reinsurance.

Net Direct Economic Exposure to Selected European Countries(1)
As of December 31, 2014

	Hungary	Italy	Portugal	Spain	Total
			(in millions)		
Sovereign and sub-sovereign exposure:					
Non-infrastructure public finance (2)	$ —	$ 723	$ 86	$ 196	$ 1,005
Infrastructure finance	256	7	—	128	391
Total sovereign and sub-sovereign	256	730	86	324	1,396
Non-sovereign exposure:					
Regulated utilities	—	129	—	—	129
RMBS	178	251	—	—	429
Total non-sovereign exposure	178	380	—	—	558
Total	$ 434	$ 1,110	$ 86	$ 324	$ 1,954
Total BIG (See Note 6)	$ 361	$ —	$ 86	$ 324	$ 771

____

(1) While the Company's exposures are shown in U.S. dollars, the obligations the Company insures are in various currencies, primarily Euros. One of the RMBS included in the table above includes residential mortgages in both Italy and Germany, and only the portion of the transaction equal to the portion of the original mortgage pool in Italian mortgages is shown in the table.

(2) The exposure shown in the "Non-infrastructure public finance" category is from transactions backed by receivable payments from sub-sovereigns in Italy, Spain and Portugal. Sub-sovereign debt is debt issued by a governmental entity or government backed entity, or supported by such an entity, that is other than direct sovereign debt of the ultimate governing body of the country.

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

The Company has excluded from the exposure tables above its indirect economic exposure to the Selected European Countries through policies it provides on pooled corporate transactions. The Company calculates indirect exposure to a country by multiplying the par amount of a transaction insured by the Company times the percent of the relevant collateral pool reported as having a nexus to the country. On that basis, the Company has calculated exposure of $70 million to Selected European Countries in transactions with $4.2 billion of net par outstanding.

Exposure to Puerto Rico

The Company insures general obligation bonds of the Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations aggregating $2.2 billion net par as of December 31, 2014. The Company rates $1.9 billion net par of that amount BIG; included in that amount are the obligations of Puerto Rico Highway and Transportation Authority ("PRHTA") (transportation), Puerto Rico Electric Power Authority ("PREPA"), and PRHTA (highway).

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

In June 2014, the Puerto Rico legislature passed the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (the "Recovery Act") in order to provide a legislative framework for certain public corporations experiencing severe financial stress to restructure their debt, including PRHTA and PREPA. Subsequently, the Commonwealth stated PREPA might need to seek relief under the Recovery Act due to liquidity constraints, and disclosed PREPA had utilized approximately $42 million on deposit in its reserve account in order to pay debt service due on its bonds on July 1, 2014.

In August 2014, PREPA entered into forbearance agreements with the GDB, its bank lenders, and bondholders and financial guaranty insurers (including AGM and AGC) that hold or guarantee more than 60% of PREPA's outstanding bonds, in order to address its near-term liquidity issues. Creditors, including AGM and AGC, agreed not to exercise available rights and remedies until March 31, 2015, and the bank lenders agreed to extend the maturity of two revolving lines of credit to the same date. PREPA agreed it would continue to make principal and interest payments on its outstanding bonds, and interest payments on its lines of credit. It also agreed it would develop a five year business plan and a recovery program in respect of its operations; a preliminary business plan was released in December 2014. Creditors, including AGM and AGC, have extended the forbearance agreements through April 15, 2015 and are continuing discussions among themselves and with PREPA regarding potentially extending the forbearance agreements beyond April 15, 2015, but there can be no assurance that such discussions will result in any further extension.

Investors in bonds issued by PREPA filed suit in the United States District Court for the District of Puerto Rico asserting the Recovery Act violates the U.S. Constitution. On February 6, 2015, the U.S. District Court for the District of Puerto Rico ruled the Recovery Act is preempted by the U.S. Bankruptcy Code and is therefore void; on February 19, 2015, the Commonwealth appealed the ruling to the U.S. Court of Appeals for the First Circuit. In addition, the Commonwealth's Resident Commissioner has introduced a bill to the U.S. Congress that, if passed, would enable the Commonwealth to authorize one or more of its public corporations to restructure their debts under chapter 9 of the U.S Bankruptcy Code if they were to become insolvent. The passage of the Recovery Act, its subsequent invalidation, and the introduction of legislation that would enable the Commonwealth to authorize chapter 9 protection for its public corporations have resulted in uncertainty among investors about the rights of creditors of the Commonwealth and its related authorities and public corporations.

Following the enactment of the Recovery Act, S&P, Moody’s and Fitch Ratings lowered the credit rating of the Commonwealth’s bonds and the ratings on certain of its public corporations. In February 2015, S&P and Moody’s and in March 2015, Fitch each again lowered the credit rating of the Commonwealth's bonds and the ratings on certain of its public corporations. The Commonwealth has disclosed its liquidity has been adversely affected by rating agency downgrades and by the limited market access for its debt, and also noted it has relied on short-term financings and interim loans from the GDB and other private lenders, which reliance has constrained its liquidity and increased its near-term refinancing risk.

In early 2015, Puerto Rico enacted legislation designed to stabilize PRHTA and improve the liquidity of the GDB. The legislation provides for certain tax revenues that would support PRHTA and requires the transfer of certain liabilities and revenues from PHRTA to another authority, as well as allowing the transfer of the operations of poorly performing transit facilities to a new authority.

Puerto Rico
Gross Par and Gross Debt Service Outstanding

	Gross Par Outstanding		Gross Debt Service Outstanding	
	December 31, 2014	December 31, 2013	December 31, 2014	December 31, 2013
	(in millions)			
Subject to the Now Voided Recovery Act (1)	$ 1,844	$ 1,980	$ 2,868	$ 3,140
Not subject to the Now Voided Recovery Act	2,204	2,627	3,711	4,374
Total	$ 4,048	$ 4,607	$ 6,579	$ 7,514

(1) On February 6, 2015, the U.S. District Court for the District of Puerto Rico ruled that the Recovery Act is preempted by the Federal Bankruptcy Code and is therefore void. On February 19, 2015, the Commonwealth appealed the ruling to the U.S. Court of Appeals for the First Circuit.

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

Puerto Rico
Net Par Outstanding

	As of December 31, 2014		As of December 31, 2013	
	Total	Internal Rating	Total	Internal Rating
	(in millions)			
Exposures subject to the Now Voided Recovery Act:				
PRHTA (Transportation revenue) ("Primary policies")	$ 223	BB-	$ 236	BB-
PRHTA (Transportation revenue) ("Second-to-pay policies") (1)	80	AA	80	AA
Total	303	BB+	316	BB+
PREPA	464	B-	488	BB-
PRHTA (Highway revenue)	197	BB	216	BB
Puerto Rico Public Finance Corporation	—	—	44	B
Total	964		1,064	
Exposures not subject to the Now Voided Recovery Act:				
Commonwealth of Puerto Rico - General Obligation Bonds	749	BB	871	BB
Puerto Rico Sales Tax Financing Corporation	261	BBB	261	A-
Puerto Rico Municipal Finance Agency	223	BB-	252	BB-
Puerto Rico Public Buildings Authority	18	BB+	32	BB
Total	1,251		1,416	
Total net exposure to Puerto Rico	$ 2,215		$ 2,480	

(1) Represents exposure as to which AGM guarantees payment of principal and interest when due in the event that both the obligor and the AGM affiliate that issued a primary insurance policy fail to pay.

The following table shows the scheduled amortization of the general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations insured and rated BIG by the Company. The Company guarantees payments of interest and principal when those amounts are scheduled to be paid and cannot be required to pay on an accelerated basis. In the event that obligors default on their obligations, the Company would only be required to pay the shortfall between the principal and interest due in any given period and the amount paid by the obligors.

Amortization Schedule of Puerto Rico BIG Net Par Outstanding and BIG Net Debt Service Outstanding As of December 31, 2014

	Scheduled BIG Net Par Amortization			Scheduled BIG Net Debt Service Amortization		
	Subject to the Now Voided Recovery Act	Not Subject to the Now Voided Recovery Act	Total	Subject to the Now Voided Recovery Act	Not Subject to the Now Voided Recovery Act	Total
			(in millions)			
2015	$ 73	$ 65	$ 138	$ 117	$ 117	$ 234
2016	35	71	106	75	120	195
2017	29	74	103	68	119	187
2018	23	40	63	59	81	140
2019	33	57	90	69	95	164
2020	46	52	98	79	87	166
2021	34	13	47	65	46	111
2022	30	25	55	60	58	118
2023	70	11	81	99	42	141
2024	56	45	101	81	77	158
2025 - 2029	232	150	382	320	272	592
2030 - 2034	175	234	409	212	319	531
2035 - 2037	48	153	201	52	169	221
Total	$ 884	$ 990	$ 1,874	$ 1,356	$ 1,602	$ 2,958

4. Financial Guaranty Insurance Premiums

The portfolio of outstanding exposures discussed in Note 3, Outstanding Exposure, includes financial guaranty contracts that meet the definition of insurance contracts as well as those that meet the definition of a derivative under GAAP. Amounts presented in this note relate only to financial guaranty insurance contracts. See Note 9, Financial Guaranty Contracts Accounted for as Credit Derivatives for amounts that relate to CDS.

Accounting Policies

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 the contract was written on a direct basis, assumed from another financial guarantor under a reinsurance treaty, ceded to another insurer under a reinsurance treaty, or acquired in a business combination.

Premium receivables comprise the present value of contractual or expected future premium collections discounted using the risk-free rate. Unearned premium reserve represents deferred premium revenue, less claim payments and recoveries received that have not yet been recognized in the statement of operations (“contra-paid”). The following discussion relates to the deferred premium revenue component of the unearned premium reserve, while the contra-paid is discussed in Note 7, Financial Guaranty Insurance Losses.

The amount of deferred premium revenue at contract inception is determined as follows:

- For premiums received upfront on financial guaranty insurance contracts that were originally underwritten by the Company, deferred premium revenue 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 that were originally underwritten by the Company, deferred premium revenue is the present value of either (1) contractual premiums due or (2) in cases where the underlying collateral is comprised of homogeneous pools of assets, the expected premiums to be collected over the life of the contract. To be considered a homogeneous pool of assets, prepayments must be contractually prepayable, the amount of prepayments must be probable, and the timing and amount of prepayments must be reasonably estimable. When the Company adjusts prepayment assumptions or expected premium collections, an adjustment is recorded to the deferred premium revenue, with a corresponding adjustment to the premium receivable, and prospective changes are recognized in premium revenues. 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. 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.

- For financial guaranty insurance contracts subject to push-down accounting, deferred premium revenue is equal to the fair value of the Company's stand-ready obligation portion of the insurance contract at the date of acquisition based on what a hypothetical similarly rated financial guaranty insurer would have charged for the contract at that date and not the actual cash flows under the insurance contract. The amount of deferred premium revenue may differ significantly from cash collections due primarily to fair value adjustments recorded in connection with a business combination.

The Company recognizes deferred premium revenue as earned premium over the contractual period or expected period of the contract in proportion to the amount of insurance protection provided. As premium revenue is recognized, a corresponding decrease to the deferred premium revenue is recorded. The amount of insurance protection provided is a function of the insured principal 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 principal amounts outstanding in the reporting period compared with the sum of each of the insured principal amounts outstanding for all periods. When an insured financial obligation is retired before its maturity, the financial guaranty insurance contract is extinguished. Any nonrefundable deferred premium revenue 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.

Financial Guaranty Insurance Premiums

Deferred premium revenue ceded to reinsurers (ceded unearned premium reserve) is recorded as an asset. Direct, assumed and ceded earned premium revenue are presented together as net earned premiums in the statement of operations. Net earned premiums comprise the following:

Net Earned Premiums

	Year Ended December 31,	
	2014	2013
	(in millions)	
Scheduled net earned premiums	$ 278	$ 323
Acceleration of net earned premiums	88	176
Accretion of discount on net premiums receivable	8	9
Net earned premiums(1)	$ 374	$ 508

(1) Excludes $31 million and $58 million for the year ended December 31, 2014 and 2013, respectively, related to consolidated FG VIEs.

Components of Unearned Premium Reserve

	As of December 31, 2014			As of December 31, 2013		
	Gross	Ceded	Net(1)	Gross	Ceded	Net(1)
	(in millions)					
Deferred premium revenue	$ 3,331	$ 966	$ 2,365	$ 3,709	$ 1,071	$ 2,638
Contra-paid(2)	94	(8)	102	(57)	(24)	(33)
Unearned premium reserve	$ 3,425	$ 958	$ 2,467	$ 3,652	$ 1,047	$ 2,605

(1) Excludes $114 million and $177 million of deferred premium revenue, and $42 million and $55 million of contra-paid related to FG VIEs as of December 31, 2014 and December 31, 2013, respectively.

(2) See Note 7, "Financial Guaranty Insurance Losses- Insurance Contracts' Loss Information" for an explanation of "contra-paid".

Gross Premium Receivable
Roll Forward

	Year Ended December 31,	
	2014	2013
	(in millions)	
Beginning of period, December 31	$ 578	$ 653
Gross premium written	136	398
Gross premiums received	(192)	(455)
Adjustments:		
Changes in the expected term	(47)	(27)
Accretion of discount	3	14
Foreign exchange translation	(28)	1
Other adjustments	0	(6)
End of period, December 31(1)	$ 450	$ 578

(1) Excludes $6 million and $9 million as of December 31, 2014 and 2013, respectively, related to consolidated FG VIEs.

Foreign exchange translation relates to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 78% and 67% of installment premiums at December 31, 2014 and 2013, respectively, are denominated in currencies other than the U.S. dollar, primarily the Euro and British Pound Sterling.

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

Expected Collections of
Gross Premiums Receivable,
Net of Commissions on Assumed Business
(Undiscounted)

	As of December 31, 2014
	(in millions)
2015 (January 1 – March 31)	$ 18
2015 (April 1 – June 30)	17
2015 (July 1 – September 30)	12
2015 (October 1 – December 31)	11
2016	45
2017	42
2018	38
2019	36
2020-2024	145
2025-2029	101
2030-2034	73
After 2034	77
Total (1)	$ 615

(1) Excludes expected cash collections on FG VIEs of $8 million.

Scheduled Net Earned Premiums

	As of December 31, 2014
	(in millions)
2015 (January 1 – March 31)	$ 62
2015 (April 1 – June 30)	61
2015 (July 1 – September 30)	59
2015 (October 1 – December 31)	57
Subtotal 2015	239
2016	220
2017	191
2018	172
2019	156
2020-2024	597
2025-2029	368
2030-2034	218
After 2034	204
Total present value basis(1)	2,365
Discount	109
Total future value	$ 2,474

(1) Excludes scheduled net earned premiums on consolidated FG VIEs of $114 million.

Selected Information for Policies Paid in Installments

	As of December 31, 2014	As of December 31, 2013
	(dollars in millions)	
Premiums receivable, net of commission payable	$ 450	$ 578
Gross deferred premium revenue	1,097	1,278
Weighted-average risk-free rate used to discount premiums	3.6%	3.6%
Weighted-average period of premiums receivable (in years)	10.1	9.8

5. Financial Guaranty Insurance Acquisition Costs

Accounting Policy

Policy acquisition costs that are directly related and essential to successful insurance contract acquisition and ceding commission income on ceded reinsurance contracts are deferred for contracts accounted for as insurance and reported net. Amortization of deferred ceding commissions includes the accretion of discount on ceding commission income and expense. Acquisition costs associated with derivative contracts are not deferred.

These costs include expenses such as the cost of underwriting personnel attributable to successful underwriting efforts. 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 rates and included in deferred acquisition costs ("DAC"), with a corresponding offset to net premiums receivable or reinsurance balances payable. Management uses its judgment in determining the type and amount of costs to be deferred. The Company conducts an annual study to determine which operating costs qualify for deferral. 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. DAC, net of deferred ceding commission income, is amortized in proportion to net earned premiums. When an insured obligation is retired early, the remaining related DAC, net of ceding commission income is recognized at that time.

Expected losses and loss adjustment expenses (“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 Ceding Commissions,
Net of DAC(1)

	Year Ended December 31,	
	2014	2013
	(in millions)	
Beginning of period	$ (86)	$ (110)
Costs deferred during the period:		
Commissions on ceded business	(7)	(13)
Premium taxes	3	3
Compensation and other acquisition costs	7	7
Total	3	(3)
Costs amortized during the period	5	27
End of period	$ (78)	$ (86)

(1) The balances are included in other liabilities on the consolidated balance sheets.

6. Expected Loss to be Paid

The insured portfolio includes policies accounted for under three separate accounting models depending on the characteristics of the contract and the Company's control rights. The Company has paid and expects to pay future losses on policies which fall under each of the three accounting models. The following provides a summarized description of the three accounting models prescribed by GAAP with a reference to the notes that describe the accounting policies and required disclosures throughout this report. The three models are: (1) insurance, (2) derivative and (3) VIE consolidation.

In order to effectively evaluate and manage the economics and liquidity of the entire insured portfolio, management compiles and analyzes loss information for all policies on a consistent basis. The Company monitors and assigns ratings and calculates expected losses in the same manner for all its exposures regardless of form or differing accounting models.

This note provides information regarding expected claim payments to be made under all contracts in the insured portfolio. Net expected loss to be paid in the tables below consists of the present value of future: expected claim and LAE payments, expected recoveries of excess spread in the transaction structures, cessions to reinsurers, and expected recoveries for breaches of representations and warranties ("R&W") and other loss mitigation strategies. 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, regardless of the accounting model. Expected loss to be paid is an important measure used by management to analyze the net economic loss on all contacts.

Accounting Policy

Insurance Accounting

For contracts accounted for as financial guaranty insurance, loss and LAE reserve is recorded only to the extent and for the amount that expected losses to be paid exceed unearned premium reserve. As a result, the Company has expected loss to be paid that have not yet been expensed. Such amounts will be recognized in future periods as deferred premium revenue amortizes into income.Expected loss to be expensed is important because it presents the Company's projection of incurred losses that will be recognized in future periods (excluding accretion of discount). See Note 7, Financial Guaranty Insurance Losses.

Derivative Accounting, at Fair Value

For contracts that do not meet the financial guaranty scope exception in the derivative accounting guidance (primarily due to the fact that the insured is not required to be exposed to the insured risk throughout the life of the contract), the Company records such credit derivative contracts at fair value on the consolidated balance sheet with changes in fair value recorded in the consolidated statement of operations. The fair value recorded on the balance sheet represents an exit price in a hypothetical market because the Company does not trade its credit derivative contracts. The fair value is determined using significant Level 3 inputs in an internally developed model while the expected loss to be paid (which represents the net present value of expected cash outflows) uses methodologies and assumptions consistent with financial guaranty insurance expected losses to be paid. See Note 8, Fair Value Measurement and Note 9, Financial Guaranty Contracts Accounted for as Credit Derivatives.

VIE Consolidation, at Fair Value

For financial guaranty insurance contracts issued on the debt of variable interest entities over which the Company is deemed to be the primary beneficiary due to its control rights, as defined in GAAP, the Company consolidates the FG VIE. The Company carries the assets and liabilities of the FG VIEs at fair value under the fair value option election. Management assesses the losses on the insured debt of the consolidated FG VIEs in the same manner as other financial guaranty insurance and credit derivative contracts. See Note 10, Consolidated Variable Interest Entities.

Expected Loss to be Paid

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

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

Economic Loss Development

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

Expected loss to be paid and economic loss development include the effects of loss mitigation strategies such as negotiated and estimated recoveries for breaches of representations and warranties, and purchases of insured debt obligations.

In circumstances where the Company has purchased its own insured obligations that have expected losses, expected loss to be paid is reduced by the proportionate share of the insured obligation that is held in the investment portfolio. The difference between the purchase price of the obligation and the fair value excluding the value of the Company's insurance, is treated as a paid loss. Assets that are purchased by the Company are recorded in the investment portfolio, at fair value, excluding the value of the Company's insurance. See Note 11, Investments and Cash and Note 8, Fair Value Measurement.

Loss Estimation Process

The Company’s loss reserve committees estimate expected loss to be paid for all contracts. Surveillance personnel present analyses related to potential losses to the Company’s loss reserve committees for consideration in estimating the expected loss to be paid. Such analyses include the consideration of various scenarios with corresponding probabilities assigned to them. Depending upon the nature of the risk, the Company’s view of the potential size of any loss and the information available to the Company, that analysis may be based upon individually developed cash flow models, internal credit rating assessments and sector-driven loss severity assumptions or judgmental assessments. The Company’s loss reserve committees review and refresh the estimate of expected loss to be paid each quarter. The Company’s estimate of ultimate loss on a policy is subject to significant uncertainty over the life of the insured transaction due to the potential for significant variability in credit performance as a result of economic, fiscal and financial market variability over the long duration of most contracts. The determination of expected loss to be paid is an inherently subjective process involving numerous estimates, assumptions and judgments.

The following tables present a roll forward of the present value of net expected loss to be paid for all contracts, whether accounted for as insurance, credit derivatives or FG VIEs, by sector, before and after the benefit for net expected recoveries for contractual breaches of R&W. The Company used weighted average risk-free rates for U.S. dollar denominated obligations that ranged from 0.0% to 2.95% as of December 31, 2014 and 0.0% to 4.44% as of December 31, 2013.

Net Expected Loss to be Paid,
Before Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Year Ended December 31, 2014

	Net Expected Loss to be Paid (Recovered) as of December 31, 2013(2)	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid (Recovered) as of December 31, 2014(2)
		(in millions)		
U.S. RMBS:				
First lien:				
Alt-A first lien	$ 261	$ 20	$ (26)	$ 255
Option ARM	94	(41)	(83)	(30)
Subprime	339	37	(45)	331
Total first lien	694	16	(154)	556
Second lien:				
Closed-end second lien	62	2	10	74
HELOCs	(63)	30	13	(20)
Total second lien	(1)	32	23	54
Total U.S. RMBS	693	48	(131)	610
Other structured finance	27	(2)	(1)	24
U.S. public finance	61	97	(16)	142
Non-U.S. public finance	42	(8)	—	34
Total	$ 823	$ 135	$ (148)	$ 810

Net Expected Loss to be Paid,
Before Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Year Ended December 31, 2013

	Net Expected Loss to be Paid (Recovered) as of December 31, 2012	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid (Recovered) as of December 31, 2013(2)
	(in millions)			
U.S. RMBS:				
First lien:				
Alt-A first lien	$ 281	$ 19	$ (39)	$ 261
Option ARM	339	56	(301)	94
Subprime	269	85	(15)	339
Total first lien	889	160	(355)	694
Second lien:				
Closed-end second lien	66	(1)	(3)	62
HELOCs	(3)	19	(79)	(63)
Total second lien	63	18	(82)	(1)
Total U.S. RMBS	952	178	(437)	693
Other structured finance	28	—	(1)	27
U.S. public finance	(58)	89	30	61
Non-U.S. public finance	38	11	(7)	42
Total	$ 960	$ 278	$ (415)	$ 823

(1) Net of ceded paid losses, whether or not such amounts have been settled with reinsurers. Ceded paid losses are typically settled 45 days after the end of the reporting period. Such amounts are recorded in reinsurance recoverable on paid losses included in other assets. The Company paid $23 million and $35 million in LAE for the years ended December 31, 2014 and 2013, respectively.

(2) Includes expected LAE to be paid of $4 million as of December 31, 2014 and $15 million as of December 31, 2013.

Net Expected Recoveries from
Breaches of R&W Rollforward
Year Ended December 31, 2014

	Future Net R&W Benefit as of December 31, 2013	R&W Development and Accretion of Discount During 2014	R&W (Recovered) During 2014	Future Net R&W Benefit as of December 31, 2014 (1)
	(in millions)			
Alt-A first lien	$ 78	$ 93	(153)	$ 18
Option ARM	98	(7)	(102)	(11)
Subprime	117	49	(58)	108
Closed-end second lien	82	—	(6)	76
HELOCs	45	72	(117)	—
Total	$ 420	$ 207	$ (436)	$ 191

Net Expected Recoveries from
Breaches of R&W Rollforward
Year Ended December 31, 2013

	Future Net R&W Benefit as of December 31, 2012	R&W Development and Accretion of Discount During 2013	R&W (Recovered) During 2013	Future Net R&W Benefit as of December 31, 2013
		(in millions)		
Alt-A first lien	$ 132	$ 66	(120)	$ 78
Option ARM	481	173	(556)	98
Subprime	107	10	—	117
Closed-end second lien	115	(9)	(24)	82
HELOCs	125	68	(148)	45
Total	$ 960	$ 308	$ (848)	$ 420

____

(1) See the section "Breaches of Representations and Warranties" below for eligible assets held in trust.

Net Expected Loss to be Paid,
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Year Ended December 31, 2014

	Net Expected Loss to be Paid (Recovered) as of December 31, 2013	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid (Recovered) as of December 31, 2014
		(in millions)		
U.S. RMBS:				
First lien:				
Alt-A first lien	$ 183	$ (73)	$ 127	$ 237
Option ARM	(4)	(34)	19	(19)
Subprime	222	(12)	13	223
Total first lien	401	(119)	159	441
Second lien:				
Closed-end second lien	(20)	2	16	(2)
HELOCs	(108)	(42)	130	(20)
Total second lien	(128)	(40)	146	(22)
Total U.S. RMBS	273	(159)	305	419
Other structured finance	27	(2)	(1)	24
U.S. public finance	61	97	(16)	142
Non-U.S. public finance	42	(8)	—	34
Total	$ 403	$ (72)	$ 288	$ 619

Net Expected Loss to be Paid,
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Year Ended December 31, 2013

	Net Expected Loss to be Paid (Recovered) as of December 31, 2012	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid (Recovered) as of December 31, 2013
		(in millions)		
U.S. RMBS:				
First lien:				
Alt-A first lien	$ 149	$ (47)	$ 81	$ 183
Option ARM	(142)	(117)	255	(4)
Subprime	162	75	(15)	222
Total first lien	169	(89)	321	401
Second lien:				
Closed-end second lien	(49)	8	21	(20)
HELOCs	(128)	(49)	69	(108)
Total second lien	(177)	(41)	90	(128)
Total U.S. RMBS	(8)	(130)	411	273
Other structured finance	28	—	(1)	27
U.S. public finance	(58)	89	30	61
Non-U.S. public finance	38	11	(7)	42
Total	$ 0	$ (30)	$ 433	$ 403

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

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

Net Expected Loss to be Paid (Recovered)
By Accounting Model
As of December 31, 2014

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives (2)	Total
		(in millions)		
U.S. RMBS:				
First lien:				
Alt-A first lien	$ 220	$ 17	$ —	$ 237
Option ARM	(19)	—	—	(19)
Subprime	153	70	—	223
Total first lien	354	87	—	441
Second lien:				
Closed-end second lien	(31)	25	4	(2)
HELOCs	(27)	7	—	(20)
Total second lien	(58)	32	4	(22)
Total U.S. RMBS	296	119	4	419
Other structured finance	22	—	2	24
U.S. public finance	142	—	—	142
Non-U.S. public finance	34	—	—	34
Total	$ 494	$ 119	$ 6	$ 619

Net Expected Loss to be Paid (Recovered)
By Accounting Model
As of December 31, 2013

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives (2)	Total
		(in millions)		
U.S. RMBS:				
First lien:				
Alt-A first lien	$ 164	$ 19	$ —	$ 183
Option ARM	(3)	(1)	—	(4)
Subprime	141	81	—	222
Total first lien	302	99	—	401
Second lien:				
Closed-end second lien	(36)	18	(2)	(20)
HELOCs	(33)	(75)	—	(108)
Total second lien	(69)	(57)	(2)	(128)
Total U.S. RMBS	233	42	(2)	273
Other structured finance	22	—	5	27
U.S. public finance	61	—	—	61
Non-U.S. public finance	42	—	—	42
Total	$ 358	$ 42	$ 3	$ 403

(1) Refer to Note 10, Consolidated Variable Interest Entities.

(2) Refer to Note 9, Financial Guaranty Contracts Accounted for as Credit Derivatives.

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

Net Economic Loss Development (Benefit)
By Accounting Model
Year Ended December 31, 2014

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
		(in millions)		
U.S. RMBS:				
First lien:				
Alt-A first lien	$ (72)	$ (1)	$ —	$ (73)
Option ARM	(35)	1	—	(34)
Subprime	(19)	7	—	(12)
Total first lien	(126)	7	—	(119)
Second lien:				
Closed-end second lien	(2)	7	(3)	2
HELOCs	(125)	83	—	(42)
Total second lien	(127)	90	(3)	(40)
Total U.S. RMBS	(253)	97	(3)	(159)
Other structured finance	1	—	(3)	(2)
U.S. public finance	97	—	—	97
Non-U.S. public finance	(8)	—	—	(8)
Total	$ (163)	$ 97	$ (6)	$ (72)

Net Economic Loss Development (Benefit)
By Accounting Model
Year Ended December 31, 2013

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
		(in millions)		
U.S. RMBS:				
First lien:				
Alt-A first lien	$ (49)	$ 2	$ —	$ (47)
Option ARM	(79)	(37)	(1)	(117)
Subprime	43	33	(1)	75
Total first lien	(85)	(2)	(2)	(89)
Second lien:				
Closed-end second lien	3	(5)	10	8
HELOCs	(22)	(27)	—	(49)
Total second lien	(19)	(32)	10	(41)
Total U.S. RMBS	(104)	(34)	8	(130)
Other structured finance	(1)	—	1	—
U.S. public finance	89	—	—	89
Non-U.S. public finance	11	—	—	11
Total	$ (5)	$ (34)	$ 9	$ (30)

____

(1) Refer to Note 10, Consolidated Variable Interest Entities.

(2) Refer to Note 9, Financial Guaranty Contracts Accounted for as Credit Derivatives.

Approach to Projecting Losses in U.S. RMBS

The Company projects losses on its insured U.S. RMBS on a transaction-by-transaction basis by projecting the performance of the underlying pool of mortgages over time and then applying the structural features (i.e., payment priorities and tranching) of the RMBS to the projected performance of the collateral over time. The resulting projected claim payments or reimbursements are then discounted using risk-free rates. For transactions where the Company projects it will receive recoveries from providers of R&W, it projects the amount of recoveries and either establishes a recovery for claims already paid or reduces its projected claim payments accordingly.

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

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

amount of the whole pool of loans (or “collateral pool balance”). The collateral pool balance decreases over time as a result of scheduled principal payments, partial and whole principal prepayments, and defaults.

In order to derive collateral pool losses from the collateral pool defaults it has projected, the Company applies a loss severity. The loss severity is the amount of loss the transaction experiences on a defaulted loan after the application of net proceeds from the disposal of the underlying property. The Company projects loss severities by sector based on its experience to date. The Company continues to update its evaluation of these exposures as new information becomes available.

The Company has been enforcing claims for breaches of R&W regarding the characteristics of the loans included in the collateral pools. The Company calculates a credit for R&W recoveries to include in its cash flow projections. Where the Company has an agreement with an R&W provider (such as its agreements with Bank of America, Deutsche Bank and UBS, which are described in more detail under "Breaches of Representations and Warranties" below), that credit is based on the agreement or potential agreement. Where the Company does not have an agreement with the R&W provider but the Company believes the R&W provider to be economically viable, the Company estimates what portion of its past and projected future claims it believes will be reimbursed by that provider.

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

The ultimate performance of the Company’s RMBS transactions remains highly uncertain, may differ from the Company's projections and may be subject to considerable volatility due to the influence of many interrelated factors that are difficult to predict, including the level and timing of loan defaults, changes in housing prices, results from the Company’s loss mitigation activities and other variables. The Company will continue to monitor the performance of its RMBS exposures and will adjust its RMBS loss projection assumptions and scenarios based on actual performance and management’s view of future performance. If actual experience differs from the Company’s assumptions, the losses incurred could be materially different from the estimate.

The Company's RMBS loss projection methodology assumes that the housing and mortgage markets will continue improving. Each period the Company makes a judgment as to whether to change the assumptions it uses to make RMBS loss projections based on its observation during the period of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, and, to the extent it observes changes, it makes a judgment as whether those changes are normal fluctuations or part of a trend.

Year-End 2014 Compared to Year-End 2013 U.S. RMBS Loss Projections

Based on its observations of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general methodology to project first lien RMBS losses as of December 31, 2014 as it used as of December 31, 2013, but it made a number of refinements to reflect its observations, notably:

- updated the liquidation rates it uses on delinquent loans based on observations and on an assumption that loan modifications (which improve liquidation rates) would over the next year be less frequent than they were over the most recent year

- updated the liquidation rate it uses for loans reported as current but that had been reported as modified over the previous twelve months, based on observed data

- established a liquidation rate assumption for loans reported as current and not modified in the past twelve months but that had been reported as delinquent in the previous twelve months

- established loss severity assumptions by vintage category as well as product type, rather than just product type as done previously

- beginning with the third quarter 2014, each quarter shortened by three months the period it is projecting it will take in the base case to reach the final CDR

The methodology and revised assumptions the Company uses to project first lien RMBS losses and the scenarios it employs are described in more detail below under " - U.S. First Lien RMBS Loss Projections: Alt A First Lien, Option ARM and Subprime". The Company estimated the impact of all of the refinements to its first lien RMBS assumptions described above to be a decrease of expected losses (gross of reinsurance) of approximately $28 million (before adjustments for settlements or loss mitigation purchases).

Based on its observations of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general methodology to project second lien RMBS losses as of December 31, 2014 as it used as of December 31, 2013, but it made a number of refinements to reflect its observations, notably with respect to most HELOC projections to:

- reflect increased recoveries on newly defaulted loans as well as previously defaulted loans

- project incremental defaults associated with increased monthly payments that occur when interest-only periods end

- increase the assumed final conditional prepayment rate ("CPR") from 10% to 15%

The net impact of the refinements in the first two bullet points, which were implemented in the third quarter 2014, was an increase of approximately $30 million in expected losses (gross of reinsurance) in the Company's base case as of September 30, 2014. The net impact of the refinements in the third bullet point was an increase of approximately $12 million in expected losses (gross of reinsurance) in the Company's base case as of December 31, 2014.

The methodology and assumptions the Company uses to project second lien RMBS losses and the scenarios it employs are described in more detail below under " - U.S. Second Lien RMBS Loss Projections: HELOCs and Closed-End Second Lien".

Year-End 2013 Compared to Year-End 2012 U.S. RMBS Loss Projections

Based on the Company's observation during the year of the performance of its insured RMBS transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general methodology (with the refinements described below) to project RMBS losses as of December 31, 2013 as it used as of December 31, 2012. The Company's use of the same general approach to project RMBS losses as of December 31, 2013 as it used as of December 31, 2012 was consistent with its view at December 31, 2013 that the housing and mortgage market recovery was occurring at a slower pace than it anticipated at December 31, 2012.

The Company refined its first lien RMBS loss projection methodology as of December 31, 2013 to model explicitly the behavior of borrowers with loans that had been modified. The Company has observed that mortgage loan servicers were modifying more mortgage loans (reducing or forbearing from collecting interest or principal or both due on mortgage loans) to reduce the borrowers' monthly payments and so improve their payment performance than was the case before the mortgage crisis. Borrowers who are current based on their new, reduced monthly payments are generally reported as current, but are more likely to default than borrowers who are current and whose loans have not been modified. The Company believes modified loans are most likely to default again during the first year after modification. The Company set its liquidation rate assumptions as of December 31, 2012 based on observed roll rates and with modification activity in mind. As of December 31, 2013 the Company made a number of refinements to its first lien RMBS loss projection assumptions to treat loan modifications explicitly. Specifically, in the base case approach, it:

- established a liquidation rate assumption for loans reported as current but that had been reported as modified in the previous 12 months,

- assumed that currently delinquent loans that did not roll to liquidation would behave like modified loans, and so applied the modified loan liquidation rate to them,

- increased from two to three years the period over which it calculates the initial CDR based on assumed liquidations of non-performing loans and modified loans, to account for the longer period modified loans will take to default,

- increased the period it assumes the transactions will experience the initial loss severity assumption before it improves and the period during which the transaction will experience low voluntary prepayment rates,

- established an assumption for servicers not to advance loan payments on all delinquent loans

The methodology and revised assumptions the Company uses to project first lien RMBS losses and the scenarios it employs are described in more detail below under " - U.S. First Lien RMBS Loss Projections: Alt A First Lien, Option ARM and Subprime". The refinement in assumptions described above resulted in a reduction of the initial CDRs but the application of the initial CDRs for a longer period, which generally resulted in a higher amount of loans being liquidated at the initial CDR under the refined assumptions than under the initial CDR under the previous assumptions. The Company estimated the impact of all of the refinements to its assumptions described above to be an increase of expected losses of approximately $2 million (before adjustments for settlements or loss mitigation purchases) by running on the first lien RMBS portfolio as of December 31, 2013 base case assumptions similar to what it used as of December 31, 2012 and comparing those results to those results from the refined assumptions.

During 2013 the Company observed improvements in the performance of its second lien RMBS transactions that, when viewed in the context of their performance prior to 2013, suggested those transactions were beginning to respond to the improvements in the residential property market and economy being widely reported by market observers. Based on such observations, in projecting losses for second lien RMBS the Company chose to decrease by two months in its base scenario and by three months in its optimistic scenario the period it assumed it would take the mortgage market to recover as compared to December 31, 2012. Also during 2013 the Company observed material improvements in the delinquency measures of certain second lien RMBS for which the servicing had been transferred, and made certain adjustments on just those transactions to reflect its view that much of this improvement was due to loan modifications and reinstatements made by the new servicer and that such recently modified and reinstated loans may have a higher likelihood of defaulting again. The methodology and assumptions the Company used to project second lien RMBS losses and the scenarios it employed are described in more detail below under " - U.S. Second Lien RMBS Loss Projections: HELOCs and Closed-End Second Lien".

The Company observed some improvement in delinquency trends in most of its RMBS transactions during 2013, with some of that improvement in second liens driven by servicing transfers it effectuated. Such improvement is naturally transmitted to its projections for each individual RMBS transaction, since the projections are based on the delinquency performance of the loans in that individual transaction.

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

The majority of projected losses in first lien RMBS transactions are expected to come from non-performing mortgage loans (those that have been modified or have been delinquent in the previous 12 months, are two or more payments behind, are in foreclosure or that have been foreclosed and so the RMBS issuer owns the underlying real estate). Changes in the amount of non-performing loans from the amount projected in the previous period are one of the primary drivers of loss development in this portfolio. In order to determine the number of defaults resulting from these delinquent and foreclosed loans, the Company applies a liquidation rate assumption to loans in each of various non-performing categories. The Company arrived at its liquidation rates based on data purchased from a third party provider and assumptions about how delays in the foreclosure process and loan modifications may ultimately affect the rate at which loans are liquidated. Each year the Company reviews the most recent twenty-four months of this data and adjusts its liquidation rates based on its observations. The following table shows liquidation assumptions for various non-performing categories.

First Lien Liquidation Rates

	December 31, 2014	December 31, 2013
Current Loans Modified in Previous 12 Months		
Alt-A	25%	35%
Option ARM	25	35
Subprime	25	35
Current Loans Delinquent in the Previous 12 Months		
Alt-A	25	N/A
Option ARM	25	N/A
Subprime	25	N/A
30 - 59 Days Delinquent		
Alt-A	35	50
Option ARM	40	50
Subprime	35	45
60 - 89 Days Delinquent		
Alt-A	50	60
Option ARM	55	65
Subprime	40	50
90 + Days Delinquent		
Alt-A	60	75
Option ARM	65	70
Subprime	55	60
Bankruptcy		
Alt-A	45	60
Option ARM	50	60
Subprime	40	55
Foreclosure		
Alt-A	75	85
Option ARM	80	80
Subprime	70	70
Real Estate Owned		
All	100	100

While the Company uses liquidation rates as described above to project defaults of non-performing loans (including current loans modified or delinquent within the last 12 months), it projects defaults on presently current loans by applying a CDR trend. The start of that CDR trend is based on the defaults the Company projects will emerge from currently nonperforming, recently nonperforming and modified loans. The total amount of expected defaults from the non-performing loans is translated into a constant CDR (*i.e.*, the CDR plateau), which, if applied for each of the next 36 months, would be sufficient to produce approximately the amount of defaults that were calculated to emerge from the various delinquency categories. The CDR thus calculated individually on the delinquent collateral pool for each RMBS is then used as the starting point for the CDR curve used to project defaults of the presently performing loans.

In the base case, after the initial 36-month CDR plateau period, each transaction's CDR is projected to improve over 12 months to an intermediate CDR (calculated as 20% of its CDR plateau); that intermediate CDR is held constant for 36 months and then trails off in steps to a final CDR of 5% of the CDR plateau. In the base case, the Company assumes the final CDR will be reached eight years and six months after the initial 36-month CDR plateau period, which is six months shorter than assumed as of December 31, 2013 but the same calendar date as it assumed as of June 30, 2014. Under the Company's methodology, defaults projected to occur in the first 36 months represent defaults that can be attributed to loans that were modified or delinquent in the last 12 months or that are currently delinquent or in foreclosure, while the defaults projected to occur using the projected CDR trend after the first 36 month period represent defaults attributable to borrowers that are currently performing or are projected to reperform.

Another important driver of loss projections is loss severity, which is the amount of loss the transaction incurs on a loan after the application of net proceeds from the disposal of the underlying property. Loss severities experienced in first lien transactions have reached historic high levels, and the Company is assuming in the base case that these high levels generally will continue for another 18 months. The Company determines its initial loss severity based on actual recent experience. The Company then assumes that loss severities begin returning to levels consistent with underwriting assumptions beginning after the initial 18 month period, declining to 40% in the base case over 2.5 years. Beginning for December 31, 2014, the Company differentiated the loss severity assumptions depending on the vintage of the transaction, as shown in the table below.

The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions used in the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 first lien U.S. RMBS.

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

	As of December 31, 2014		As of December 31, 2013	
	Range	Weighted Average	Range	Weighted Average
Alt-A First Lien				
Plateau CDR	3.7% - 13.4%	9.3%	5.1% - 18.4%	12.3%
Intermediate CDR	0.7% - 2.7%	1.9%	1.0% - 3.7%	2.5%
Period until intermediate CDR	48 months		48 months	
Final CDR	0.2% - 0.7%	0.5%	0.3% - 0.9%	0.6%
Initial loss severity:				
2005 and prior	60%		65%	
2006	70%		65%	
2007	65%		65%	
Initial CPR	1.7% - 9.5%	5.1%	0.0% - 18.4%	7.2%
Final CPR(2)	15%		15%	
Option ARM				
Plateau CDR	4.3% - 14.2%	10.9%	4.9% - 16.8%	13.9%
Intermediate CDR	0.9% - 2.8%	2.2%	1.0% - 3.4%	2.8%
Period until intermediate CDR	48 months		48 months	
Final CDR	0.2% - 0.7%	0.5%	0.2% - 0.8%	0.7%
Initial loss severity:				
2005 and prior	60%		65%	
2006	70%		65%	
2007	65%		65%	
Initial CPR	2.3% - 6.2%	3.3%	1.2% - 10.4%	5.0%
Final CPR(2)	15%		15%	
Subprime				
Plateau CDR	6.0% - 15.0%	10.8%	7.2% - 16.2%	12.0%
Intermediate CDR	1.2% - 3.0%	2.2%	1.4% - 3.2%	2.4%
Period until intermediate CDR	48 months		48 months	
Final CDR	0.3% - 0.7%	0.5%	0.4% - 0.8%	0.6%
Initial loss severity:				
2005 and prior	75%		90%	
2006	90%		90%	
2007	90%		90%	
Initial CPR	0.1% - 5.3%	3.4%	0.0% - 8.0%	4.2%
Final CPR(2)	15%		15%	

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

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

The rate at which the principal amount of loans is voluntarily prepaid may impact both the amount of losses projected (since that amount is a function of the conditional default rate, the loss severity and the loan balance over time) as well as the amount of excess spread (the amount by which the interest paid by the borrowers on the underlying loan exceeds the amount of interest owed on the insured obligations). The assumption for the voluntary CPR follows a similar pattern to that of the

conditional default rate. The current level of voluntary prepayments is assumed to continue for the plateau period before gradually increasing over 12 months to the final CPR, which is assumed to be 15% in the base case. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. These assumptions are the same as those the Company used for December 31, 2013.

In estimating expected losses, the Company modeled and probability weighted sensitivities for first lien transactions by varying its assumptions of how fast a recovery is expected to occur. One of the variables used to model sensitivities was how quickly the conditional default rate returned to its modeled equilibrium, which was defined as 5% of the initial conditional default rate. The Company also stressed CPR and the speed of recovery of loss severity rates. The Company probability weighted a total of five scenarios (including its base case) as of December 31, 2014. The Company used a similar approach to establish its pessimistic and optimistic scenarios as of December 31, 2014 as it used as of December 31, 2013, increasing and decreasing the periods of stress from those used in the base case.

In a somewhat more stressful environment than that of the base case, where the conditional default rate plateau was extended six months (to be 42 months long) before the same more gradual conditional default rate recovery and loss severities were assumed to recover over 4.5 rather than 2.5 years (and subprime loss severities were assumed to recover only to 60% and Option ARM and Alt A loss severities to only 45%), expected loss to be paid would increase from current projections by approximately $15 million for Alt-A first liens, $4 million for Option ARM and $52 million for subprime transactions.

In an even more stressful scenario where loss severities were assumed to rise and then recover over nine years and the initial ramp-down of the conditional default rate was assumed to occur over 15 months and other assumptions were the same as the other stress scenario, expected loss to be paid would increase from current projections by approximately $38 million for Alt-A first liens, $9 million for Option ARM and $73 million for subprime transactions.

In a scenario with a somewhat less stressful environment than the base case, where conditional default rate recovery was somewhat less gradual, expected loss to be paid would increase from current projections by approximately $1 million for Alt-A first lien and would decrease approximately $11 million for Option ARM and $11 million for subprime transactions.

In an even less stressful scenario where the conditional default rate plateau was six months shorter (30 months, effectively assuming that liquidation rates would improve) and the conditional default rate recovery was more pronounced, (including an initial ramp-down of the conditional default rate over nine months), expected loss to be paid would decrease from current projections by approximately $12 million for Alt-A first liens, $19 million for Option ARM and $43 million for subprime transactions.

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

The Company believes the primary variable affecting its expected losses in second lien RMBS transactions is the amount and timing of future losses in the collateral pool supporting the transactions. Expected losses are also a function of the structure of the transaction; the voluntary prepayment rate (typically also referred to as CPR of the collateral); the interest rate environment; and assumptions about the draw rate and loss severity.

The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions for the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 second lien U.S. RMBS.

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

HELOC key assumptions	**As of December 31, 2014**		**As of December 31, 2013**	
	Range	**Weighted Average**	**Range**	**Weighted Average**
Plateau CDR	2.8% - 6.8%	4.1%	2.3% - 7.7%	4.9%
Final CDR trended down to	0.6% - 3.2%	1.2%	0.4% - 3.2%	1.1%
Period until final CDR	34 months		34 months	
Initial CPR	6.9% - 21.8%	10.8%	2.7% - 17.9%	9.9%
Final CPR(2)	15.0% - 21.8%	15.6%	10%	
Loss severity	90% - 98%	90.3%	98%	

Closed-end second lien key assumptions	**As of December 31, 2014**		**As of December 31, 2013**	
	Range	**Weighted Average**	**Range**	**Weighted Average**
Plateau CDR	6.1% - 12.5%	7.3%	7.5% - 15.1%	8.2%
Final CDR trended down to	3.5% - 8.6%	4.0%	3.5% - 8.6%	4.0%
Period until final CDR	34 months		34 months	
Initial CPR	2.8% - 13.1%	10.1%	3.1% - 9.4%	7.9%
Final CPR(2)	15%		10%	
Loss severity	98%		98%	

____

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

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

In second lien transactions the projection of near-term defaults from currently delinquent loans is relatively straightforward because loans in second lien transactions are generally "charged off" (treated as defaulted) by the securitization's servicer once the loan is 180 days past due. Most second lien transactions report the amount of loans in five monthly delinquency categories (*i.e.*, 30-59 days past due, 60-89 days past due, 90-119 days past due, 120-149 days past due and 150-179 days past due). The Company estimates the amount of loans that will default over the next five months by calculating current representative liquidation rates (the percent of loans in a given delinquency status that are assumed to ultimately default) from selected representative transactions and then applying an average of the preceding twelve months' liquidation rates to the amount of loans in the delinquency categories. The amount of loans projected to default in the first through fifth months is expressed as a CDR. The first four months' CDR is calculated by applying the liquidation rates to the current period past due balances (i.e., the 150-179 day balance is liquidated in the first projected month, the 120-149 day balance is liquidated in the second projected month, the 90-119 day balance is liquidated in the third projected month and the 60-89 day balance is liquidated in the fourth projected month). For the fifth month the CDR is calculated using the average 30-59 day past due balances for the prior three months, adjusted as necessary to reflect one-time service events. The fifth month CDR is then used as the basis for the plateau period that follows the embedded five months of losses.

For the base case scenario, the CDR (the "plateau CDR") was held constant for one month. Once the plateau period has ended, the CDR is assumed to gradually trend down in uniform increments to its final long-term steady state CDR. (The long-term steady state CDR is calculated as the constant CDR that would have yielded the amount of losses originally expected at underwriting.) In the base case scenario, the time over which the CDR trends down to its final CDR is 28 months. Therefore, the total stress period for second lien transactions is 34 months, comprising five months of delinquent data, a one month plateau period and 28 months of decrease to the steady state CDR, the same as of December 31, 2013.

HELOC loans generally permit the borrower to pay only interest for an initial period (often ten years) and, after that period, require the borrower to make both the monthly interest payment and a monthly principal payment, and so increase the borrower's aggregate monthly payment. Some of the HELOC loans underlying the Company's insured HELOC transactions have reached their principal amortization period. Based on the Company's observation, including information obtained over the last year on the performance of certain loans reaching their principal amortization period and its views of the efficacy of planned servicer intervention, it introduced this year an assumption in the projections for most of its HELOC transactions that 7.5% of loans reaching their amortization periods will default around the time of the payment increase. These projected defaults are in addition to those generated using the CDR curve as described above.

When a second lien loan defaults, there is generally a very low recovery. The Company had assumed as of December 31, 2013 that it will recover only 2% of the collateral defaulting. However, based on additional information the Company obtained over the last year, it increased this recovery assumption in the projections for most of its HELOC transactions as of December 31, 2014 to 10% of collateral defaulting in the future, and also assumed declining additional post-default receipts on previously defaulted collateral.

The rate at which the principal amount of loans is prepaid may impact both the amount of losses projected as well as the amount of excess spread. In the base case, the current CPR (based on experience of the most recent three quarters) is assumed to continue until the end of the plateau before gradually increasing to the final CPR over the same period the CDR decreases. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. The final CPR is assumed to be 15% for both HELOC and closed-end second lien transactions, which is lower than the historical average but reflects the Company's continued uncertainty about the projected performance of the borrowers in these transactions. This pattern is consistent with how the Company modeled the CPR at December 31, 2013. To the extent that prepayments differ from projected levels it could materially change the Company's projected excess spread and losses.

The net impact of the three refinements the Company made to projecting expected losses in certain HELOC transactions described above (increased defaults of loans reaching their amortization period, increased recoveries, decreased the redefault rate on modified loans and the increase in the final CPR to 15%) was an increase of approximately $42 million in expected losses (gross of reinsurance) in the Company's base case as of December 31, 2014 compared to what it would have been without the refinements. The Company uses a number of other variables in its second lien loss projections, including the spread between relevant interest rate indices and HELOC draw rates (the amount of new advances provided on existing HELOCs expressed as a percentage of the current pool balance). These variables have been relatively stable for well over a year and in the relevant ranges have less impact on the projection results than the variables discussed above. However, in a number of HELOC transactions the servicers have been modifying poorly performing loans from floating to fixed rates, and, as a result, rising interest rates would negatively impact the excess spread available from these modified loans to support the transactions. The Company incorporated these modifications in its assumptions.

In estimating expected losses, the Company modeled and probability weighted three possible CDR curves applicable to the period preceding the return to the long-term steady state CDR using the same approaches and weightings as it did as of December 31, 2013. The Company believes that the level of the elevated CDR and the length of time it will persist is the primary driver behind the likely amount of losses the collateral will suffer. The Company continues to evaluate the assumptions affecting its modeling results.

The Company's base case assumed a one month CDR plateau and a 28 month ramp-down (for a total stress period of 34 months). The Company also modeled a scenario with a longer period of elevated defaults and another with a shorter period of elevated defaults. Increasing the CDR plateau to four months and increasing the ramp-down by five months to 33-months (for a total stress period of 42 months) would increase the expected loss by approximately $10 million for HELOC transactions and $1 million for closed-end second lien transactions. On the other hand, keeping the CDR plateau at one month but decreasing the length of the CDR ramp-down to 18 months (for a total stress period of 24 months) would decrease the expected loss by approximately $10 million for HELOC transactions and $1 million for closed-end second lien transactions.

Breaches of Representations and Warranties

Generally, when mortgage loans are transferred into a securitization, the loan originator(s) and/or sponsor(s) provide R&W that the loans meet certain characteristics, and a breach of such R&W often requires that the loan be repurchased from the securitization. In many of the transactions the Company insures, it is in a position to enforce these R&W provisions. The Company has pursued breaches of R&W on a loan-by-loan basis or in cases where a provider of R&W refused to honor its repurchase obligations, the Company sometimes chose to initiate litigation. See "Recovery Litigation" below. The Company's success in pursuing these strategies permitted the Company to enter into agreements with R&W providers under which those

providers made payments to the Company, agreed to make payments to the Company in the future, and / or repurchased loans from the transactions, all in return for releases of related liability by the Company. Through December 31, 2014 the Company has caused entities providing R&Ws to pay, or agree to pay approximately $3.3 billion (gross of reinsurance) in respect of their R&W liabilities for transactions in which the Company has provided insurance, and has included in its net expected loss estimates as of December 31, 2014 an estimated net benefit of $191 million (net of reinsurance) projected to be received pursuant to existing agreements with R&W providers. Most of the amount projected to be received pursuant to existing agreements with R&W providers benefits from eligible assets placed in trusts to collateralize the R&W provider's future reimbursement obligation, with the amount of such collateral subject to increase or decrease from time to time as determined by rating agency requirements. Currently the Company has agreements with three counterparties where a future reimbursement obligation is collateralized by eligible assets held in trust:

- **Bank of America**. Under Assured Guaranty's agreement with Bank of America Corporation and certain of its subsidiaries ("Bank of America"), Bank of America agreed to reimburse Assured Guaranty for 80% of claims on the first lien transactions covered by the agreement that Assured Guaranty pays in the future, until the aggregate lifetime collateral losses (not insurance losses or claims) on those transactions reach $6.6 billion. As of December 31, 2014, aggregate lifetime collateral losses on those transactions was $4.1 billion ($3.8 billion for AGM and $0.3 billion for AGC), and Assured Guaranty was projecting in its base case that such collateral losses would eventually reach $5.1 billion ($4.7 billion for AGM and $0.4 billion for AGC). Bank of America's reimbursement obligation is secured by $136 million of collateral held in trust for the Company's benefit and $361 million of collateral held in trust that is available for either AGM or AGC.

- **Deutsche Bank.** Under Assured Guaranty's May 2012 agreement with Deutsche Bank AG and certain of its affiliates (collectively, "Deutsche Bank"), Deutsche Bank agreed to reimburse Assured Guaranty for certain claims it pays in the future on eight first and second lien transactions, including 80% of claims it pays on those transactions until the aggregate lifetime claims (before reimbursement) reach $319 million. As of December 31, 2014, Assured Guaranty was projecting in its base case that such aggregate lifetime claims would remain below $319 million. In the event aggregate lifetime claims paid exceed $389 million, Deutsche Bank must reimburse Assured Guaranty for 85% of such claims paid (in excess of $389 million) until such claims paid reach $600 million. Deutsche Bank's obligation to reimburse AGM is secured by $61 million of collateral held in trust for AGM's benefit and $0.7 million of collateral held in trust that is available for either AGM or AGC.

- **UBS.** On May 6, 2013, Assured Guaranty entered into an agreement with UBS Real Estate Securities Inc. and affiliates ("UBS") and a third party resolving Assured Guaranty's claims and liabilities related to specified RMBS transactions that were issued, underwritten or sponsored by UBS and insured by AGM or AGC under financial guaranty insurance policies. Under the agreement, UBS agreed to reimburse AGM for 85% of future losses on three first lien RMBS transactions, and such reimbursement obligation is secured by $109 million of collateral held in trust for the Company's benefit.

The Company uses the same RMBS projection scenarios and weightings to project its future R&W benefit as it uses to project RMBS losses on its portfolio. To the extent the Company increases its loss projections, the R&W benefit (whether pursuant to an R&W agreement) generally will also increase, subject to the agreement limits and thresholds described above. Similarly, to the extent the Company decreases its loss projections, the R&W benefit generally will also decrease, subject to the agreement limits and thresholds described above.

The number of risks subject to R&W recovery is 16, with related net debt service of $1.0 billion as of December 31, 2014 compared to 24 with net debt service of $2.3 billion as of December 31, 2013. A risk represents the aggregate of the financial guaranty policies that share the same revenue source for purposes of making Debt Service payments.

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

Components of R&W Development

	Year Ended December 31,	
	2014	2013
	(in millions)	
Inclusion or removal of deals with breaches of R&W during period	$ —	$ 6
Change in recovery assumptions as the result of recovery success	31	(5)
Estimated increase (decrease) in defaults that will result in additional (lower) breaches	(12)	49
Settlements and anticipated settlements	181	247
Accretion of discount on balance	7	11
Total	$ 207	$ 308

Manufactured Housing

The Company insures a total of $160 million net par of securities backed by manufactured housing loans, of which $100 million is rated BIG. The Company has expected loss to be paid of $19 million as of December 31, 2014. The economic loss development during 2014 was approximately $1 million, which was primarily attributable to the decline in risk free rates used to discount losses.

Selected U.S. Public Finance Transactions

The Company insures general obligation bonds of the Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations aggregating $2.2 billion net par. The Company rates $1.9 billion net par of that amount BIG. For additional information regarding the Company's exposure to general obligations of Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations, please refer to "Exposure to Puerto Rico" in Note 3, Outstanding Exposure.

The Company has net par exposure to the City of Detroit, Michigan of $1.4 billion as of December 31, 2014 to the general obligation and water and sewer utility sectors, as described below (which exposures are now investment grade by virtue of improvements and agreements reached through the bankruptcy process and settlement). In December 2014, the City of Detroit emerged from bankruptcy under Chapter 9 of the U.S. Bankruptcy Code. The City's proposed plan of adjustment and disclosure statement with the Bankruptcy Court was approved in November 2014.

- The Company has net par exposure to $670 million of sewer revenue bonds and $700 million of water revenue bonds. The sewer and water systems provide services to areas that extend beyond the city limits, and the bonds are secured by a lien on "special revenues." The Company rates the bonds, which are secured by a lien on "special revenues," BBB. The exposure reflects the City's issuance in September 2014 of new series of sewer and water revenue bonds to finance (i) the purchase of outstanding sewer and water revenue bonds offered and accepted under a tender offer commenced by the City and (ii) the refunding of certain other sewer revenue and revenue refunding bonds, and the Company's insurance of a portion of such issuance. In connection with these transactions, approximately $547 million of AGM's then combined $1.4 billion net par exposure to the sewer and water revenue bonds was purchased in the tender offer or refunded, and AGM insured approximately $841 million gross par of the new sewer and water revenue bonds. Under the City's amended plan of adjustment, the impairment of all outstanding sewer and water revenue bonds (even those not purchased pursuant to the tender offer or refunded) that had been proposed was removed, including those provisions which provided for the impairment of interest rates and call protection on such bonds.

- The Company has net par exposure of $37 million to Michigan Finance Authority by virtue of a court ordered exchange with all holders of the City's general obligation bonds which occurred upon emergence from bankruptcy in December 2014. The Michigan Finance Authority bonds are secured by a pledge of the unlimited tax, full faith, credit and resources of the City and the specific ad valorem taxes approved by the voters solely to pay debt service on the general obligation bonds and additional security in the form of a subordinate statutory lien on, and intercept of, the City's distributable state aid.

On June 28, 2012, the City of Stockton, California filed for bankruptcy protection under Chapter 9 of the U.S. Bankruptcy Code. AGM's net exposure to the City's general fund is $62 million, consisting of pension obligation bonds. AGC also had exposure to lease revenue bonds; as of December 31, 2014, AGC owned all of such bonds and held them in its investment portfolio. On October 3, 2013, AGM and AGC reached a settlement with the City regarding the treatment of the bonds insured by AGM and

AGC in the City's plan of adjustment. Under the terms of the settlement, AGM will be entitled to certain fixed payments and certain variable payments contingent on the City's revenue growth and AGC will continue to receive net revenues from an office building and an option to take title to that building. On October 30, 2014, the bankruptcy court confirmed the City's plan of adjustment, which includes the terms of such settlement, and the plan became effective on February 25, 2015.

The Company projects that its total net expected loss across its troubled U.S. public finance credits as of December 31, 2014, which incorporated the likelihood of the outcomes mentioned above, will be $142 million compared with a net expected loss of $61 million as of December 31, 2013. Economic loss development in 2014 was approximately $97 million, which was primarily attributable to Puerto Rico and Detroit exposures.

Certain Selected European Country Transactions

The Company insures with sub-sovereign exposure to various Spanish and Portuguese issuers where a Spanish and Portuguese sovereign default may cause the regions also to default. The Company's gross exposure to these Spanish and Portuguese credits is $514 million and $103 million, respectively and exposure net of reinsurance for Spanish and Portuguese credits is $324 million and $86 million, respectively. The Company rates most of these issuers in the BB category due to the financial condition of Spain and Portugal and their dependence on the sovereign. The Company's Hungary exposure is to infrastructure bonds dependent on payments from Hungarian governmental entities and covered mortgage bonds issued by Hungarian banks. The Company's gross exposure to these Hungarian credits is $524 million and its exposure net of reinsurance is $434 million, most of which is rated BIG. The Company estimated net expected losses of $38 million related to these Spanish, Portuguese and Hungarian credits The positive economic loss development during 2014 was approximately $4 million, which was primarily attributable to the favorable movement in the exchange rates between the US Dollar and both the Euro and Hungarian Forint during the year.

Infrastructure Finance

The Company has insured exposure of approximately $2.8 billion to infrastructure transactions with refinancing risk as to which the Company may need to make claim payments that it did not anticipate paying when the policies were issued. Although the Company may not experience ultimate loss on a particular transaction, the aggregate amount of the claim payments may be substantial and reimbursement may not occur for an extended time, if at all. These transactions generally involve long-term infrastructure projects that were financed by bonds that mature prior to the expiration of the project concession. The Company expects the cash flows from these projects to be sufficient to repay all of the debt over the life of the project concession, but also expects the debt to be refinanced in the market at or prior to its maturity. If the issuer is unable to refinance the debt due to market conditions, the Company may have to pay a claim when the debt matures, and then recover its payment from cash flows produced by the project in the future. The Company generally projects that in most scenarios it will be fully reimbursed for such payments. However, the recovery of the payments is uncertain and may take from 10 to 35 years, depending on the transaction and the performance of the underlying collateral. The Company estimates total claims for the two largest transactions with significant refinancing risk, assuming no refinancing and based on certain performance assumptions could be $1.6 billion on a gross basis; such claims would be payable from 2017 through 2022.

Recovery Litigation

RMBS Transactions

In November 2014, AGM and its affiliate AGC reached a confidential settlement with DLJ Mortgage Capital, Inc., Credit Suisse First Boston Mortgage Securities Corp. and Credit Suisse Securities (USA) LLC to resolve a lawsuit relating to six first lien U.S. RMBS transactions. AGM and AGC sought damages for alleged breaches of representations and warranties in respect of the underlying loans in these transactions, and failure to cure or repurchase defective loans identified by AGM and AGC. On November 25, 2014, the parties filed a joint stipulation discontinuing the lawsuit with prejudice. While U.S. Bank National Association, as trustee for the transactions, had filed a motion on November 20, 2014 to intervene as a plaintiff in the lawsuit, on March 5, 2015 the court denied the motion to intervene. In the fourth quarter of 2014, AGM recorded a benefit in connection with the settlement.

Previously, AGM also had sued Deutsche Bank AG affiliates DB Structured Products, Inc. and ACE Securities Corp. on a second lien U.S. RMBS transaction that it had insured. In November 2014, AGM resolved those claims against Deutsche Bank and filed a stipulation with the Supreme Court of the State of New York to dismiss the lawsuit; the court ordered the dismissal of the matter on November 17, 2014.

7. Financial Guaranty Insurance Losses

Accounting Policies

Loss and LAE Reserve

Loss and LAE reserve reported on the balance sheet relates only to direct and assumed reinsurance contracts that are accounted for as insurance, all of which are financial guaranty insurance contracts. The corresponding reserve ceded to reinsurers is reported as reinsurance recoverable on unpaid losses. As discussed in Note 8, Fair Value Measurement, contracts that meet the definition of a derivative, as well as consolidated FG VIE assets and liabilities, are recorded separately at fair value. Any expected losses related to consolidated FG VIEs are eliminated upon consolidation. Any expected losses on credit derivatives are not recorded as loss and LAE reserve on the consolidated balance sheet.

Under financial guaranty insurance accounting, the sum of unearned premium reserve and loss and LAE reserve represents the Company's stand‑ready obligation. Unearned premium reserve is deferred premium revenue, less claim payments and recoveries received that have not yet been recognized in the statement of operations ("contra-paid"). At contract inception, the entire stand-ready obligation is represented by unearned premium reserve. A loss and LAE reserve for an insurance contract is only recorded when the expected loss to be paid net of contra-paid (“total losses”) exceed the deferred premium revenue, on a contract by contract basis.

When a claim payment is made on a contract, it first reduces any recorded loss and LAE reserve. To the extent there is no loss and LAE reserve on a contract, which occurs when total losses are less than deferred premium revenue, or to the extent loss and LAE reserve is not sufficient to cover a claim payment, then such claim payment is recorded as “contra-paid,” which reduces the unearned premium reserve. The contra-paid is recognized in the line item “loss and LAE” in the consolidated statement of operations when and for the amount that total losses exceed the remaining deferred premium revenue on the insurance contract. Loss and LAE in the consolidated statement of operations is presented net of cessions to reinsurers.

Salvage and Subrogation Recoverable

When the Company becomes entitled to the cash flow from the underlying collateral of an insured credit under salvage and subrogation rights as a result of a claim payment or estimated future claim payment, it reduces the expected loss to be paid on the contract. Such reduction in expected loss to be paid can result in one of the following:

- a reduction in the corresponding loss and LAE reserve with a benefit to the income statement,
- no entry recorded, if “total loss” is not in excess of deferred premium revenue, or
- the recording of a salvage asset with a benefit to the income statement if the transaction is in a net recovery position at the reporting date.

The Company recognizes the expected recovery of claim payments (including recoveries from settlement with R&W providers) made by the Company prior to the date of its acquisition by AGL consistent with its policy for recognizing recoveries on all financial guaranty insurance contracts. To the extent that the estimated amount of recoveries increases or decreases, due to changes in facts and circumstances, the Company would recognize a benefit or expense consistent with how changes in the expected recovery of all other claim payments are recorded. The ceded component of salvage and subrogation recoverable is recorded in the line item reinsurance balances payable.

Expected Loss to be Expensed

Expected loss to be expensed represents past or expected future net claim payments that have not yet been expensed. Such amounts will be expensed in future periods as deferred premium revenue 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.

Insurance Contracts' Loss Information

The following table provides balance sheet information on loss and LAE reserves and salvage and subrogation recoverable, net of reinsurance. The Company used weighted average risk-free rates for U.S. dollar denominated financial guaranty insurance obligations that ranged from 0.0% to 2.95% as of December 31, 2014 and 0.0% to 4.44% as of December 31, 2013. Financial guaranty insurance expected LAE reserve was $4 million as of December 31, 2014 and $15 million as of December 31, 2013.

**Loss and LAE Reserve
and Salvage and Subrogation Recoverable
Net of Reinsurance
Insurance Contracts**

	As of December 31, 2014			As of December 31, 2013		
	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)
			(in millions)			
U.S. RMBS:						
First lien:						
Alt-A first lien	$ 22	$ —	$ 22	$ 63	$ —	$ 63
Option ARM	11	39	(28)	17	41	(24)
Subprime	156	7	149	137	1	136
First lien	189	46	143	217	42	175
Second lien:						
Closed-end second lien	—	39	(39)	—	45	(45)
HELOC	0	34	(34)	—	113	(113)
Second lien	0	73	(73)	—	158	(158)
Total U.S. RMBS	189	119	70	217	200	17
Other structured finance	20	—	20	20	—	20
U.S. public finance	119	—	119	35	—	35
Non-U.S. public finance	21	—	21	24	—	24
Subtotal	349	119	230	296	200	96
Effect of consolidating FG VIEs	(78)	(1)	(77)	(89)	(85)	(4)
Total (1)	$ 271	$ 118	$ 153	$ 207	$ 115	$ 92

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

The following table reconciles the reported gross and ceded reserve and salvage and subrogation amount to the financial guaranty net reserves (salvage) in the financial guaranty BIG transaction loss summary tables.

Components of Net Reserves (Salvage)
Insurance Contracts

	As of December 31, 2014	As of December 31, 2013
	(in millions)	
Loss and LAE reserve	$ 404	$ 273
Reinsurance recoverable on unpaid losses	(133)	(66)
Loss and LAE reserve, net	271	207
Salvage and subrogation recoverable	(130)	(140)
Salvage and subrogation payable(1)	12	25
Salvage and subrogation recoverable, net	(118)	(115)
Net reserves (salvage)	$ 153	$ 92

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

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

	As of December 31, 2014			As of December 31, 2013		
	For all Financial Guaranty Insurance Contracts	Effect of Consolidating FG VIEs	Reported on Balance Sheet (1)	For all Financial Guaranty Insurance Contracts	Effect of Consolidating FG VIEs	Reported on Balance Sheet (1)
	(in millions)					
Salvage and subrogation recoverable, net	$ 7	$ —	$ 7	$ 102	$ (49)	$ 53
Loss and LAE reserve, net	158	—	158	272	—	272

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

The table below provides a reconciliation of net expected loss to be paid to net expected loss to be expensed. Expected loss to be paid differs from expected loss to be expensed due to: (1) the contra-paid which represent the claim payments made and recoveries received that have not yet been recognized in the statement of operations, (2) salvage and subrogation recoverable for transactions that are in a net recovery position where the Company has not yet received recoveries on claims previously paid (having the effect of reducing net expected loss to be paid by the amount of the previously paid claim and the expected recovery), but will have no future income effect (because the previously paid claims and the corresponding recovery of those claims will offset in income in future periods), and (3) loss reserves that have already been established (and therefore expensed but not yet paid).

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

	As of December 31, 2014
	(in millions)
Net expected loss to be paid	$ 613
Less: net expected loss to be paid for FG VIEs	119
Total	494
Contra-paid, net	(102)
Salvage and subrogation recoverable, net of reinsurance	118
Loss and LAE reserve, net of reinsurance	(271)
Net expected loss to be expensed (present value)(1)	$ 239

____

(1) Excludes $84 million as of December 31, 2014 related to consolidated FG VIEs.

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

Net Expected Loss to be Expensed Financial Guaranty Insurance Contracts

	As of December 31, 2014
	(in millions)
2015 (January 1 - March 31)	$ 7
2015 (April 1 - June 30)	6
2015 (July 1- September 30)	7
2015 (October 1 - December 31)	8
Subtotal 2015	28
2016	29
2017	22
2018	19
2019	17
2020-2024	61
2025-2029	32
2030-2034	21
After 2034	10
Net expected loss to be expensed	239
Discount	155
Total future value	$ 394

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

	Year Ended December 31,	
	2014	2013
	(in millions)	
Structured Finance:		
U.S. RMBS:		
First lien:		
Alt-A first lien	$ (39)	$ (2)
Option ARM	(24)	(54)
Subprime	4	75
First lien	(59)	19
Second lien:		
Closed-end second lien	(1)	19
HELOC	(30)	(14)
Second lien	(31)	5
Total U.S. RMBS	(90)	24
Other structured finance	1	1
Structured finance	(89)	25
Public Finance:		
U.S. public finance	96	78
Non-U.S. public finance	(1)	8
Public finance	95	86
Loss and LAE on insurance contracts before FG VIE consolidation	6	111
Effect of consolidating FG VIEs	(31)	(19)
Loss and LAE	$ (25)	$ 92

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

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of December 31, 2014

	BIG Categories								
	BIG 1		BIG 2		BIG 3				
	Gross	Ceded	Gross	Ceded	Gross	Ceded	Total BIG, Net	Effect of Consolidating VIEs	Total
	(dollars in millions)								
Number of risks(1)	71	(65)	14	(14)	38	(38)	123	—	123
Remaining weighted-average contract period (in years)	8.4	8.1	7.9	8.8	7.6	8.1	8.2	—	8.2
Outstanding exposure:									
Principal	$ 8,281	$ (3,341)	$ 1,594	$ (468)	$ 2,013	$ (279)	$ 7,800	$ —	$ 7,800
Interest	3,693	(1,435)	616	(187)	784	(105)	3,366	—	3,366
Total(2)	$ 11,974	$ (4,776)	$ 2,210	$ (655)	$ 2,797	$ (384)	$ 11,166	$ —	$ 11,166
Expected cash outflows (inflows)	$ 1,538	$ (796)	$ 621	$ (128)	$ 1,101	$ (101)	$ 2,235	$ (298)	$ 1,937
Potential recoveries									
Undiscounted R&W	(12)	0	(46)	2	(160)	11	(205)	—	(205)
Other(3)	(1,526)	767	(197)	6	(326)	44	(1,232)	149	(1,083)
Total potential recoveries	(1,538)	767	(243)	8	(486)	55	(1,437)	149	(1,288)
Subtotal	0	(29)	378	(120)	615	(46)	798	(149)	649
Discount	11	0	(67)	18	(150)	3	(185)	30	(155)
Present value of expected cash flows	$ 11	$ (29)	$ 311	$ (102)	$ 465	$ (43)	$ 613	$ (119)	$ 494
Deferred premium revenue	$ 324	$ (100)	$ 107	$ (9)	$ 287	$ (43)	$ 566	$ (111)	$ 455
Reserves (salvage)(4)	$ (41)	$ (9)	$ 207	$ (92)	$ 185	$ (20)	$ 230	$ (77)	$ 153

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of December 31, 2013

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	91	(84)	23	(23)	33	(33)	147	—	147
Remaining weighted-average contract period (in years)	9.0	8.8	5.6	5.0	8.0	9.1	8.3	—	8.3
Outstanding exposure:									
Principal	$ 10,298	$ (4,203)	$ 1,693	$ (197)	$ 1,644	$ (241)	$ 8,994	$ —	$ 8,994
Interest	4,762	(1,914)	541	(53)	714	(107)	3,943	—	3,943
Total(2)	$ 15,060	$ (6,117)	$ 2,234	$ (250)	$ 2,358	$ (348)	$ 12,937	$ —	$ 12,937
Expected cash outflows (inflows)	$ 1,557	$ (711)	$ 909	$ (51)	$ 1,013	$ (86)	$ 2,631	$ (573)	$ 2,058
Potential recoveries									
Undiscounted R&W	(38)	1	(199)	9	(301)	16	(512)	38	(474)
Other(3)	(1,571)	684	(454)	26	(275)	26	(1,564)	457	(1,107)
Total potential recoveries	(1,609)	685	(653)	35	(576)	42	(2,076)	495	(1,581)
Subtotal	(52)	(26)	256	(16)	437	(44)	555	(78)	477
Discount	17	0	(64)	3	(106)	(5)	(155)	36	(119)
Present value of expected cash flows	$ (35)	$ (26)	$ 192	$ (13)	$ 331	$ (49)	$ 400	$ (42)	$ 358
Deferred premium revenue	$ 446	$ (128)	$ 153	$ (10)	$ 270	$ (34)	$ 697	$ (172)	$ 525
Reserves (salvage)(4)	$ (98)	$ 0	$ 76	$ (6)	$ 159	$ (35)	$ 96	$ (4)	$ 92

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

(2) Includes BIG amounts related to FG VIEs.

(3) Includes excess spread and draws on HELOCs.

(4) See table "Components of net reserves (salvage)."

Ratings Impact on Financial Guaranty Business

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

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

has been met; (iv) the bank counterparty has elected to terminate the swap; (v) a termination payment is payable by the municipal obligor; and (vi) the municipal obligor has failed to make the termination payment payable by it, then AGM would be required to pay the termination payment due by the municipal obligor, in an amount not to exceed the policy limit set forth in the financial guaranty insurance policy. At AGM's current financial strength ratings, if the conditions giving rise to the obligation of AGM to make a termination payment under the swap termination policies were all satisfied, then AGM could pay claims in an amount not exceeding approximately $146 million in respect of such termination payments. Taking into consideration whether the rating of the municipal obligor is below any applicable specified trigger, if the financial strength ratings of AGM were further downgraded below "A" by S&P or below "A2" by Moody's, and the conditions giving rise to the obligation of AGM to make a payment under the swap policies were all satisfied, then AGM could pay claims in an additional amount not exceeding approximately $393 million in respect of such termination payments.

As another example, with respect to variable rate demand obligations ("VRDOs") for which a bank has agreed to provide a liquidity facility, a downgrade of AGM may provide the bank with the right to give notice to bondholders that the bank will terminate the liquidity facility, causing the bondholders to tender their bonds to the bank. Bonds held by the bank accrue interest at a “bank bond rate” that is higher than the rate otherwise borne by the bond (typically the prime rate plus 2.00% - 3.00%, and capped at the lesser of 25% and the maximum legal limit). In the event the bank holds such bonds for longer than a specified period of time, usually 90-180 days, the bank has the right to demand accelerated repayment of bond principal, usually through payment of equal installments over a period of not less than five years. In the event that a municipal obligor is unable to pay interest accruing at the bank bond rate or to pay principal during the shortened amortization period, a claim could be submitted to AGM under its financial guaranty policy. As of December 31, 2014, the Company had insured approximately $5.3 billion net par of VRDOs, of which approximately $0.2 billion of net par constituted VRDOs issued by municipal obligors rated BBB- or lower pursuant to the Company’s internal rating. The specific terms relating to the rating levels that trigger the bank’s termination right, and whether it is triggered by a downgrade by one rating agency or a downgrade by all rating agencies then rating the insurer, vary depending on the transaction.

In addition, AGM may be required to pay claims in respect of AGMH’s former financial products business if Dexia SA and its affiliates, from which Assured Guaranty had purchased AGMH and its subsidiaries, do not comply with their obligations following a downgrade of the financial strength rating of AGM. Most of the guaranteed investment contracts ("GICs") insured by AGM allow the GIC holder to terminate the GIC and withdraw the funds in the event of a downgrade of AGM below A3 or A-, with no right of the GIC issuer to avoid such withdrawal by posting collateral or otherwise enhancing its credit. Each GIC contract stipulates the thresholds below which the GIC issuer must post eligible collateral, along with the types of securities eligible for posting and the collateralization percentage applicable to each security type. These collateralization percentages range from 100% of the GIC balance for cash posted as collateral to, typically, 108% for asset-backed securities. If the entire aggregate accreted GIC balance of approximately $2.3 billion as of December 31, 2014 were terminated, the assets of the GIC issuers (which had an aggregate accreted principal of approximately $3.4 billion and an aggregate market value of approximately $3.1 billion) would be sufficient to fund the withdrawal of the GIC funds.

8. Fair Value Measurement

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

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

Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments include amounts to reflect counterparty credit quality, the Company’s creditworthiness and constraints on liquidity. As markets and products develop and the pricing for certain products becomes more or less transparent, the Company may refine its methodologies and assumptions. During 2014, no changes were made to the Company’s valuation models that had or are expected to have, a material impact on the Company’s consolidated balance sheets or statements of operations and comprehensive income.

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

The fair value hierarchy is determined based on whether the inputs to valuation techniques used to measure fair value are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Company estimates of market assumptions. The fair value hierarchy prioritizes model inputs into three broad levels as follows, with Level 1 being the highest and Level 3 the lowest. An asset or liability’s categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation.

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

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

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

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

Measured and Carried at Fair Value

Fixed-Maturity Securities and Short-Term Investments

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

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

Prices determined based on models where at least one significant model assumption or input is unobservable, are considered to be Level 3 in the fair value hierarchy. As of December 31, 2014, the Company used models to price 28 fixed-maturity securities (which were purchased or obtained for loss mitigation purposes), which was 9% or $581 million of the Company's fixed-maturity securities and short-term investments at fair value. Certain Level 3 securities were priced with the assistance of an independent third-party. The pricing is based on a discounted cash flow approach using the third-party’s proprietary pricing models. The models use inputs such as projected prepayment speeds; severity assumptions; recovery lag assumptions; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); home price depreciation/appreciation rates based on macroeconomic forecasts and recent trading activity. The yield used to discount the

projected cash flows is determined by reviewing various attributes of the bond including collateral type, weighted average life, sensitivity to losses, vintage, and convexity, in conjunction with market data on comparable securities. Significant changes to any of these inputs could materially change the expected timing of cash flows within these securities which is a significant factor in determining the fair value of the securities.

Other Invested Assets

As of December 31, 2014, other invested assets include investments carried and measured at fair value on a recurring basis of $94 million and include primarily investments in the global property catastrophe risk market and investment in a high yield fund that invests primarily in senior loans and bonds. Both of these investments were classified as Level 3. As of December 31, 2013, other invested assets included investments carried and measured at fair value on a recurring basis of $80 million and included primarily certain short-term investments and fixed-maturity securities classified as trading carried as Level 2.

Other Assets

Committed Capital Securities

The fair value of AGM Committed Preferred Trust Securities (the “AGM CPS”), which is recorded in “other assets” on the consolidated balance sheets, represents the difference between the present value of remaining expected put option premium payments under AGM CPS agreements, and the estimated present value that the Company would hypothetically have to pay currently for a comparable security (see Note 18, Notes Payable and Credit Facilities). The AGM CPS are carried at fair value with changes in fair value recorded on the consolidated statement of operations. The estimated current cost of the AGM CPS is based on several factors, including broker-dealer quotes for the outstanding securities, the U.S. dollar forward swap curve, London Interbank Offered Rate ("LIBOR") curve projections and the term the securities are estimated to remain outstanding.

Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company’s credit derivatives consist primarily of insured CDS contracts, and also include interest rate swaps that fall under derivative accounting standards requiring fair value accounting through the statement of operations. The Company does not enter into CDS with the intent to trade these contracts and the Company may not unilaterally terminate a CDS contract absent an event of default or termination event that entitles the Company to terminate; however, the Company has mutually agreed with various counterparties to terminate certain CDS transactions. Such terminations generally are not completed at fair value but instead for an amount that approximates the present value of future premiums.

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

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

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

The fair value of the Company’s credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay and the estimated present value of premiums that a financial

guarantor of comparable credit-worthiness would hypothetically charge or pay at the reporting date for the same protection. The fair value of the Company's credit derivatives depends on a number of factors, including notional amount of the contract, expected term, credit spreads, changes in interest rates, the credit ratings of referenced entities, the Company's own credit risk and remaining contractual cash flows. The expected remaining contractual premium cash flows are the most readily observable inputs since they are based on the CDS contractual terms. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. Consistent with previous years, market conditions at December 31, 2014 were such that market prices of the Company's CDS contracts were not available.

Management considers factors such as current prices charged for similar agreements, when available, performance of underlying assets, life of the instrument, and the nature and extent of activity in the financial guaranty credit derivative marketplace. The assumptions that management uses to determine the fair value may change in the future due to market conditions. Due to the inherent uncertainties of the assumptions used in the valuation models, actual experience may differ from the estimates reflected in the Company's consolidated financial statements and the differences may be material.

Assumptions and Inputs

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

- Gross spread.
- The allocation of gross spread among:
  - the profit the originator, usually an investment bank, realizes for putting the deal together and funding the transaction ("bank profit");
  - premiums paid to the Company for the Company's credit protection provided ("net spread"); and
  - the cost of CDS protection purchased by the originator to hedge their counterparty credit risk exposure to the Company ("hedge cost").
- The weighted average life which is based on Debt Service schedules.

The rates used to discount future expected premium cash flows ranged from 0.26% to 2.66% at December 31, 2014 and 0.21% to 3.80% at December 31, 2013.

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

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

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

- Actual collateral specific credit spreads (if up-to-date and reliable market-based spreads are available).
- Deals priced or closed during a specific quarter within a specific asset class and specific rating. There were no deals closed during the period presented.
- Credit spreads interpolated based upon market indices.
- Credit spreads provided by the counterparty of the CDS.
- Credit spreads extrapolated based upon transactions of similar asset classes, similar ratings, and similar time to maturity.

Information by Credit Spread Type (1)

	As of December 31, 2014	As of December 31, 2013
Based on actual collateral specific spreads	0.1%	0.1%
Based on market indices	99.9%	99.9%
Total	100%	100%

(1) Based on par.

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

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

The premium the Company receives is referred to as the "net spread." The Company's pricing model takes into account not only how credit spreads on risks that it assumes affect pricing, but also how the Company's own credit spread affects the pricing of its deals. The Company's own credit risk is factored into the determination of net spread based on the impact of changes in the quoted market price for credit protection bought on the Company, as reflected by quoted market prices on CDS referencing AGM. For credit spreads on the Company's name the Company obtains the quoted price of CDS contracts traded on AGM from market data sources published by third parties. The cost to acquire CDS protection referencing AGM affects the amount of spread on CDS deals that the Company retains and, hence, their fair value. As the cost to acquire CDS protection referencing AGM increases, the amount of premium the Company retains on a deal generally decreases. As the cost to acquire CDS protection referencing AGM decreases, the amount of premium the Company retains on a deal generally increases. In the Company's valuation model, the premium the Company captures is not permitted to go below the minimum rate that the Company would currently charge to assume similar risks. This assumption can have the effect of mitigating the amount of unrealized gains that are recognized on certain CDS contracts. Given the current market conditions and the

Company's own credit spreads, approximately 19%, and 83%, based on number of deals, of the Company's CDS contracts are fair valued using this minimum premium as of December 31, 2014 and December 31, 2013, respectively. The percentage of deals that price using the minimum premiums has fluctuated since December 31, 2013 due to changes in AGM's credit spreads. In general when AGM's credit spreads narrow, the cost to hedge AGM's name declines and more transactions price above previously established floor levels. Meanwhile, when AGM's credit spreads widen, the cost to hedge AGM's name increases causing more transactions to price at previously established floor levels. The Company corroborates the assumptions in its fair value model, including the portion of exposure to AGM hedged by its counterparties, with independent third parties each reporting period. The current level of AGM's own credit spread has resulted in the bank or deal originator hedging a significant portion of its exposure to AGM. This reduces the amount of contractual cash flows AGM can capture as premium for selling its protection.

The amount of premium a financial guaranty insurance market participant can demand is inversely related to the cost of credit protection on the insurance company as measured by market credit spreads assuming all other assumptions remain constant. This is because the buyers of credit protection typically hedge a portion of their risk to the financial guarantor, due to the fact that the contractual terms of the Company's contracts typically do not require the posting of collateral by the guarantor. The extent of the hedge depends on the types of instruments insured and the current market conditions.

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

Example

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

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

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

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

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

Strengths and Weaknesses of Model

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

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

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

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

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

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

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

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

- At December 31, 2014 and 2013, the markets for the inputs to the model were highly illiquid, which impacts their reliability.

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

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

Fair Value Option on FG VIEs' Assets and Liabilities

The Company elected the fair value option for all the FG VIEs' assets and liabilities. See Note 10, Consolidated Variable Interest Entities.

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

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

The fair value of the Company’s FG VIE liabilities is also generally sensitive to changes relating to estimated prepayment speeds; market values of the underlying assets; estimated default rates (determined on the basis of an analysis of collateral attributes such as: historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); discount rates implied by market prices for similar securities; and house price depreciation/appreciation rates based on macroeconomic forecasts. In addition, the Company’s FG VIE liabilities with recourse are also sensitive to changes in the Company’s implied credit worthiness. Significant changes to any of these inputs could materially change the timing of expected losses within the insured transaction which is a significant factor in determining the implied benefit from the Company’s insurance policy guaranteeing the timely payment of principal and interest for the tranches of debt issued by the FG VIE that is insured by the Company. In general, extending the timing of expected loss payments by the Company into the future typically leads to a decrease in the value of the Company’s insurance and a decrease in the fair value of the Company’s FG VIE liabilities with recourse, while a shortening of the timing of expected loss payments by the Company typically leads to an increase in the value of the Company’s insurance and an increase in the fair value of the Company’s FG VIE liabilities with recourse.

Not Carried at Fair Value

Financial Guaranty Insurance Contracts

The fair value of the Company’s financial guaranty contracts accounted for as insurance was based on management’s estimate of what a similarly rated financial guaranty insurance company would demand to acquire the Company’s in-force book of financial guaranty insurance business. This amount was based on the pricing assumptions management has observed for portfolio transfers that have occurred in the financial guaranty market and included adjustments to the carrying value of unearned premium reserve for stressed losses, ceding commissions and return on capital. The significant inputs were not readily observable. The Company accordingly classified this fair value measurement as Level 3.

Other Invested Assets

Other invested assets primarily consist of a surplus note issued by AGC to AGM and assets acquired in refinancing transactions. The fair value of the surplus note was determined by calculating the effect of changes in U.S. Treasury yield adjusted for a credit factor at the end of each reporting period. The fair value measurement of the surplus note was classified as Level 3.

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

Other Assets and Other Liabilities

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

Notes Payable

The fair value of the notes payable was determined by calculating the present value of the expected cash flows. The Company uses a market approach to determine discounted future cash flows using market driven discount rates and a variety of assumptions, if applicable, including LIBOR curve projections, prepayment and default assumptions, and AGM CDS spreads. The fair value measurement was classified as Level 3 in the fair value hierarchy.

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, 2014

		Fair Value Hierarchy		
	Fair Value	Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$ 4,189	$ —	$ 4,181	$ 8
U.S. government and agencies	69	—	69	—
Corporate securities	643	—	564	79
Mortgage-backed securities:				
RMBS	661	—	262	399
Commercial mortgage-backed securities ("CMBS")	266	—	266	—
Asset-backed securities	193	—	98	95
Foreign government securities	191	—	191	—
Total fixed-maturity securities	6,212	—	5,631	581
Short-term investments	377	197	180	—
Other invested assets (1)	99	—	16	83
Credit derivative assets	79	—	—	79
FG VIEs' assets, at fair value	823	—	—	823
Other assets	17	—	—	17
Total assets carried at fair value	$ 7,607	$ 197	$ 5,827	$ 1,583
Liabilities:				
Credit derivative liabilities	$ 287	$ —	$ —	$ 287
FG VIEs' liabilities with recourse, at fair value	830	—	—	830
FG VIEs' liabilities without recourse, at fair value	114	—	—	114
Total liabilities carried at fair value	$ 1,231	$ —	$ —	$ 1,231

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2013

		Fair Value Hierarchy		
	Fair Value	Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$ 3,690	$ —	$ 3,682	$ 8
U.S. government and agencies	69	—	69	—
Corporate securities	629	—	493	136
Mortgage-backed securities:				
RMBS	438	—	200	238
CMBS	210	—	210	—
Asset-backed securities	300	—	159	141
Foreign government securities	186	—	186	—
Total fixed-maturity securities	5,522	—	4,999	523
Short-term investments	667	411	256	—
Other invested assets (1)	86	—	78	8
Credit derivative assets	98	—	—	98
FG VIEs' assets, at fair value	1,691	—	—	1,691
Other assets	21	—	—	21
Total assets carried at fair value	$ 8,085	$ 411	$ 5,333	$ 2,341
Liabilities:				
Credit derivative liabilities	$ 326	$ —	$ —	$ 326
FG VIEs' liabilities with recourse, at fair value	1,275	—	—	1,275
FG VIEs' liabilities without recourse, at fair value	686	—	—	686
Total liabilities carried at fair value	$ 2,287	$ —	$ —	$ 2,287

(1) Includes Level 3 mortgage loans that are recorded at fair value on a non-recurring basis.

Changes in Level 3 Fair Value Measurements

The table below presents a roll forward of the Company's Level 3 financial instruments carried at fair value on a recurring basis during the years ended December 31, 2014 and 2013.

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2014

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Other Invested Assets	FG VIEs' Assets at Fair Value	Other Assets	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)									
Fair value as of December 31, 2013	$ 8	$ 136	$ 238	$ 141	$ 2	$ 1,691	$ 21	$ (228)	$ (1,275)	$ (686)
Total pretax realized and unrealized gains/(losses) recorded in:(1)										
Net income (loss)	1 (2)	(46) (2)	16 (2)	12 (2)	0 (7)	144 (3)	(4) (4)	41 (6)	(30) (3)	(48) (3)
Other comprehensive income (loss)	0	(6)	25	2	6	—	—	—	—	—
Purchases	—	—	160	—	70	—	—	—	—	—
Settlements	(1)	(5)	(41)	(60)	0	(360)	—	(21)	351	14
FG VIE consolidations	—	—	—	—	—	46	—	—	(25)	(21)
FG VIE deconsolidations	—	—	1	—	—	(698)	—	—	149	627
Fair value as of December 31, 2014	$ 8	$ 79	$ 399	$ 95	$ 78	$ 823	$ 17	$ (208)	$ (830)	$ (114)
Change in unrealized gains/(losses) related to financial instruments held as of December 31, 2014	$ 0	$ (6)	$ 22	$ 1	$ 6	$ 110	$ (4)	$ 19	$ (14)	$ (10)

Fair Value Level 3 Rollforward
Recurring Basis
Year Ended December 31, 2013

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Other Invested Assets	FG VIEs' Assets at Fair Value	Other Assets	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)									
Fair value as of December 31, 2012	$ 12	$ —	$ 184	$ 249	$ 1	$ 1,870	$ 14	$ (283)	$ (1,605)	$ (678)
Total pretax realized and unrealized gains/ (losses) recorded in:(1)										
Net income (loss)	1 (2)	4 (2)	11 (2)	62 (2)	(1) (7)	554 (3)	7 (4)	98 (6)	(100) (3)	(153) (3)
Other comprehensive income (loss)	(1)	4	21	(51)	2	—	—	—	—	—
Purchases	—	130 (8)	66	22	2 (8)	—	—	—	—	—
Settlements	(4)	(2)	(44)	(141)	(2)	(587)	—	(43)	307	118
FG VIE consolidations	—	—	—	—	—	48	—	—	(12)	(37)
FG VIE deconsolidations	—	—	—	—	—	(194)	—	—	135	64
Fair value as of December 31, 2013	$ 8	$ 136	$ 238	$ 141	$ 2	$ 1,691	$ 21	$ (228)	$ (1,275)	$ (686)
Change in unrealized gains/ (losses) related to financial instruments held as of December 31, 2013	$ (1)	$ 4	$ 20	$ (28)	$ 2	$ 428	$ 7	$ 54	$ (100)	$ (214)

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

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

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

(4) Recorded in fair value gains (losses) on committed capital securities.

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

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

(7) Reported in other income.

(8) Non-cash transaction.

Level 3 Fair Value Disclosures

Quantitative Information About Level 3 Fair Value Inputs
At December 31, 2014

Financial Instrument Description (1)	Fair Value at December 31, 2014 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets:				
Fixed-maturity securities:				
Obligations of state and political subdivisions	$ 8	Rate of inflation	1.0% - 3.0%	2.0%
		Cash flow receipts	0.5% - 22.4%	22.1%
		Yield	4.6%	
		Collateral recovery period	1 month - 9 years	8.4 years
Corporate securities	79	Yield	17.8%	
RMBS	399	CPR	0.3% - 8.1%	3.1%
		CDR	3.1% - 10.6%	5.4%
		Loss severity	52.6% - 100.0%	75.7%
		Yield	4.6% - 11.7%	6.4%
Asset-backed securities:				
Investor owned utility	95	Cash flow receipts	100%	
		Collateral recovery period	4 years	
		Discount factor	7.0%	
Other invested assets	83	Discount for lack of liquidity	20%	
		Recovery on delinquent loans	40%	
		Default rates	0.0% - 7.0%	5.8%
		Loss severity	40.0% - 75.0%	68.3%
		Prepayment speeds	5.0% - 15.0%	12.3%
		Net asset value (per share)	$ 965 - $1,159	$1,082
FG VIEs' assets, at fair value	823	CPR	0.3% - 7.0%	3.2%
		CDR	1.6% - 11.8%	4.4%
		Loss severity	40.0% - 100.0%	81.4%
		Yield	2.7% - 17.7%	7.9%

Financial Instrument Description (1)	Fair Value at December 31, 2014 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Other assets	17	Quotes from third party pricing	$ 52 - $57	$54.5
		Term (years)	5 years	
Liabilities:				
Credit derivative liabilities, net	(208)	Hedge cost (in bps)	21.2 - 243.8	38.6
		Bank profit (in bps)	1.0 - 916.9	48.6
		Internal floor (in bps)	7.0 - 100.0	9.2
		Internal credit rating	AAA - CCC	AAA
FG VIEs' liabilities, at fair value	(944)	CPR	0.3% - 7.0%	3.2%
		CDR	1.6% - 11.8%	4.4%
		Loss severity	40.0% - 100.0%	81.4%
		Yield	2.7% - 17.7%	6.2%

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

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

Financial Instrument Description (1)	Fair Value at December 31, 2013 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets:				
Fixed-maturity securities:				
Obligations of state and political subdivisions	$ 8	Rate of inflation	1.0% - 3.0%	2.0%
		Cash flow receipts	0.5% - 19.3%	19.0%
		Discount rates	4.6%	4.6%
		Collateral recovery period	1 month - 10 years	9.3 years
Corporate securities	136	Yield	8.3%	
RMBS	238	CPR	1.0% - 9.1%	4.2%
		CDR	5.0% - 25.8%	18.1%
		Loss severity	48.1% - 101.8%	88.5%
		Yield	2.5% - 7.8%	5.0%
Asset-backed securities:				
Investor owned utility	141	Liquidation value (in millions)	$195 - $245	$228
		Years to liquidation	0 years - 3 years	2 years
		Collateral recovery period	12 months - 6 years	3.5 years
		Discount factor	15.3%	15.3%
Other invested assets	8	Discount for lack of liquidity	10.0% - 20.0%	20.0%
		Recovery on delinquent loans	20.0% - 60.0%	40.0%
		Default rates	1.0% - 10.0%	3.2%
		Loss severity	40.0% - 90.0%	73.5%
		Prepayment speeds	6.0% - 15.0%	13.1%
FG VIEs’ assets, at fair value	1,691	CPR	0.3% - 9.7%	5.6%
		CDR	3.0% - 25.8%	13.6%
		Loss severity	37.5% - 101.5%	77.6%
		Yield	3.5% - 9.2%	6.4%

Financial Instrument Description (1)	Fair Value at December 31, 2013 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Other assets	21	Quotes from third party pricing	$47 - $52	$49.5
		Term (years)	5 years	
Liabilities:				
Credit derivative liabilities, net	(228)	Hedge cost (in bps)	55.0 - 525.0	72.3
		Bank profit (in bps)	1.0 - 1,418.5	56.7
		Internal floor (in bps)	7.0 - 100.0	13.2
		Internal credit rating	AAA - CCC	AAA
FG VIEs' liabilities, at fair value	(1,961)	CPR	0.3% - 9.7%	5.6%
		CDR	3.0% - 25.8%	13.6%
		Loss severity	37.5% - 101.5%	77.6%
		Yield	3.5% - 9.2%	6.4%

____

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

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

Fair Value of Financial Instruments

	As of December 31, 2014		As of December 31, 2013	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in millions)			
Assets:				
Fixed-maturity securities	$ 6,212	$ 6,212	$ 5,522	$ 5,522
Short-term investments	377	377	667	667
Other invested assets	407	491	405	442
Credit derivative assets	79	79	98	98
FG VIEs' assets, at fair value	823	823	1,691	1,691
Other assets	89	89	82	82
Liabilities:				
Financial guaranty insurance contracts(1)	2,325	3,279	2,312	2,481
Notes payable	19	16	39	38
Credit derivative liabilities	287	287	326	326
FG VIEs' liabilities with recourse, at fair value	830	830	1,275	1,275
FG VIEs' liabilities without recourse, at fair value	114	114	686	686
Other liabilities	21	21	16	16

____

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

9. Financial Guaranty Contracts Accounted for as Credit Derivatives

Accounting Policy

Credit derivatives are recorded at fair value. Changes in fair value are recorded in "net change in fair value of credit derivatives" on the consolidated statement of operations. Realized gains and other settlements on credit derivatives include credit derivative premiums received and receivable for credit protection the Company has sold under its insured CDS contracts, premiums paid and payable for credit protection the Company has purchased, claims paid and payable and received and receivable related to insured credit events under these contracts, ceding commissions expense or income and realized gains or losses related to their early termination. Fair value of credit derivatives is reflected as either net assets or net liabilities determined on a contract by contract basis in the Company's consolidated balance sheets. See Note 8, Fair Value Measurement, for a discussion on the fair value methodology for credit derivatives.

Credit Derivatives

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

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

Credit Derivative Net Par Outstanding by Sector

The estimated remaining weighted average life of credit derivatives was 2.5 years at December 31, 2014 and 2.3 years at December 31, 2013. The components of the Company's credit derivative net par outstanding are presented below.

Credit Derivatives
Subordination and Ratings

	As of December 31, 2014				As of December 31, 2013			
Asset Type	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating
	(dollars in millions)							
Pooled corporate obligations:								
Collateralized loan obligations/ collateralized bond obligations	$ 7,375	29.6%	33.6%	AAA	$ 11,250	29.4%	30.2%	AAA
Synthetic investment grade pooled corporate	7,354	22.3	20.3	AAA	9,186	21.1	19.5	AAA
Synthetic high yield pooled corporate	—	—	—	—	2,684	47.2	41.1	AAA
Trust preferred securities collateralized debt obligations ("TruPS CDOs")	9	56.0	86.4	AAA	16	56.0	85.1	AAA
Market value CDOs of corporate obligations	946	17.0	20.1	AAA	1,184	17.0	27.5	AAA
Total pooled corporate obligations	15,684	25.5	26.6	AAA	24,320	27.6	27.3	AAA
U.S. RMBS:								
Subprime first lien	55	—	—	AAA	64	—	—	AAA
Closed-end second lien	61	—	—	BBB+	73	—	—	A
Total U.S. RMBS	116	—	—	AA-	137	—	—	AA
Other	2,393	—	—	A-	2,871	—	—	A-
Total	$ 18,193			AAA	$ 27,328			AAA

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

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

The $2.4 billion of exposure in "Other" CDS contracts as of December 31, 2014 comprises numerous deals typically structured with significant underlying credit enhancement and spread across various asset classes, such as commercial receivables, international RMBS, infrastructure, regulated utilities and consumer receivables.

Distribution of Credit Derivative Net Par Outstanding by Internal Rating

Ratings	As of December 31, 2014 Net Par Outstanding	As of December 31, 2014 % of Total	As of December 31, 2013 Net Par Outstanding	As of December 31, 2013 % of Total
	(dollars in millions)			
AAA	$ 14,471	79.5%	$ 23,200	84.9%
AA	1,843	10.1	1,858	6.8
A	920	5.1	899	3.2
BBB	830	4.6	1,081	4.0
BIG	129	0.7	290	1.1
Credit derivative net par outstanding	$ 18,193	100.0%	$ 27,328	100.0%

Fair Value of Credit Derivatives

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

	Year Ended December 31, 2014	Year Ended December 31, 2013
	(in millions)	
Realized gains on credit derivatives	$ 33	$ 56
Net credit derivative losses (paid and payable) recovered and recoverable and other settlements	(11)	(15)
Realized gains (losses) and other settlements on credit derivatives	22	41
Net change in unrealized gains (losses) on credit derivatives:		
Pooled corporate obligations	13	$ 3
U.S. RMBS	3	1
Other (1)	3	53
Net change in unrealized gains (losses) on credit derivatives (2)	19	57
Net change in fair value of credit derivatives	$ 41	$ 98

(1) "Other" includes all other U.S. and international asset classes, such as commercial receivables, international infrastructure, international RMBS securities, and pooled infrastructure securities.

(2) Except for net estimated credit impairments (i.e., net expected loss to be paid as discussed in Note 6), the unrealized gains and losses on credit derivatives are expected to reduce to zero as the exposure approaches its maturity date. With considerable volatility continuing in the market, unrealized gains (losses) on credit derivatives may fluctuate significantly in future periods.

The table below sets out the net par amount of credit derivative contracts that the Company and its counterparties agreed to terminate on a consensual basis.

Net Par and Realized Gains (Losses) on Credit Derivatives from Terminations of CDS Contracts

	Year Ended December 31, 2014	Year Ended December 31, 2013
	(in millions)	
Net par of terminated CDS contracts	$ 565	$ 2,003
Realized gains (losses) and other settlements	1	13

In 2014, unrealized fair value gains were generated primarily in the pooled corporate obligations and Other sectors. The unrealized gains were a result of the run-off of outstanding exposure as the transactions in these sectors approach maturity, as well as the expiration of several large synthetic high yield pooled corporate transactions. These unrealized gains were partially offset by unrealized losses resulting from the decreased cost to buy protection in AGM's name as the market cost of AGM's credit protection decreased during the period. Several transactions were pricing above their floor levels (or minimum rate at which the Company would consider assuming these risks based on historical experience); therefore when the cost of purchasing CDS protection on AGM decreased, which management refers to as the CDS spread on AGM, the implied spreads that the Company would expect to receive on these transactions increased.

In 2013, unrealized fair value gains were generated primarily in the Other sector. The unrealized gain in the Other sector was driven primarily by the price improvement on a XXX life securitization transaction and the run-off of par outstanding. These unrealized gains were partially offset by unrealized losses resulting from the slightly decreased cost to buy protection in AGM's name as the market cost of AGM's credit decreased during the period. Several transactions were pricing above their floor levels; therefore when the cost of purchasing CDS protection on AGM decreased, the implied spreads that the Company would expect to receive on these transactions increased.

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

Five-Year CDS Spread on AGM
Quoted price of CDS contract (in basis points)

	As of December 31,		
	2014	2013	2012
AGM	325	525	536

One-Year CDS Spread on AGM
Quoted price of CDS contract (in basis points)

	As of December 31,		
	2014	2013	2012
AGM	85	220	257

Fair Value of Credit Derivatives Assets (Liabilities)
and Effect of AGM
Credit Spreads

	As of December 31, 2014	As of December 31, 2013
	(in millions)	
Fair value of credit derivatives before effect of AGM credit spread	$ (344)	$ (438)
Plus: Effect of AGM credit spread	136	210
Net fair value of credit derivatives	$ (208)	$ (228)

The fair value of CDS contracts at December 31, 2014, before considering the implications of AGM's credit spreads, is a direct result of continued wide credit spreads in the fixed income security markets and ratings downgrades. The asset class that remain most affected is a XXX life securitization transaction. Comparing December 31, 2014 with December 31, 2013, there was a narrowing of spreads primarily related to pooled corporate obligations. This narrowing of spreads combined with the runoff of par outstanding and termination of CDS transactions, resulted in a gain of approximately $94 million, before taking into account AGM's credit spreads.

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

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

Net Fair Value and Expected Losses of Credit Derivatives by Sector

Asset Type	Fair Value of Credit Derivative Asset (Liability), net As of December 31, 2014	Fair Value of Credit Derivative Asset (Liability), net As of December 31, 2013	Expected Loss to be (Paid) Recovered (1) As of December 31, 2014	Expected Loss to be (Paid) Recovered (1) As of December 31, 2013
	(in millions)			
Pooled corporate obligations	$ 10	$ (2)	$ —	$ —
U.S. RMBS	(7)	(9)	(4)	2
Other	(211)	(217)	(2)	(4)
Total	$ (208)	$ (228)	$ (6)	$ (2)

(1) There was no R&W benefit on credit derivatives as of December 31, 2014 and 2013.

Sensitivity to Changes in Credit Spread

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

Effect of Changes in Credit Spread As of December 31, 2014

Credit Spreads(1)	Estimated Net Fair Value (Pre-Tax)	Estimated Change in Gain/(Loss) (Pre-Tax)
	(in millions)	
100% widening in spreads	$ (373)	$ (165)
50% widening in spreads	(291)	(83)
25% widening in spreads	(251)	(43)
10% widening in spreads	(225)	(17)
Base Scenario	(208)	—
10% narrowing in spreads	(193)	15
25% narrowing in spreads	(171)	37
50% narrowing in spreads	(136)	72

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

10. Consolidated Variable Interest Entities

The Company provides financial guaranties with respect to debt obligations of special purpose entities, including VIEs. AGM does not sponsor any VIEs when underwriting third party financial guaranty insurance or credit derivative transactions, nor has it acted as the servicer or collateral manager for any VIE obligations that it insures. The transaction structure generally provides certain financial protections to the Company. This financial protection can take several forms, the most common of which are overcollateralization, first loss protection (or subordination) and excess spread. In the case of overcollateralization (i.e., the principal amount of the securitized assets exceeds the principal amount of the structured finance

obligations guaranteed by the Company), the structure allows defaults of the securitized assets before a default is experienced on the structured finance obligation guaranteed by the Company. In the case of first loss, the financial guaranty insurance policy only covers a senior layer of losses experienced by multiple obligations issued by special purpose entities, including VIEs. The first loss exposure with respect to the assets is either retained by the seller or sold off in the form of equity or mezzanine debt to other investors. In the case of excess spread, the financial assets contributed to special purpose entities, including VIEs, generate cash flows that are in excess of the interest payments on the debt issued by the special purpose entity. Such excess spread is typically distributed through the transaction's cash flow waterfall and may be used to create additional credit enhancement, applied to redeem debt issued by the special purpose entities, including VIEs (thereby, creating additional overcollateralization), or distributed to equity or other investors in the transaction.

AGM is not primarily liable for the debt obligations issued by the VIEs they insure and would only be required to make payments on these insured debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due and only for the amount of the shortfall. AGM's creditors do not have any rights with regard to the collateral supporting the debt issued by the FG VIEs. Proceeds from sales, maturities, prepayments and interest from such underlying collateral may only be used to pay Debt Service on VIE liabilities. Net fair value gains and losses on FG VIEs are expected to reverse to zero at maturity of the VIE debt, except for net premiums received and net claims paid by AGM under the financial guaranty insurance contract. The Company's estimate of expected loss to be paid for FG VIEs is included in Note 6, Expected Loss to be Paid.

Accounting Policy

The Company evaluates whether it is the primary beneficiary of its VIEs. If the Company concludes that it is the primary beneficiary, it is required to consolidate the entire VIE in the Company's financial statements and eliminate the effects of the financial guaranty insurance contracts issued by AGM on the consolidated FG VIEs debt obligations.

The primary beneficiary of a VIE is the enterprise that has both 1) the power to direct the activities of a VIE that most significantly impact the entity's economic performance; and 2) the obligation to absorb losses of the entity that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE.

As part of the terms of its financial guaranty contracts, the Company obtains certain protective rights with respect to the VIE that are triggered by the occurrence of certain events, such as failure to be in compliance with a covenant due to poor deal performance or a deterioration in a servicer or collateral manager's financial condition. At deal inception, the Company typically is not deemed to control a VIE; however, once a trigger event occurs, the Company's control of the VIE typically increases. The Company continuously evaluates its power to direct the activities that most significantly impact the economic performance of VIEs that have debt obligations insured by the Company and, accordingly, where the Company is obligated to absorb VIE losses or receive benefits that could potentially be significant to the VIE. The Company obtains protective rights under its insurance contracts that give the Company additional controls over a VIE if there is either deterioration of deal performance or in the financial health of the deal servicer. The Company is deemed to be the control party for certain VIEs under GAAP, typically when its protective rights give it the power to both terminate and replace the deal servicer, which are characteristics specific to the Company's financial guaranty contracts. If the protective rights that could make the Company the control party have not been triggered, then the VIE is not consolidated. If the Company is deemed no longer to have those protective rights, the transaction is deconsolidated.

The FG VIEs' liabilities that are insured by the Company are considered to be with recourse, because the Company guarantees the payment of principal and interest regardless of the performance of the related FG VIEs' assets. FG VIEs' liabilities that are not insured by the Company are considered to be without recourse, because the payment of principal and interest of these liabilities is wholly dependent on the performance of the FG VIEs' assets.

The Company has limited contractual rights to obtain the financial records of its consolidated FG VIEs. The FG VIEs do not prepare separate GAAP financial statements; therefore, the Company compiles GAAP financial information for them based on trustee reports prepared by and received from third parties. Such trustee reports are not available to the Company until approximately 30 days after the end of any given period. The time required to perform adequate reconciliations and analyses of the information in these trustee reports results in a one quarter lag in reporting the FG VIEs' activities. The Company records the fair value of FG VIE assets and liabilities based on modeled prices. The Company updates the model assumptions each reporting period for the most recent available information, which incorporates the impact of material events that may have occurred since the quarter lag date. Interest income and interest expense are derived from the trustee reports and included in "fair value gains (losses) on FG VIEs" in the consolidated statement of operations. The Company has elected the fair value

option for assets and liabilities classified as FG VIEs' assets and liabilities because the carrying amount transition method was not practical.

The cash flows generated by the FG VIE assets, including R&W recoveries, are classified as cash flows from investing activities. Paydowns of FG liabilities are supported by the cash flows generated by FG VIE assets, and for liabilities with recourse, possibly claim payments made by AGM under its financial guaranty insurance contracts. Paydowns of FG liabilities both with and without recourse are classified as cash flows used in financing activities by the Company. Interest income, interest expense and other expenses of the FG VIE assets and liabilities are classified as operating cash flows. Claim payments made by AGM under the financial guaranty contracts issued to the FG VIEs are eliminated upon consolidation and therefore such claim payments are treated as paydowns of FG VIE liabilities as a financing activity as opposed to an operating activity of AGM.

Consolidated FG VIEs

Number of FG VIEs Consolidated

	Year Ended December 31,	
	2014	2013
Beginning of the period, December 31	32	25
Consolidated(1)	1	11
Deconsolidated(1)	(6)	(3)
Matured	(2)	(1)
End of the period, December 31	25	32

____

(1) Net gain on deconsolidation was $102 million in 2014 and net loss on consolidation and deconsolidation was $7 million in 2013 and recorded in “fair value gains (losses) on FG VIEs” in the consolidated statement of operations.

The total unpaid principal balance for the FG VIEs' assets that were over 90 days or more past due was approximately $177 million at December 31, 2014 and $549 million at December 31, 2013. The aggregate unpaid principal of the FG VIEs' assets was approximately $670 million greater than the aggregate fair value at December 31, 2014. The aggregate unpaid principal of the FG VIEs' assets was approximately $1,490 million greater than the aggregate fair value at December 31, 2013, excluding the effect of R&W settlements. The change in the instrument-specific credit risk of the FG VIEs' assets held as of December 31, 2014 that was recorded in the consolidated statements of operations for 2014 were gains of $171 million. The change in the instrument-specific credit risk of the FG VIEs' assets held as of December 31, 2013 that was recorded in the consolidated statements of operations for 2013 were gains of $254 million. To calculate the instrument specific credit risk, the changes in the fair value of the FG VIE assets are allocated between those changes that are due to the instrument specific credit risk and those are due to other factors, including interest rates. The instrument specific credit risk amount is determined by using expected contractual cash flows vs. current expected cash flows discounted at original contractual rate. The net present value is calculated by discounting the expected cash flows of the underlying security, excluding the Company’s financial guaranty insurance, at the relevant effective interest rate.

The unpaid principal for FG VIE liabilities with recourse was $1,132 million and $1,634 million as of December 31, 2014 and December 31, 2013, respectively. FG VIE liabilities with recourse will mature at various dates ranging from 2025 to 2038. The aggregate unpaid principal balance of the FG VIE liabilities with and without recourse was approximately $548 million greater than the aggregate fair value of the FG VIEs’ liabilities as of December 31, 2014. The aggregate unpaid principal balance was approximately $1,211 million greater than the aggregate fair value of the FG VIEs’ liabilities as of December 31, 2013.

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

Consolidated FG VIEs
By Type of Collateral

	As of December 31, 2014		As of December 31, 2013	
	Assets	Liabilities	Assets	Liabilities
	(in millions)			
With recourse:				
U.S. RMBS first lien	$ 498	$ 570	$ 576	$ 730
U.S. RMBS second lien	193	260	394	545
Total with recourse	691	830	970	1,275
Without recourse	132	114	721	686
Total	$ 823	$ 944	$ 1,691	$ 1,961

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

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

	Year Ended December 31,	
	2014	2013
	(in millions)	
Net earned premiums	$ (31)	$ (58)
Net investment income	(9)	(11)
Net realized investment gains (losses)	(5)	1
Fair value gains (losses) on FG VIEs	234	343
Other income (loss)	(2)	—
Loss and LAE	31	19
Effect on net income before tax	218	294
Less: tax provision (benefit)	77	103
Effect on net income (loss)	$ 141	$ 191
Effect on cash flows from operating activities	$ 62	$ (146)

	As of December 31, 2014	As of December 31, 2013
	(in millions)	
Effect on shareholder's equity (decrease) increase	$ (25)	$ (148)

Fair value gains (losses) on FG VIEs represent the net change in fair value on the consolidated FG VIEs' assets and liabilities. In 2014, the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of $234 million. The primary driver of this gain, $102 million, was a result of the deconsolidation of five VIEs. In addition, there was a gain of $37 million resulting from the Company exercising its option to accelerate two second lien RMBS bonds. The remainder of the gain for the

period was driven by the price appreciation on the Company's FG VIE assets during the year resulting from improvements in the underlying collateral, as well as large principal paydowns made on the Company's FG VIEs.

In 2013, the Company recorded a pre-tax net fair value gain of consolidated FG VIEs of $343 million. The gain was primarily driven by R&W benefits received on several VIE assets as a result of settlements with various counterparties throughout the year. These R&W settlements resulted in a gain of approximately $265 million. The remainder of the gain was driven by price appreciation on the Company's FG VIE assets during the year resulting from improvements in the underlying collateral, as well as large principal paydowns made on the Company's FG VIEs.

Non-Consolidated VIEs

As of December 31, 2014 and December 31, 2013 the Company had issued financial guaranty contracts for approximately 430 and 440 VIEs, respectively, that it did not consolidate. To date, the Company's analyses have indicated that it does not have a controlling financial interest in any other VIEs and, as a result, they are not consolidated in the consolidated financial statements. The Company's exposure provided through its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 3, Outstanding Exposure.

11. Investments and Cash

Accounting Policy

The vast majority of the Company's investment portfolio is composed of fixed-maturity and short-term investments, classified as available-for-sale at the time of purchase (approximately 94% based on fair value at December 31, 2014), and therefore carried at fair value. Changes in fair value for other-than-temporarily-impaired ("OTTI") securities are bifurcated between credit losses and non-credit changes in fair value. The credit loss on OTTI securities is recorded in the statement of operations and the non-credit component of the change in fair value of securities whether OTTI or not, is recorded in other comprehensive income ("OCI"). For securities 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, declines in fair value are 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 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.

The Company purchases securities that it has insured, and for which it has expected losses to be paid, in order to mitigate the economic effect of insured losses ("loss mitigation securities"). These securities were purchased at a discount and are accounted for excluding the effects of the Company’s insurance.

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.

Other invested assets primarily include:

- preferred stocks, which are carried at fair value with changes in unrealized gains and losses recorded in OCI,
- trading securities, which are carried at fair value with unrealized gains and losses recorded in net income,
- a surplus note issued by AGC to AGM (see Note 16, Related Party Transactions). The surplus note is being held to maturity.

Cash consists of cash on hand and demand deposits. As a result of the lag in reporting, FG VIEs and short-term investments do not reflect cash outflow to the holders of the debt issued by the FG VIEs for claim payments made by the Company to the consolidated FG VIEs until the subsequent reporting period.

Assessment for Other-Than-Temporary Impairments

The amount of other-than-temporary-impairment recognized in earnings depends on whether (1) an entity intends to sell the security or (2) it is more-likely-than-not that the entity will be required to sell the security before recovery of its amortized cost basis.

If an entity does not intend to sell the security and it is not more-likely-than-not that the Company will be required to sell the security before recovery of its amortized cost basis, the other-than-temporary-impairment is separated into (1) the amount representing the credit loss and (2) the amount related to all other factors.

The Company has a formal review process to determine other-than-temporary-impairment 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;
- the impact of foreign exchange rates; 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 impaired and the net present value is less than the amortized cost of the investment, an other-than-temporary impairment 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 including default rates, recoveries and changes in value. The assumptions used in these projections requires the use of significant management judgment.

The Company's assessment of a decline in value included management's current assessment of the factors noted above. The Company also seeks advice from its outside investment managers. If that assessment changes in the future, the Company may ultimately record a loss after having originally concluded that the decline in value was temporary.

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 was $63 million and $60 million as of December 31, 2014 and December 31, 2013, respectively.

Net Investment Income

	Year Ended December 31,	
	2014	2013
	(in millions)	
Income from fixed-maturity securities managed by third parties	$ 185	$ 169
Income from internally managed securities:		
Fixed maturities	58	59
Other invested assets	29	22
Gross investment income	272	250
Investment expenses	(5)	(4)
Net investment income	$ 267	$ 246

Net Realized Investment Gains (Losses)

	Year Ended December 31,	
	2014	2013
	(in millions)	
Gross realized gains on available-for-sale securities	$ 7	$ 50
Gross realized gains on other assets in investment portfolio	7	7
Gross realized losses on available-for-sale securities	(1)	(5)
Gross realized losses on other assets in investment portfolio	(2)	(8)
Other-than-temporary impairment	(70)	(21)
Net realized investment gains (losses)	$ (59)	$ 23

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

Roll Forward of Credit Losses in the Investment Portfolio

	Year Ended December 31,	
	2014	2013
	(in millions)	
Balance, beginning of period	$ 34	$ 36
Additions for credit losses on securities for which an other-than-temporary-impairment was not previously recognized	63	8
Eliminations of securities issued by FG VIEs	1	—
Reductions for securities sold during the period	—	(21)
Additions for credit losses on securities for which an other-than-temporary-impairment was previously recognized	6	11
Balance, end of period	$ 104	$ 34

Investment Portfolio

Fixed-Maturity Securities and Short-Term Investments
by Security Type
As of December 31, 2014

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI (2) Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Quality(3)
	(dollars in millions)						
Fixed-maturity securities:							
Obligations of state and political subdivisions	63%	$ 3,928	$ 261	$ 0	$ 4,189	$ 1	AA
U.S. government and agencies	1	64	5	0	69	—	AA+
Corporate securities	10	632	15	(4)	643	(2)	A-
Mortgage-backed securities(4):							
RMBS	10	656	24	(19)	661	(3)	BIG
CMBS	4	258	8	0	266	—	AAA
Asset-backed securities	3	191	2	0	193	1	A
Foreign government securities	3	191	3	(3)	191	—	AA+
Total fixed-maturity securities	94	5,920	318	(26)	6,212	(3)	AA-
Short-term investments	6	377	0	0	377	—	AAA
Total investment portfolio	100%	$ 6,297	$ 318	$ (26)	$ 6,589	$ (3)	AA-

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

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Quality(3)
	(dollars in millions)						
Fixed-maturity securities:							
Obligations of state and political subdivisions	59%	$ 3,557	$ 153	$ (20)	$ 3,690	$ 0	AA
U.S. government and agencies	1	66	4	(1)	69	—	AA+
Corporate securities	10	624	13	(8)	629	—	A-
Mortgage-backed securities(4):							
RMBS	8	463	12	(37)	438	(28)	BBB-
CMBS	3	209	3	(2)	210	—	AAA
Asset-backed securities	5	298	3	(1)	300	(2)	A
Foreign government securities	3	177	9	0	186	—	AA+
Total fixed-maturity securities	89	5,394	197	(69)	5,522	(30)	AA-
Short-term investments	11	667	0	0	667	—	AAA
Total investment portfolio	100%	$ 6,061	$ 197	$ (69)	$ 6,189	$ (30)	AA-

(1) Based on amortized cost.

(2) Accumulated OCI ("AOCI"). See also Note 20, Other Comprehensive Income.

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

(4) Government-agency obligations were approximately 24% of mortgage backed securities as of December 31, 2014 and 26% as of December 31, 2013 based on fair value.

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

The following tables present the fair value of the Company's available-for-sale portfolio of obligations of state and political subdivisions as of December 31, 2014 and December 31, 2013 by state.

Fair Value of Available-for-Sale Portfolio of
Obligations of State and Political Subdivisions
As of December 31, 2014 (1)

State	State General Obligation	Local General Obligation	Revenue Bonds	Fair Value	Amortized Cost	Average Credit Rating
			(in millions)			
New York	$ 14	$ 18	$ 407	$ 439	$ 416	AA
Texas	26	174	206	406	383	AA
California	36	46	267	349	318	AA-
Florida	39	21	223	283	260	AA-
Illinois	4	61	133	198	183	A+
Washington	31	27	120	178	167	AA
Massachusetts	44	—	124	168	155	AA
Arizona	—	7	134	141	132	AA
Michigan	—	—	105	105	96	A+
Ohio	6	23	65	94	88	AA
All others	186	184	770	1,140	1,077	AA-
Total	$ 386	$ 561	$ 2,554	$ 3,501	$ 3,275	AA-

Fair Value of Available-for-Sale Portfolio of
Obligations of State and Political Subdivisions
As of December 31, 2013 (1)

State	State General Obligation	Local General Obligation	Revenue Bonds	Fair Value	Amortized Cost	Average Credit Rating
			(in millions)			
New York	$ 12	$ 33	$ 393	$ 438	$ 430	AA
Texas	44	177	167	388	373	AA
California	26	52	239	317	306	AA-
Florida	33	34	190	257	244	AA-
Illinois	—	50	113	163	158	A+
Washington	18	19	117	154	151	AA
Massachusetts	42	5	100	147	144	AA
Arizona	—	8	132	140	137	AA
Michigan	—	28	80	108	102	A+
Pennsylvania	47	23	28	98	96	A+
All others	149	136	726	1,011	976	AA-
Total	$ 371	$ 565	$ 2,285	$ 3,221	$ 3,117	AA-

(1) Excludes $688 million and $469 million as of December 31, 2014 and 2013, 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 is comprised primarily of essential service revenue bonds issued by transportation authorities and other utilities, water and sewer authorities, universities and healthcare providers.

Revenue Bonds
Sources of Funds

Type	As of December 31, 2014 Fair Value	As of December 31, 2014 Amortized Cost	As of December 31, 2013 Fair Value	As of December 31, 2013 Amortized Cost
	(in millions)			
Transportation	$ 643	$ 593	$ 486	$ 464
Tax backed	397	374	509	496
Municipal utilities	388	363	386	372
Higher education	372	350	242	239
Water and sewer	365	343	292	289
Healthcare	272	245	231	220
All others	117	111	139	135
Total	$ 2,554	$ 2,379	$ 2,285	$ 2,215

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

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

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2014

	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
	(dollars in millions)					
Obligations of state and political subdivisions	$ 61	$ 0	$ 7	$ 0	$ 68	$ 0
U.S. government and agencies	2	0	12	0	14	0
Corporate securities	151	(3)	48	(1)	199	(4)
Mortgage-backed securities:						
RMBS	172	(3)	85	(16)	257	(19)
CMBS	22	0	—	—	22	0
Asset-backed securities	24	0	—	—	24	0
Foreign government securities	108	(3)	—	—	108	(3)
Total	$ 540	$ (9)	$ 152	$ (17)	$ 692	$ (26)
Number of securities		79		34		113
Number of securities with other-than-temporary impairment		3		5		8

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

	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
			(dollars in millions)			
Obligations of state and political subdivisions	$ 705	$ (20)	$ 1	$ 0	$ 706	$ (20)
U.S. government and agencies	11	(1)	—	—	11	(1)
Corporate securities	231	(8)	2	0	233	(8)
Mortgage-backed securities:						
RMBS	81	(4)	155	(33)	236	(37)
CMBS	91	(2)	—	—	91	(2)
Asset-backed securities	151	(1)	—	—	151	(1)
Foreign government securities	12	0	1	0	13	0
Total	$ 1,282	$ (36)	$ 159	$ (33)	$ 1,441	$ (69)
Number of securities		280		20		300
Number of securities with other-than-temporary impairment		7		10		17

Of the securities in an unrealized loss position for 12 months or more as of December 31, 2014, three securities had unrealized losses greater than 10% of book value. The total unrealized loss for these securities as of December 31, 2014 was $15 million. The Company has determined that the unrealized losses recorded as of December 31, 2014 are yield related and not the result of other-than-temporary-impairment.

The amortized cost and estimated fair value of available-for-sale fixed-maturity securities by contractual maturity as of December 31, 2014 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, 2014

	Amortized Cost	Estimated Fair Value
	(in millions)	
Due within one year	$ 69	$ 69
Due after one year through five years	1,077	1,107
Due after five years through 10 years	1,455	1,538
Due after 10 years	2,405	2,571
Mortgage-backed securities:		
RMBS	656	661
CMBS	258	266
Total	$ 5,920	$ 6,212

The investment portfolio contains securities that are either held in trust for the benefit of reinsurers in accordance with statutory requirements, placed on deposit to fulfill state licensing requirements, or otherwise restricted in the amount of $50 million and $32 million as of December 31, 2014 and December 31, 2013, respectively, based on fair value. In addition, as noted in Note 16, Related Party Transactions, the total collateral required to be funded into a reinsurance trust account by AGM for the benefit of AGE as of December 31, 2014 was approximately £142 million.

AGM also posted $238 million, which was held in trust, for the benefit of AGE.

No material investments of the Company were non-income producing for years ended December 31, 2014, and 2013 respectively.

Internally Managed Portfolio

The investment portfolio tables shown above include both assets managed externally and internally. In the table below, more detailed information is provided for the component of the total investment portfolio that is internally managed (excluding short-term investments). The internally managed portfolio, as defined below, represents approximately 11% and 10% of the investment portfolio, on a fair value basis as of December 31, 2014 and December 31, 2013, respectively. The internally managed portfolio consists primarily of the Company's investments in securities for (i) loss mitigation purposes, (ii) other risk management purposes and (iii) where the Company believes a particular security presents an attractive investment opportunity.

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

Additional detail about the types and amounts of securities acquired by the Company for loss mitigation, other risk management and in the trading portfolio is set forth in the table below.

Internally Managed Portfolio
Carrying Value

	As of December 31, 2014	As of December 31, 2013
	(in millions)	
Assets purchased for loss mitigation and other risk management purposes:		
Fixed maturity securities	$ 634	$ 554
Other invested assets	28	59
Other	79	47
Total	$ 741	$ 660

12. Investment in MAC Holdings

On July 16, 2013, subsidiaries of Assured Guaranty Ltd. completed a series of transactions that increased the capitalization of its subsidiary, MAC, to $800 million on a statutory basis.

AGM and its subsidiaries Assured Guaranty Municipal Insurance Company ("AGMIC") and Assured Guaranty (Bermuda) Ltd. ("AGBM") terminated the reinsurance pooling agreement pursuant to which AGMIC and AGBM had assumed a quota share percentage of the financial guaranty insurance policies issued by AGM, and AGM reassumed such ceded business. Subsequently, AGMIC was merged into AGM, with AGM as the surviving company.

AGBM, which had made a loan of $82.5 million to Assured Guaranty US Holdings Inc. ("AGUS"), an indirect parent holding company of AGM, received all of the outstanding shares of MAC held by AGUS and cash, in full satisfaction of the principal of and interest on such loan. After AGBM distributed substantially all of its assets, including the MAC shares, to AGM as a dividend, AGM sold AGBM to its affiliate Assured Guaranty Re Ltd. (“AG Re”). Subsequently, AGBM and AG Re merged, with AG Re as the surviving company. The sale of AGBM to, and subsequent merger with, AG Re were each effective as of July 17, 2013.

MAC Holdings, was formed to own 100% of the outstanding stock of MAC. AGM and its affiliate AGC subscribed for approximately 61% and 39% of the outstanding MAC Holdings common stock, respectively, for which AGM paid $425

million and AGM's affiliate AGC paid $275 million, as consideration. The consideration consisted of all of MAC's outstanding common stock (in the case of AGM), cash and marketable securities.

MAC Holdings then contributed cash and marketable securities having a fair market value sufficient to increase MAC's policyholders' surplus to approximately $400 million, and purchased a surplus note issued by MAC in the principal amount of $300 million. In addition, AGM purchased a surplus note issued by MAC in the principal amount of $100 million

Following the increase in MAC's capitalization, AGM ceded par exposure of approximately $87 billion and unearned premiums of approximately $468 million to MAC, and AGC ceded par exposure of approximately $24 billion and unearned premiums of approximately $249 million to MAC.

In addition, on July 15, 2013, AGM and its wholly-owned subsidiary, AGE (together, the "AGM Group"), were notified that the New York State Department of Financial Services ("NYDFS") does not object to the AGM Group reassuming contingency reserves that they had ceded to AG Re and electing to cease ceding future contingency reserves to AG Re under the following circumstances:

- The AGM Group may reassume 33% of a contingency reserve base of approximately $250 million (the “NY Contingency Reserve Base”) in 2013, after July 16, 2013, the date on which the transactions for the capitalization of MAC were completed (the “Closing Date”).

- The AGM Group may reassume 50% of the NY Contingency Reserve Base in 2014, no earlier than the one year anniversary of the Closing Date, with the prior approval of the NYDFS.

- The AGM Group may reassume the remaining 17% of the NY Contingency Reserve Base in 2015, no earlier than the two year anniversary of the Closing Date, with the prior approval of the NYDFS.

The reassumption of the contingency reserves has the effect of increasing contingency reserves by the amount reassumed and decreasing policyholders' surplus by the same amount; there would be no impact on the statutory or rating agency capital as a result of the reassumption. The reassumption of contingency reserves would permit the release of amounts from the AG Re trust accounts securing AG Re's reinsurance of the AGM Group.

In the third quarter of 2013, AGM reassumed 33% of its contingency reserve bases, which permitted the release of approximately $53 million of assets from the AG Re trust accounts securing AG Re's reinsurance of AGM, after adjusting for increases in the amounts required to be held in such accounts due to changes in asset values.

In the third quarter of 2014, AGM reassumed 50% of its contingency reserve base (approximately $110 million). In addition, in the fourth quarter of 2014, AGE reassumed 83% (representing the first and second installments of the approved reassumption) of its portion of the NY Contingency Reserve Base (approximately $24.5 million in the aggregate). These 2014 reassumptions collectively permitted the release of approximately $133 million of assets from the AG Re trust accounts securing AG Re's reinsurance of the AGM Group and AGC, after taking into account other, normal-course adjustments to AG Re’s collateral requirements such as changes in asset values and changes in assumed reserves.

As noted above, AGUS repaid the $82.5 million loan from AGBM with the outstanding shares of MAC that AGUS held and with cash. At the time of the capitalization transactions, MAC had the following assets and liabilities:

	July 1, 2013 (in millions)
Assets	
Investments	$ 72.5
Cash	0.0
Intangible assets	16.0
Other assets	2.3
Total assets	$ 90.8
Liabilities	
Other liabilities	$ 2.4
Total liabilities	$ 2.4

13. Insurance Company Regulatory Requirements

The Company's ability to pay dividends depends, among other things, upon their 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 their state of domicile and other states. Financial statements prepared in accordance with accounting practices prescribed or permitted by local insurance regulatory authorities differ in certain respects from GAAP.

The Company's U.S. domiciled insurance companies prepare statutory financial statements in accordance with accounting practices prescribed or permitted by the National Association of Insurance Commissioners ("NAIC") and their respective insurance departments. Prescribed statutory accounting practices are set forth in the NAIC Accounting Practices and Procedures Manual. The Company has no permitted accounting practices on a statutory basis.

GAAP differs in certain significant respects from U.S. insurance companies' statutory accounting practices prescribed or permitted by insurance regulatory authorities. The principal differences result from the following statutory accounting practices:

- upfront premiums are earned when related principal and interest have expired rather than earned over the expected period of coverage;
- acquisition costs are charged to expense as incurred rather than over the period that related premiums are earned;
- a contingency reserve is computed based on statutory requirements, but no such reserve is required under GAAP;
- certain assets designated as "non-admitted assets" are charged directly to statutory surplus, but are reflected as assets under GAAP;
- investments in subsidiaries are carried on the balance sheet on the equity basis, to the extent admissible, rather than consolidated with the parent;
- the amount of deferred tax assets that may be admitted is subject to an adjusted surplus threshold and is generally limited to the lesser of those assets the Company expects to realize within three years of the balance sheet date or fifteen percent of the Company's adjusted surplus. This realization period and surplus percentage is subject to change based on the amount of adjusted surplus. Under GAAP there is no non-admitted asset determination, rather a valuation allowance is recorded to reduce the deferred tax asset to an amount that is more likely than not to be realized;
- insured credit derivatives are accounted for as insurance contracts rather than as derivative contracts measured at fair value;
- bonds are generally carried at amortized cost rather than fair value;
- VIEs and refinancing vehicles are not consolidated;
- payment of principal and interest on surplus notes is recorded only upon approval of the insurance regulator rather than periodic accrual of interest;
- push-down acquisition accounting is not applicable under statutory accounting practices, as it is under GAAP;
- expected losses are discounted at a rate of 5%, recorded when the loss is deemed probable and without consideration of the deferred premium revenue rather than discounted at the risk free rate at the end of each reporting period and only to the extent they exceed deferred premium revenue;
- the present value of installment premiums and commissions are not recorded on the balance sheet as they are under GAAP.

Insurance Regulatory Amounts Reported

	Policyholders' Surplus As of December 31, 2014	Policyholders' Surplus As of December 31, 2013	Net Income (Loss) Year Ended December 31, 2014	Net Income (Loss) Year Ended December 31, 2013
	(in millions)			
AGM(1)	$ 2,267	$ 1,733	$ 304	$ 340
MAC	612	514	75	26

(1) Policyholders' surplus of AGM includes its indirect share of MAC. AGM owns approximately 61% of the outstanding stock of Municipal Assurance Holdings Inc. ("MAC Holdings"), which owns 100% of the outstanding common stock of MAC.

From time to time, AGM has obtained approval from its regulator to release contingency reserves based on losses or because the accumulated reserve is deemed excessive in relation to the insurer's outstanding insured obligations. In 2014, on the latter basis, AGM obtained NYDFS approval for a contingency reserve release of approximately $588 million.

Dividend Restrictions and Capital Requirements

Under New York insurance law, AGM may only pay dividends out of "earned surplus", which is the portion of a company's surplus that represents the net earnings, gains or profits (after deduction of all losses) that have not been distributed to shareholders as dividends or transferred to stated capital or capital surplus, or applied to other purposes permitted by law, but does not include unrealized appreciation of assets. AGM may pay dividends without the prior approval of the New York Superintendent of Financial Services ("New York Superintendent") that, together with all dividends declared or distributed by it during the preceding 12 months, does not exceed the lesser of 10% of its policyholders' surplus (as of the last annual or quarterly statement filed with the New York Superintendent) or 100% of its adjusted net investment income during that period. The maximum amount available during 2015 for AGM to distribute as dividends without regulatory approval, after giving effect to dividends paid in the prior 12 months, is estimated to be approximately $227 million, of which approximately $67 million is available for distribution in the first quarter of 2015.

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

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

Dividends and Surplus Notes
By Insurance Company

	Year Ended December 31, 2014	Year Ended December 31, 2013
	(in millions)	
Dividends paid by AGM to AGMH	$ 160	$ 163
Repayment of surplus note by AGM to AGMH	50	50
Issuance of surplus notes by MAC to MAC Holdings(1)	—	(300)
Issuance of surplus notes by MAC to AGM(1)	—	(100)

(1) The surplus notes issued by MAC are eliminated in consolidation.

14. 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.

Non-interest-bearing tax and loss bonds are purchased in the amount of the tax benefit that results from deducting contingency reserves as provided under Internal Revenue Code Section 832(e). The Company records the purchase of tax and loss bonds in deferred taxes.

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

Overview

In conjunction with AGL's purchase of AGMH on July 1, 2009, AGM and its insurance company subsidiaries have joined the consolidated federal tax group of Assured Guaranty US Holdings Inc. ("AGUS"), an indirect parent holding company of AGM. A new tax sharing agreement was entered into effective July 1, 2009, subsequently amended to include MAC, whereby each company in the AGUS consolidated tax group pays or receives its proportionate share of the consolidated federal tax burden for the group as if each company filed on a separate return basis with current period credit for net losses. Beginning on May 31, 2012, MAC also joined the AGUS consolidated tax group.

Provision for Income Taxes

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

Effective Tax Rate Reconciliation

	Year Ended December 31,	
	2014	2013
	(in millions)	
Expected tax provision (benefit) at statutory rate	$ 270	$ 359
Tax-exempt interest	(44)	(41)
Change in liability for uncertain tax positions	6	—
Other	(3)	4
Total provision (benefit) for income taxes	$ 229	$ 322
Effective tax rate	29.6%	31.4%

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

Components of Net Deferred Tax Assets

	As of December 31,	
	2014	2013
	(in millions)	
Deferred tax assets:		
Unrealized losses on credit derivative financial instruments, net	$ 79	$ 75
Unearned premium reserves, net	93	87
Loss and LAE reserve	47	108
Tax and loss bonds	39	21
Deferred ceding commission income	31	34
Foreign tax credit	—	27
FG VIEs	9	18
Deferred compensation	15	8
Investment basis difference	66	58
Other	9	8
Total deferred income tax assets	388	444
Deferred tax liabilities:		
Contingency reserves	64	25
Unrealized appreciation on committed capital securities	16	7
Unrealized appreciation on investments	106	45
Market discount	30	24
Other	11	12
Total deferred income tax liabilities	227	113
Net deferred income tax asset	$ 161	$ 331

The Company has utilized all of its foreign tax credit carry-forward balances as of December 31, 2014.

Valuation Allowance

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

Audits

AGUS has open tax years with the U.S. Internal Revenue Service ("IRS") for 2009 forward and is currently under audit for the 2009 - 2012 tax years. The IRS concluded its field work with respect to tax years 2006 through 2008 without adjustment. On February 20, 2013 the IRS notified AGUS that the Joint Committee on Taxation completed its review of the 2006 through 2008 tax years and has accepted the results of the IRS examination without exception. AGMH and subsidiaries have separate open tax years with the IRS of January 1, 2009 through the July 1, 2009 when they joined the AGUS consolidated group. The IRS concluded its field work with respect to tax years 2008 for AGMH and subsidiaries while members of the Dexia Holdings Inc. consolidated tax group without adjustment. The Company is indemnified by Dexia for any potential liability associated with any audit of any periods prior to the acquisition of AGMH. The Company's U.K. subsidiary, AGE, is not currently under examination and has open tax years of 2012 forward.

Uncertain Tax Positions

The following table provides a reconciliation of the beginning and ending balances of the total liability for unrecognized tax benefits. The Company does not believe it is reasonably possible that this amount will change significantly in the next twelve months.

	2014	2013
	(in millions)	
Balance as of January 1,	$ 5	$ 5
True-up from tax return filings	6	—
Balance as of December 31,	$ 11	$ 5

The Company's policy is to recognize interest and penalties related to uncertain tax positions in income tax expense and has accrued $0.5 million for 2014 and $0.3 million for 2013. As of December 31, 2014 and December 31, 2013, the Company had accrued $2.3 million and $1.7 million of interest, respectively.

The total amount of unrecognized tax benefits at December 31, 2014, that would affect the effective tax rate, if recognized, was $11 million.

Tax Treatment of CDS

The Company treats the guaranty it provides on CDS as an insurance contract for tax purposes and as such a taxable loss does not occur until the Company expects to make a loss payment to the buyer of credit protection based upon the occurrence of one or more specified credit events with respect to the contractually referenced obligation or entity. The Company holds its CDS to maturity, at which time any unrealized fair value loss in excess of credit-related losses would revert to zero. The tax treatment of CDS is an unsettled area of the law. The uncertainty relates to the IRS determination of the income or potential loss associated with CDS as either subject to capital gain (loss) or ordinary income (loss) treatment. In treating CDS as insurance contracts the Company treats both the receipt of premium and payment of losses as ordinary income and believes it is more likely than not that any CDS credit related losses will be treated as ordinary by the IRS. To the extent the IRS takes the view that the losses are capital losses in the future and the Company incurred actual losses associated with the CDS, the Company would need sufficient taxable income of the same character within the carryback and carryforward period available under the tax law.

15. Reinsurance and Other Monoline Exposures

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

Accounting Policy

For business assumed and ceded, the accounting model of the underlying direct financial guaranty contract dictates the accounting model used for the reinsurance contract (except for those eliminated as FG VIEs). For any assumed or ceded financial guaranty insurance premiums, the accounting model described in Note 4 is followed, for assumed and ceded financial guaranty insurance losses, the accounting model in Note 7 is followed. For any ceded credit derivative contracts, the accounting model in Note 9 is followed.

Ceded and Assumed Business

The Company has Ceded Business to affiliated and non-affiliated companies to limit its exposure to risk. Under these relationships, the Company cedes a portion of its insured risk in exchange for a premium paid to the reinsurer. The Company remains primarily liable for all risks it directly underwrites and is required to pay all gross claims. It then seeks reimbursement from the reinsurer for its proportionate share of claims. The Company may be exposed to risk for this exposure if it were required to pay the gross claims and not be able to collect ceded claims from an assuming company experiencing financial distress. A number of the financial guaranty insurers to which the Company has ceded par have experienced financial distress

and been downgraded by the rating agencies as a result. In addition, state insurance regulators have intervened with respect to some of these insurers. The Company's ceded contracts generally allow the Company to recapture Ceded Business after certain triggering events, such as reinsurer downgrades.

AGM is also party to reinsurance agreements as a reinsurer to its affiliated financial guaranty insurance companies.

The Company has assumed business primarily from its affiliate, AGC. Under this relationship, the Company assumes a portion of the ceding company's insured risk in exchange for a premium. The Company may be exposed to risk in this portfolio in that the Company may be required to pay losses without a corresponding premium in circumstances where the ceding company is experiencing financial distress and is unable to pay premiums. The Company's agreement with AGC is generally subject to termination at the option of the ceding company if the Company fails to meet certain financial and regulatory criteria or to maintain a specified minimum financial strength rating. Upon termination under these conditions, the Company may be required to return to the ceding company unearned premiums and loss reserves calculated on a statutory basis of accounting, attributable to the reinsurance assumed, after which the Company would be released from liability with respect to the Assumed Business. Upon the occurrence of the conditions set forth above, whether or not an agreement is terminated, the Company may be obligated to increase the level of ceding commission paid. In 2013, MAC assumed a book of U.S. public finance business from AGM and AGC. See Note 12, Investment in MAC Holdings for a description of the affiliated reinsurance transactions.

Over the past several years, the Company has entered into several commutations in order to reassume previously ceded books of business from its reinsurers.

Net Effect of Commutations of Ceded Reinsurance Contracts

	Year Ended December 31,	
	2014	2013
	(in millions)	
Increase in net unearned premium reserve	$ 20	$ 11
Increase in net par outstanding	1,091	151
Commutation gains recorded in other income	23	2

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

Effect of Reinsurance on Statement of Operations

	Year Ended December 31,	
	2014	2013
	(in millions)	
Premiums Written:		
Direct	$ 89	$ 123
Assumed(1)	0	248
Ceded	(31)	(47)
Net	$ 58	$ 324
Premiums Earned:		
Direct	$ 476	$ 690
Assumed	26	13
Ceded	(128)	(195)
Net	$ 374	$ 508
Loss and LAE:		
Direct	$ 48	$ 163
Ceded	(73)	(71)
Net	$ (25)	$ 92

(1) For 2013, primarily represents par assumed by MAC from AGC.

Reinsurer Exposure

In addition to assumed and ceded reinsurance arrangements, the Company may also have exposure to some financial guaranty reinsurers (i.e., monolines) in other areas. Second-to-pay insured par outstanding represents transactions the Company has insured that were previously insured by other monolines. The Company underwrites such transactions based on the underlying insured obligation without regard to the primary insurer. Another area of exposure is in the investment portfolio where the Company holds fixed-maturity securities that are wrapped by monolines and whose value may decline based on the rating of the monoline. As of December 31, 2014, based on fair value, the Company had fixed-maturity securities in its investment portfolio consisting of $298 million insured by National Public Finance Guarantee Corporation ("NPFGC"), $223 million insured by Ambac Assurance Corporation ("Ambac"), $86 million insured by AGC, and $29 million insured by other guarantors.

Exposure by Reinsurer

Reinsurer	Ratings at March 19, 2015		Par Outstanding (1) As of December 31, 2014		
	Moody's Reinsurer Rating	S&P Reinsurer Rating	Ceded Par Outstanding	Second-to-Pay Insured Par Outstanding	Assumed Par Outstanding
				(dollars in millions)	
Affiliated Companies: (2)					
AGC	A3	AA	$ —	$ 493	$ 22,018
AG Re	Baa1	AA	58,891	—	—
Affiliated Companies			58,891	493	22,018
Non-Affiliated Companies:					
American Overseas Reinsurance Company Limited (f/k/a Ram Re)	WR(3)	WR	5,535	—	30
Tokio Marine & Nichido Fire Insurance Co., Ltd.	Aa3(4)	AA-(4)	5,280	—	—
Radian Asset Assurance Inc.	Ba1	B+	4,045	19	—
Syncora Guarantee Inc.	WR	WR	3,715	609	—
Mitsui Sumitomo Insurance Co. Ltd.	A1	A+(4)	2,043	—	—
ACA Financial Guaranty Corp.	NR(6)	WR	746	2	—
Swiss Reinsurance Co.	Aa3	AA-	93	—	—
NPFGC (7)	A3	AA-	—	4,354	—
Ambac	WR	WR	—	2,700	—
MBIA	(5)	(5)	—	1,996	—
Financial Guaranty Insurance Co.	WR	WR	—	999	—
Ambac Assurance Corp. Segregated Account	NR	NR	—	107	—
CIFG Assurance North America Inc.	WR	WR	—	45	—
Other	Various	Various	—	—	1
Non-Affiliated Companies			21,457	10,831	31
Total			$ 80,348	$ 11,324	$ 22,049

(1) Includes par related to insured credit derivatives.

(2) MAC is rated AA+ (stable outlook) from KBRA and of AA (stable outlook) from S&P. Assumed par outstanding includes $21,988 million assumed by MAC from AGC.

(3) Represents "Withdrawn Rating."

(4) The Company has structural collateral agreements satisfying the triple-A credit requirement of S&P and/or Moody's.

(5) MBIA includes subsidiaries MBIA Insurance Corp. rated B by S&P and B2 by Moody's and MBIA U.K. Insurance Ltd. rated B by S&P and Ba2 by Moody's.

(6) Represents "Not Rated."

(7) NPFGC is also rated AA+ from KBRA.

Ceded Par Outstanding by Reinsurer and Credit Rating
As of December 31, 2014

Reinsurer	AAA	AA	A	BBB	BIG	Total
			(in millions)			
Affiliated Companies	$ 985	$ 15,309	$ 28,950	$ 12,150	$ 1,497	$ 58,891
American Overseas Reinsurance Company Limited (f/k/a Ram Re)	282	2,161	1,697	990	405	5,535
Tokio Marine & Nichido Fire Insurance Co., Ltd.	763	972	1,485	1,281	779	5,280
Radian Asset Assurance Inc.	207	327	1,984	1,038	489	4,045
Syncora Guarantee Inc.	—	291	498	2,193	733	3,715
Mitsui Sumitomo Insurance Co. Ltd.	134	679	742	299	189	2,043
ACA Financial Guaranty Corp.	—	458	277	11	—	746
Swiss Reinsurance Co.	—	—	0	26	67	93
Total	$ 2,371	$ 20,197	$ 35,633	$ 17,988	$ 4,159	$ 80,348

In accordance with U.S. statutory accounting requirements and U.S. insurance laws and regulations, in order for the Company to receive credit for liabilities ceded to reinsurers domiciled outside of the U.S., such reinsurers must secure their liabilities to the Company. All of the unauthorized reinsurers in the table above are required to post collateral for the benefit of the Company in an amount at least equal to the sum of their ceded unearned premium reserve, loss reserves and contingency reserves all calculated on a statutory basis of accounting. In addition, certain authorized reinsurers in the table above post collateral on terms negotiated with the Company. Collateral may be in the form of letters of credit or trust accounts. The total collateral posted by all affiliated and non-affiliated reinsurers as of December 31, 2014 is approximately $1.2 billion.

Second-to-Pay
Insured Par Outstanding by Rating
As of December 31, 2014(1)

	Public Finance					Structured Finance				
	AAA	AA	A	BBB	BIG	AAA	AA	BBB	BIG	Total
					(in millions)					
Affiliated Companies	$ —	$ 84	$ —	$ —	$ —	$ —	$ 409	$ —	$ —	$ 493
Non-Affiliated Companies:										
Radian Asset Assurance Inc.	—	—	2	10	7	—	—	—	—	19
Syncora Guarantee Inc.	—	25	108	297	179	—	—	—	—	609
ACA Financial Guaranty Corp.	—	1	—	1	—	—	—	—	—	2
NPFGC	121	1,604	2,629	—	—	—	—	—	—	4,354
Ambac	29	909	1,435	283	—	—	—	38	6	2,700
MBIA	—	47	255	248	—	—	1,268	73	105	1,996
Financial Guaranty Insurance Co.	—	14	552	25	189	186	—	—	33	999
Ambac Assurance Corp. Segregated Account	—	—	—	—	—	—	32	—	75	107
CIFG Assurance North America Inc.	—	4	15	1	25	—	—	—	—	45
Non-Affiliated Companies:	150	2,604	4,996	865	400	186	1,300	111	219	10,831
Total	$ 150	$ 2,688	$ 4,996	$ 865	$ 400	$ 186	$ 1,709	$ 111	$ 219	$ 11,324

(1) Assured Guaranty's internal rating.

Amounts Due (To) From Reinsurers
As of December 31, 2014

	Assumed Premium	Ceded Premium, net of Commissions	Ceded Expected Loss and LAE
		(in millions)	
AGC	$ 2	$ —	$ —
AG Re	—	(55)	68
American Overseas Reinsurance Company Limited	—	(7)	10
Tokio Marine & Nichido Fire Insurance Co., Ltd.	—	(13)	46
Radian Asset Assurance Inc.	—	(13)	19
Syncora Guarantee Inc.	—	(29)	4
Mitsui Sumitomo Insurance Co. Ltd.	—	(3)	15
Swiss Reinsurance Co.	—	(2)	6
Other	—	(17)	—
Total	$ 2	$ (139)	$ 168

Excess of Loss Reinsurance Facility

AGC, AGM and MAC entered into an aggregate excess of loss reinsurance facility with a number of reinsurers, effective as of January 1, 2014. Currently, the facility covers losses occurring from January 1, 2015 through December 31, 2021, subject to the payment of certain additional premium by AGC, AGM and MAC on or before January 1, 2016. If AGC, AGM and MAC elect not to pay such additional premium, the facility terminates on January 1, 2016. The facility covers certain U.S. public finance credits insured or reinsured by AGC, AGM and MAC as of September 30, 2013, excluding credits that were rated non-investment grade as of December 31, 2013 by Moody's or S&P or internally by AGC, AGM or MAC and is subject to certain per credit limits. Among the credits excluded are those associated with the Commonwealth of Puerto Rico and its related authorities and public corporations. The facility attaches when AGC's, AGM's and MAC's net losses (net of AGC's and AGM's reinsurance (including from affiliates) and net of recoveries) exceed $1.5 billion in the aggregate. The facility covers a portion of the next $500 million of losses, with the reinsurers assuming pro rata in the aggregate $450 million of the $500 million of losses and AGC, AGM and MAC jointly retaining the remaining $50 million of losses. The reinsurers are required to be rated at least AA- or to post collateral sufficient to provide AGM, AGC and MAC with the same reinsurance credit as reinsurers rated AA-. AGM, AGC and MAC are obligated to pay the reinsurers their share of recoveries relating to losses during the coverage period in the covered portfolio. AGC, AGM and MAC paid approximately $19 million of premiums for the term January 1, 2014 through December 31, 2014 and also paid approximately $19 million of premiums for the term January 1, 2015 through December 31, 2015.

16. Related Party Transactions

Guarantees or Contingencies for Related Parties

AGM currently provides support to its subsidiary AGE through a quota share and excess of loss reinsurance agreement (the "Reinsurance Agreement") and a net worth maintenance agreement (the "Net Worth Agreement"). Such agreements replace and supersede the second amended and restated quota share and stop loss reinsurance agreement and the second amended and restated net worth maintenance agreement, respectively, previously in place between the parties. For transactions closed prior to 2011, AGE typically guaranteed all of the guaranteed obligations directly and AGM reinsured under the quota share cover of the Reinsurance Agreement approximately 92% of AGE's retention after cessions to other reinsurers. In 2011, AGE and AGM implemented a co-guarantee structure pursuant to which (i) AGE directly guarantees a portion of the guaranteed obligations in an amount equal to what would have been AGE's pro rata retention percentage under the quota share cover, (ii) AGM directly guarantees the balance of the guaranteed obligations, and (iii) AGM also provides a second-to-pay guarantee for AGE's portion of the guaranteed obligations.

Under the excess of loss cover of the Reinsurance Agreement, AGM will pay AGE quarterly the amount by which (i) the sum of (a) AGE's incurred losses calculated in accordance with UK GAAP as reported by AGE in its financial returns filed with the Prudential Regulation Authority ("PRA") and (b) AGE's paid losses and LAE, in both cases net of all other performing reinsurance, including the reinsurance provided by AGM under the quota share cover of the Reinsurance Agreement, exceeds (ii) an amount equal to (a) AGE's capital resources under U.K. law minus (b) the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K. In addition, the Reinsurance Agreement permits AGE to terminate the Reinsurance Agreement upon the following events: a downgrade of AGM's ratings by Moody's below Aa3 or by S&P below AA- if the company fails to restore its rating(s) to the required level within a prescribed period of time; AGM's insolvency; failure by AGM to maintain the minimum capital required by its domiciliary jurisdiction; or AGM filing a petition in bankruptcy, going into liquidation or rehabilitation or having a receiver appointed. The Reinsurance Agreement also provides that no amounts are owing under the excess of loss cover (or the stop loss cover of the second amended and restated quota share and stop loss reinsurance agreement previously in place between the parties) with respect to any quarter ending prior to April 1, 2014.

The quota share and excess loss covers each exclude transactions guaranteed by AGE on or after July 1, 2009 that are not municipal, utility, project finance or infrastructure risks or similar types of risks.

The Reinsurance Agreement also contemplates the establishment of collateral by AGM to support its reinsurance obligations to AGE. In December 2014, to satisfy a new PRA requirement that AGM post collateral to support its reinsurance obligations to AGE, AGM and AGE amended the Reinsurance Agreement to incorporate the PRA's requirement. Pursuant to such amended Reinsurance Agreement, AGM's collateral requirement will be measured as of the end of each calendar quarter by (i) using the PRA's FG Benchmark Model to calculate at the 99.5% confidence interval the losses expected to be borne collectively by AGE's three affiliated reinsurers, AGM, Assured Guaranty Re Ltd. ("AG Re") and Assured Guaranty Re Overseas Ltd. ("AGRO"); (ii) deducting from such calculation AGE's capital resources under such model; and (iii) requiring AGM, AG Re and AGRO collectively to maintain collateral equal to fifty percent (50%) of such difference, i.e., the excess

of AGM's, AG Re's and AGRO's assumed modeled losses over AGE's capital resources. The FG Benchmark Model is the model currently used by the PRA to determine the capital adequacy of UK financial guaranty companies. It broadly adopts Basel II's risk weighting approach for setting bank capital requirements, but with certain modifications to account for differences between banks and financial guarantors. In December 2014, AGM and AGE also entered into a related trust agreement pursuant to which AGM, prior to year-end, established, and deposited assets into, a reinsurance trust account for the benefit of AGE to satisfy the PRA's collateral requirement as of September 30, 2014, as measured in accordance with such amended Reinsurance Agreement. The total collateral required to be funded into such reinsurance trust account by AGM as of December 31, 2014 was approximately £142 million.

Pursuant to the Net Worth Agreement, AGM is obligated to cause AGE to maintain capital resources equal to 110% of the greatest of the amounts as may be required by the PRA as a condition for AGE to maintain its authorization to carry on a financial guarantee business in the U.K., provided that AGM's contributions (a) do not exceed 35% of its policyholders' surplus on an accumulated basis as determined by the laws of the State of New York, and (b) are in compliance with Section 1505 of the New York Insurance Law. AGM has never been required to make any contributions to AGE's capital under the current Net Worth Agreement or the prior net worth maintenance agreement.

Management, Service Contracts or Cost Sharing Arrangements

In 2010, the Company entered into a service agreement with various of its affiliates, including AGC, pursuant to which AGC makes available to it certain equipment, insurance and/or services, including underwriting, actuarial, surveillance, marketing, claims handling, legal, information technologies, corporate secretarial, human resources, accounting, tax, financial reporting and investment planning services. In addition, under the agreement the Company makes available to AGC and the other affiliate parties the use of certain equipment and office space owned by the Company. Expenses are allocated directly where appropriate and, where not appropriate, based upon an allocation of employee time and corresponding office overhead. The agreement provides for quarterly settlements and an express right of offset with regard to amounts owing between parties under this Agreement and other agreements between such parties.

See Note 19, Employee Benefit Plans for expenses related to Long-Term Compensation Plans of AGL which are allocated to AGM. For the years ended December 31, 2014 and 2013, the Company was allocated expenses of $79 million and $72 million, respectively, under these affiliate expense sharing agreements.

The following table summarizes the amounts due (to) from affiliate companies under the expense sharing agreements.

Amounts Due (To) From Affiliated Companies

	As of December 31,	
	2014	2013
	(in millions)	
Affiliated companies		
Assured Guaranty Corp.	$ (47)	$ (50)
Assured Guaranty Ltd.	(4)	(3)
Assured Guaranty Finance Overseas Ltd.	(2)	(2)
Other	(4)	(1)
Total	$ (57)	$ (56)

Assured Guaranty Re Ltd.

The Company cedes business to AG Re under certain reinsurance agreements. The following table summarizes the affiliated components of each balance sheet item, where applicable.

	As of December 31,	
	2014	2013
	(in millions)	
Assets:		
Ceded unearned premium reserve (1)	$ 591	$ 611
Reinsurance recoverable on unpaid losses	55	30
Reinsurance recoverable on paid losses(2)	1	7
Profit commission receivable (2)	1	2
Net credit derivative assets	24	28
Liabilities:		
Ceded premium payable, net of ceding commission	55	73
Ceded salvage and subrogation recoverable	2	5
Ceded funds held	30	59
Other liabilities (3)	111	108
Other information:		
Exposure		
Ceded par outstanding	58,891	61,333

(1) Includes $3 million and $6 million of ceded contra-paid on losses at December 31, 2014 and December 31, 2013, respectively.

(2) Included in other assets on the consolidated balance sheets.

(3) Represents deferred ceding commissions.

The table below summarizes ceded activity to AG Re reflected in the consolidated statements of operations.

	Year Ended December 31,	
	2014	2013
	(in millions)	
Revenues:		
Net earned premiums	$ (75)	$ (98)
Profit commission income	1	2
Realized gains and other settlements on credit derivatives	(1)	(7)
Net unrealized gains (losses) on credit derivatives	(7)	(14)
Expenses:		
Loss and loss adjustment expenses (recoveries)	(30)	(41)
Commissions incurred (earned)	(13)	(27)

Assured Guaranty Corp.

The Company assumes business from AGC under certain reinsurance agreements. The following table summarizes the affiliated components of each balance sheet item, where applicable.

	As of December 31,	
	2014	2013
	(in millions)	
Assets:		
Premium receivable	$ 2	$ 3
Liabilities:		
Unearned premium reserve	209	236

The table below summarizes assumed activity from AGC reflected in the consolidated statements of operations.

	Year Ended December 31,	
	2014	2013
	(in millions)	
Revenues:		
Net earned premiums	$ 26	$ 13

Other Invested Assets

Surplus Note from AGC

On December 18, 2009, AGC issued a surplus note with a principal amount of $300 million to AGM. This note carries a simple interest rate of 5.0% per annum and matures on December 31, 2029. Principal is payable at the option of AGC prior to the final maturity of the note in 2029 and interest is payable on the note annually in arrears as of December 31 of each year, commencing December 31, 2010. Payments of principal and interest are subject to AGC having policyholders' surplus in excess of statutory minimum requirements after such payment and to prior written approval by the Maryland Insurance Administration. AGM recognized $15 million and $15 million of interest income in each of the years ended December 31, 2014 and 2013. AGM also received $15 million and $15 million of interest from AGC in each of the years ended December 31, 2014 and 2013. There was no principal paydown on the surplus note by AGC.

Loan Receivable from Affiliate

Loan to Assured Guaranty US Holdings Inc.

In May 2012, AGBM entered into a five-year loan agreement with AGUS which authorizes borrowings up to $172.5 million. On May 31, 2012, AGUS borrowed $82.5 million under such agreement. Interest is accruing on the unpaid principal amount of the loan at a rate of six-month LIBOR plus 3% per annum. The entire outstanding principal balance of the loan, together with all accrued and unpaid interest, would have been due and payable on the fifth anniversary of the date the loan is made. In July 2013, this loan was repaid. See Note 12, Investment in MAC Holdings, for more information. AGM recognized $2 million of interest income in 2013.

Capital Contributions from AGMH

In the third quarter of 2008, AGM issued a non-interest bearing surplus note with no term to AGMH in exchange for $300 million which, due to the terms of the agreement, is recorded as capital. Principal on the surplus note may be paid at any time at the option of the Company, subject to prior approval of the New York Superintendent and in compliance with the conditions to such payments as contained in the New York Insurance Laws. The Company repaid $50 million in principal on these surplus notes in 2014 and $50 million in 2013. As of December 31, 2014, an aggregate principal of $25 million remained outstanding on the surplus note, which AGM fully repaid in March 2015 after obtaining approval from the New York Department of Financial Services.

In connection with capitalization of MAC (see Note 12, Investment in MAC Holdings), in July 2013 AGMH made a non-cash contribution of $9 million to AGM.

17. Commitments and Contingencies

Leases

Effective June 2004, AGM entered into a 21-year sublease agreement with Deutsche Bank AG for office space at 31 West 52nd Street, New York, New York. The Company moved to this space in June 2005. The lease contains scheduled rent increases every five years after the 19-month rent-free period, as well as lease incentives for initial construction costs of up to $6 million, as defined in the sublease. The lease contains provisions for rent increases related to increases in the building's operating expenses. The lease also contains a renewal option for an additional ten-year period, and an option to rent additional office space at various points in the future, in each case at then-current market rents. The Company shares its New York office space with certain of its affiliates. Total rent expense allocated to the Company for all premises was $4.6 million in 2014 and $5.1 million in 2013.

Future Minimum Rental Payments

Year	(in millions)
2015	$ 7
2016	7
2017	8
2018	8
2019	8
Thereafter	51
Total	$ 89

Legal Proceedings

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, including matters discussed below. The Company reviews relevant information with respect to its litigation and regulatory matters on a quarterly, and annual basis and updates its accruals, disclosures and estimates of reasonably possible loss based on such reviews.

Litigation

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

In addition, in the ordinary course of its business, the Company asserts claims in legal proceedings against third parties to recover losses paid in prior periods. For example, as described in the "Recovery Litigation," section of Note 6, Expected Loss to be Paid, AGM has filed claims from time to time against sponsors and underwriters of RMBS securities that it had insured, alleging, among other claims, that such persons had breached R&W in the transaction documents, or failed to cure or repurchase defective loans. The amounts, if any, the Company will recover in proceedings to recover losses are uncertain, and recoveries, or failure to obtain recoveries, in any one or more of these proceedings during any quarter or year could be material to the Company's results of operations in that particular quarter or year.

Proceedings Relating to the Company's Financial Guaranty Business

AGM and AGMH receive subpoenas *duces tecum* and interrogatories from regulators from time to time.

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

Proceedings Resolved Since September 30, 2014

Beginning in July 2008, AGM and various other financial guarantors were named in complaints filed in the Superior Court for the State of California, City and County of San Francisco by a number of plaintiffs. Subsequently, plaintiffs' counsel filed amended complaints against AGM and AGC and added additional plaintiffs. These complaints alleged that the financial guaranty insurer defendants (i) participated in a conspiracy in violation of California's antitrust laws to maintain a dual credit rating scale that misstated the credit default risk of municipal bond issuers and created market demand for municipal bond insurance, (ii) participated in risky financial transactions in other lines of business that damaged each insurer's financial condition (thereby undermining the value of each of their guaranties), and (iii) failed to adequately disclose the impact of those transactions on their financial condition. In addition to their antitrust claims, various plaintiffs asserted claims for breach of the covenant of good faith and fair dealing, fraud, unjust enrichment, negligence, and negligent misrepresentation. On October 29, 2014, AGC and AGM filed a good faith settlement notice with the Superior Court for the State of California, City and County of San Francisco, informing the court and co-defendants that AGC, AGM and the plaintiffs had reached an agreement to settle and resolve the cases as between them. The plaintiffs agreed to dismiss the litigation in exchange for AGC and AGM waiving legal fees that had been awarded to them and making a payment to such plaintiffs. On December 12, 2014, the court entered an order determining that the parties had settled in good faith. Plaintiffs have submitted all appropriate dismissals to all courts, and AGC and AGM have submitted a dismissal for their cross-appeal.

On November 19, 2012, Lehman Brothers Holdings Inc. (“LBHI”) and Lehman Brothers Special Financing Inc. (“LBSF") commenced an adversary complaint and claim objection in the United States Bankruptcy Court for the Southern District of New York against Credit Protection Trust 283 (“CPT 283”), FSA Administrative Services, LLC, as trustee for CPT 283, and AGM, in connection with CPT 283's termination of a CDS between LBSF and CPT 283. CPT 283 terminated the CDS as a consequence of LBSF failing to make a scheduled payment owed to CPT 283, which termination occurred after LBHI filed for bankruptcy but before LBSF filed for bankruptcy. The CDS provided that CPT 283 was entitled to receive from LBSF a termination payment in that circumstance of approximately $43.8 million (representing the economic equivalent of the future fixed payments CPT 283 would have been entitled to receive from LBSF had the CDS not been terminated), and CPT 283 filed proofs of claim against LBSF and LBHI (as LBSF's credit support provider) for such amount. LBHI and LBSF sought to disallow and expunge (as impermissible and unenforceable penalties) CPT 283's proofs of claim against LBHI and LBSF and recover approximately $67.3 million, which LBHI and LBSF allege was the mark-to-market value of the CDS to LBSF (less unpaid amounts) on the day CPT 283 terminated the CDS, plus interest, attorney's fees, costs and other expenses. On the same day, LBHI and LBSF also commenced an adversary complaint and claim objection against Credit Protection Trust 207 (“CPT 207”), FSA Administrative Services, LLC, as trustee for CPT 207, and AGM, in connection with CPT 207's termination of a CDS between LBSF and CPT 207. Similarly, the CDS provided that CPT 207 was entitled to receive from LBSF a termination payment in that circumstance of $492,555. LBHI and LBSF seek to disallow and expunge CPT 207's proofs of claim against LBHI and LBSF and recover approximately $1.5 million. On January 30, 2015, the parties signed an agreement pursuant to which LBHI and LBSF dismissed their litigation related to CPT 283's and CPT 207's CDS terminations and the parties agreed that CPT 283 and CPT 207 have a total allowed claim in bankruptcy against LBSF and LBHI of $20 million.

Proceedings Related to AGMH’s Former Financial Products Business

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

Governmental Investigations into Former Financial Products Business

AGMH and/or AGM have received subpoenas *duces tecum* and interrogatories or civil investigative demands from the Attorneys General of the States of Connecticut, Florida, Illinois, Massachusetts, Missouri, New York, Texas and West Virginia relating to their investigations of alleged bid rigging of municipal GICs. AGMH has been responding to such requests. AGMH may receive additional inquiries from these or other regulators and expects to provide additional information to such regulators regarding their inquiries in the future. In addition,

- AGMH received a subpoena from the Antitrust Division of the Department of Justice in November 2006 issued in connection with an ongoing criminal investigation of bid rigging of awards of municipal GICs and other municipal derivatives; and

- AGM received a subpoena from the U.S. Securities and Exchange Commission (the "SEC") in November 2006 related to an ongoing industry-wide investigation concerning the bidding of municipal GICs and other municipal derivatives.

Pursuant to the subpoenas, AGMH has furnished to the Department of Justice and SEC records and other information with respect to AGMH's municipal GIC business. The ultimate loss that may arise from these investigations remains uncertain.

In July 2010, a former employee of AGM who had been involved in AGMH's former Financial Products Business was indicted along with two other persons with whom he had worked at Financial Guaranty Insurance Company. Such former employee and the other two persons were convicted on fraud conspiracy counts. After appeal, their convictions were reversed by a three-judge panel of the U.S. Court of Appeals for the Second Circuit in November 2013. In January 2014, the Department of Justice petitioned the U.S. Court of Appeals for the Second Circuit for a panel rehearing and a rehearing *en banc* of the appeal; the motion was denied on August 15, 2014, and the time period within which to petition for a writ of *certiorari* to the Supreme Court has expired.

Lawsuits Relating to Former Financial Products Business

During 2008, nine putative class action lawsuits were filed in federal court alleging federal antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. These cases have been coordinated and consolidated for pretrial proceedings in the U.S. District Court for the Southern District of New York as *MDL 1950, In re Municipal Derivatives Antitrust Litigation,* Case No. 1:08-cv-2516 ("MDL 1950"). Five of these cases named both AGMH and AGM: (a) *Hinds County, Mississippi v. Wachovia Bank, N.A.*; (b) *Fairfax County, Virginia v. Wachovia Bank, N.A.*; (c) *Central Bucks School District, Pennsylvania v. Wachovia Bank, N.A.*; (d) *Mayor and City Council of Baltimore, Maryland v. Wachovia Bank, N.A.*; and (e) *Washington County, Tennessee v. Wachovia Bank, N.A.* In April 2009, the MDL 1950 court granted the defendants' motion to dismiss on the federal claims, but granted leave for the plaintiffs to file an amended complaint. The Corrected Third Consolidated Amended Class Action Complaint, filed on October 9, 2013, lists neither AGM nor AGMH as a named defendant or a co-conspirator. The complaint generally seeks unspecified monetary damages, interest, attorneys' fees and other costs. The other four cases named AGMH (but not AGM) and also alleged that the defendants violated California state antitrust law and common law by engaging in illegal bid-rigging and market allocation, thereby depriving the cities or municipalities of competition in the awarding of GICs and ultimately resulting in the cities paying higher fees for these products: (f) *City of Oakland, California v. AIG Financial Products Corp.*; (g) *County of Alameda, California v. AIG Financial Products Corp.*; (h) *City of Fresno, California v. AIG Financial Products Corp.*; and (i) *Fresno County Financing Authority v. AIG Financial Products Corp*. When the four plaintiffs filed a consolidated complaint in September 2009, the plaintiffs did not name AGMH as a defendant. However, the complaint does describe some of AGMH's and AGM's activities. The consolidated complaint generally seeks unspecified monetary damages, interest, attorneys' fees and other costs. In April 2010, the MDL 1950 court granted in part and denied in part the named defendants' motions to dismiss this consolidated complaint. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from these lawsuits.

In 2008, AGMH and AGM also were named in five non-class action lawsuits originally filed in the California Superior Courts alleging violations of California law related to the municipal derivatives industry: (a) *City of Los Angeles, California v. Bank of America, N.A.*; (b) *City of Stockton, California v. Bank of America, N.A.*; (c) *County of San Diego, California v. Bank of America, N.A.*; (d) *County of San Mateo, California v. Bank of America, N.A.*; and (e) *County of Contra Costa, California v. Bank of America, N.A.* Amended complaints in these actions were filed in September 2009, adding a federal antitrust claim and naming AGM (but not AGMH) and AGUS, among other defendants. These cases have been transferred to the Southern District of New York and consolidated with MDL 1950 for pretrial proceedings. In late 2009, AGM and AGUS, among other defendants, were named in six additional non-class action cases filed in federal court, which also have been coordinated and

consolidated for pretrial proceedings with MDL 1950: (f) *City of Riverside, California v. Bank of America, N.A.*; (g) *Sacramento Municipal Utility District v. Bank of America, N.A.*; (h) *Los Angeles World Airports v. Bank of America, N.A.*; (i) *Redevelopment Agency of the City of Stockton v. Bank of America, N.A.*; (j) *Sacramento Suburban Water District v. Bank of America, N.A.*; and (k) *County of Tulare, California v. Bank of America, N.A.* The MDL 1950 court denied AGM and AGUS's motions to dismiss these eleven complaints in April 2010. Amended complaints were filed in May 2010. On October 29, 2010, AGM and AGUS were voluntarily dismissed with prejudice from the *Sacramento Municipal Utility District* case only. The complaints in these lawsuits generally seek or sought unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from the remaining lawsuits.

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

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

In September 2009, the Attorney General of the State of West Virginia filed a lawsuit (Circuit Ct. Mason County, W. Va.) against Bank of America, N.A. alleging West Virginia state antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. An amended complaint in this action was filed in June 2010, adding a federal antitrust claim and naming AGM (but not AGMH) and AGUS, among other defendants. This case has been removed to federal court as well as transferred to the S.D.N.Y. and consolidated with MDL 1950 for pretrial proceedings. AGM and AGUS answered West Virginia's Second Amended Complaint on November 11, 2013. The complaint in this lawsuit generally seeks civil penalties, unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from this lawsuit.

18. Notes Payable and Credit Facilities

Notes Payable

Notes Payable represents debt issued by VIEs consolidated by AGM to one of the Financial Products Companies that were transferred to Dexia Holdings prior to the acquisition of AGMH. The funds borrowed were used to finance the purchase of the underlying obligations of AGM-insured obligations which had breached triggers allowing AGM to exercise its right to accelerate payment of a claim in order to mitigate loss. The assets purchased are classified as assets acquired in refinancing transactions and recorded in "other invested assets." The terms of the notes payable match the terms of the assets acquired in refinancing transactions.

The principal and carrying values of the Company's notes payable are presented in the table below.

Principal and Carrying Amounts of Notes Payable

	As of December 31,			
	2014		2013	
	Principal	Carrying Value	Principal	Carrying Value
	(in millions)			
Notes Payable	$ 16	$ 19	$ 34	$ 38

The Company recorded $2 million and $6 million of interest expense on the notes payable for the years ended December 31, 2014, and December 31, 2013, respectively.

Expected Maturity Schedule of Notes Payable

Expected Withdrawal Date	Principal Amount
	(in millions)
2015	$ 7
2016	3
2017	3
2018	2
2019	1
Thereafter	—
Total	$ 16

Recourse Credit Facilities

2009 Strip Coverage Facility

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

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

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

Currently, all the leveraged lease transactions in which AGM acts as strip coverage provider are breaching a rating trigger related to AGM and are subject to early termination. However, early termination of a lease does not result in a draw on the AGM policy if the tax-exempt entity makes the required termination payment. If all the leases were to terminate early and the tax-exempt entities do not make the required early termination payments, then AGM would be exposed to possible liquidity claims on gross exposure of approximately $1.2 billion as of December 31, 2014. To date, none of the leveraged lease transactions that involve AGM has experienced an early termination due to a lease default and a claim on the AGM policy. It is difficult to determine the probability that AGM will have to pay strip provider claims or the likely aggregate amount of such

claims. At December 31, 2014, approximately $1.4 billion of cumulative strip par exposure had been terminated since 2008 on a consensual basis. The consensual terminations have resulted in no claims on AGM.

On July 1, 2009, AGM and Dexia Crédit Local S.A., acting through its New York Branch ("Dexia Crédit Local (NY)"), entered into a credit facility (the "Strip Coverage Facility"). Under the Strip Coverage Facility, Dexia Crédit Local (NY) agreed to make loans to AGM to finance all draws made by lessors on AGM strip policies that were outstanding as of November 13, 2008, up to the commitment amount. The commitment amount of the Strip Coverage Facility was $1 billion at closing of the acquisition of AGMH. AGM has reduced the maximum commitment amount from time to time, after taking into account its experience with its exposure to leveraged lease transactions. Most recently, as of June 30, 2014, AGM reduced the maximum commitment amount to $495 million and agreed with Dexia Crédit Local (NY) that the commitment amount would no longer amortize on a scheduled monthly basis.

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

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

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

The Company was in compliance with all financial covenants as of December 31, 2014.

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

As of December 31, 2014, no amounts were outstanding under this facility, nor have there been any borrowings during the life of this facility.

AGM CPS Securities

In June 2003, $200 million of "AGM CPS", money market preferred trust securities, were issued by trusts created for the primary purpose of issuing the AGM CPS, investing the proceeds in high-quality commercial paper and selling put options to AGM, allowing AGM to issue the trusts non-cumulative redeemable perpetual preferred stock (the "AGM Preferred Stock") of AGM in exchange for cash. There are four trusts, each with an initial aggregate face amount of $50 million. These trusts hold auctions every 28 days, at which time investors submit bid orders to purchase AGM CPS. If AGM were to exercise a put option, the applicable trust would transfer the portion of the proceeds attributable to principal received upon maturity of its assets, net of expenses, to AGM in exchange for AGM Preferred Stock. AGM pays a floating put premium to the trusts, which represents the difference between the commercial paper yield and the winning auction rate (plus all fees and expenses of the trust). If an auction does not attract sufficient clearing bids, however, the auction rate is subject to a maximum rate of one-month LIBOR plus 200 basis points for the next succeeding distribution period. Beginning in August 2007, the AGM CPS required the maximum rate for each of the relevant trusts. AGM continues to have the ability to exercise its put option and cause the related trusts to purchase AGM Preferred Stock. The trusts provide AGM access to new capital at its sole discretion through the exercise of the put options. As of December 31, 2014 the put option had not been exercised. The Company does not consider itself to be the primary beneficiary of the trusts. See Note 8, Fair Value Measurement, –Other Assets–Committed Capital Securities, for a fair value measurement discussion.

19. Employee Benefit Plans

Accounting Policy

AGM 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 all compensation expense based on time studies conducted annually.

Assured Guaranty Ltd. 2004 Long-Term Incentive Plan

Under the Assured Guaranty Ltd. 2004 Long-Term Incentive Plan, as amended (the "Incentive Plan"), the number of AGL common shares that may be delivered under the Incentive Plan may not exceed 18,670,000. In the event of certain transactions affecting AGL's common shares, the number or type of shares subject to the Incentive Plan, the number and type of shares subject to outstanding awards under the Incentive Plan, and the exercise price of awards under the Incentive Plan, may be adjusted.

The Incentive Plan authorizes the grant of incentive stock options, non-qualified stock options, stock appreciation rights, and full value awards that are based on AGL's common shares. The grant of full value awards may be in return for a participant's previously performed services, or in return for the participant surrendering other compensation that may be due, or may be contingent on the achievement of performance or other objectives during a specified period, or may be subject to a risk of forfeiture or other restrictions that will lapse upon the achievement of one or more goals relating to completion of service by the participant, or achievement of performance or other objectives. Awards under the Incentive Plan may accelerate and become vested upon a change in control of AGL.

The Incentive Plan is administered by a committee of the Board of Directors of AGL. The Compensation Committee of the Board serves as this committee except as otherwise determined by the Board. The Board may amend or terminate the Incentive Plan. As of December 31, 2014, 10,712,661 common shares of AGL were available for grant under the Incentive Plan.

The Company recognized expenses of $4 million and $3 million for the years ended December 31, 2014 and 2013, respectively, under the Incentive Plan.

Time Vested Stock Options

Nonqualified or incentive stock options may be granted to employees and directors of Assured Guaranty. Stock options are generally granted once a year with exercise prices equal to the closing price on the date of grant. To date, AGL has only issued non-qualified stock options. All stock options, except for performance stock options, granted to employees vest in equal annual installments over a three-year period and expire seven years or ten years from the date of grant. None of AGL's options, except for performance stock options, have a performance or market condition.

Performance Stock Options

Assured Guaranty grants performance stock options under the Incentive Plan. These awards are non-qualified stock options with exercise prices equal to the closing price of an AGL common share on the applicable date of grant. These awards vest 35%, 50% or 100%, if the price of AGL's common shares using the highest 40-day average share price during the relevant three-year performance period reaches certain hurdles. If the share price is between the specified levels, the vesting level will be interpolated accordingly. These awards expire seven years from the date of grant.

Restricted Stock Awards

Restricted stock awards are valued based on the closing price of the underlying shares at the date of grant. These restricted stock awards to employees generally vest in equal annual installments over a four-year period.

Restricted Stock Units

Restricted stock units are valued based on the closing price of the underlying shares at the date of grant. Restricted stock units generally vest in equal annual installments over a four-year period or fully vest after a three-year period.

Performance Restricted Stock Units

Assured Guaranty has granted performance restricted stock units under the Incentive Plan. These awards vest 35%, 100%, or 200%, if the price of AGL's common shares using the highest 40-day average share price during the relevant three-year performance period reaches certain hurdles. If the share price is between the specified levels, the vesting level will be interpolated accordingly.

Employee Stock Purchase Plan

Assured Guaranty established the AGL Employee Stock Purchase Plan ("Stock Purchase Plan") in accordance with Internal Revenue Code Section 423, and participation is available to all eligible employees. Maximum annual purchases by participants are limited to the number of whole shares that can be purchased by an amount equal to 10% of the participant's compensation or, if less, shares having a value of $25,000. Participants may purchase shares at a purchase price equal to 85% of the lesser of the fair market value of the stock on the first day or the last day of the subscription period. The Company recorded $0.1 million and $0.1 million in share-based compensation, after the effects of DAC, under the Stock Purchase Plan during the years ended December 31, 2014 and 2013, respectively.

Defined Contribution Plans

Employees receive employer contributions into the AGC Employee Retirement Plan (“AGC ERP”) based on a fixed percentage of the employee's compensation and are eligible to make employee contributions and to receive matching employer contributions based on a percentage of compensation up to limits prescribed by Internal Revenue Code Section 401(k). The Company recognized defined contribution expenses of $5 million and $4 million for the years ended December 31, 2014 and 2013, respectively.

Employees receive employer contributions into the AGC Supplemental Executive Retirement Plan based on a fixed percentage of the employee's compensation and are eligible to make employee contributions and to receive matching employer contributions based on a percentage of compensation.

Cash-Based Compensation

Performance Retention Plan

Assured Guaranty has established the Assured Guaranty Ltd. Performance Retention Plan (“PRP”) which permits the grant of cash based awards to selected employees. PRP awards may be treated as nonqualified deferred compensation subject to the rules of Internal Revenue Code Section 409A. The PRP is a sub-plan under the Company's Long-Term Incentive Plan (enabling awards under the plan to be performance based compensation exempt from the $1 million limit on tax deductible compensation).

Generally, each PRP award is divided into three installments, with 25% of the award allocated to a performance period that includes the year of the award and the next year, 25% of the award allocated to a performance period that includes the year of the award and the next two years, and 50% of the award allocated to a performance period that includes the year of the award and the next three years. Each installment of an award vests if the participant remains employed through the end of the performance period for that installment. Awards may vest upon the occurrence of other events as set forth in the plan documents. Payment for each performance period is made at the end of that performance period. One half of each installment is increased or decreased in proportion to the increase or decrease of adjusted book value per share during the performance period, and one half of each installment is increased or decreased in proportion to the operating return on equity during the performance period. Operating return on equity and adjusted book value are defined in each PRP award agreement.

A payment otherwise subject to the $1 million limit on tax deductible compensation, will not be made unless performance satisfies a minimum threshold.

The Company recognized performance retention plan expenses of $7 million and $8 million for the years ended December 31, 2014 and 2013, respectively, representing its proportionate share of the Assured Guaranty expense.

20. Other Comprehensive Income

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

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2014

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, December 31, 2013	$ 105	$ (19)	86
Other comprehensive income (loss) attributable to AGM before reclassifications	86	(28)	58
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(9)	70	61
Tax (provision) benefit	4	(25)	(21)
Total amount reclassified from AOCI, net of tax	(5)	45	40
Net current period other comprehensive income (loss) attributable to AGM	81	17	98
Balance, December 31, 2014	$ 186	$ (2)	$ 184

Changes in Accumulated Other Comprehensive Income by Component
Year Ended December 31, 2013

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, December 31, 2012	$ 226	$ 6	$ 232
Other comprehensive income (loss) attributable to AGM before reclassifications	(103)	(27)	(130)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(27)	3	(24)
Tax (provision) benefit	9	(1)	8
Total amounts reclassified from AOCI, net of tax	(18)	2	(16)
Net current period other comprehensive income (loss) attributable to AGM	(121)	(25)	(146)
Balance, December 31, 2013	$ 105	$ (19)	$ 86

21. Subsequent Events

Subsequent events have been considered through March 30, 2015, the date on which these financial statements were issued.

APPENDIX 5

UNAUDITED FINANCIAL STATEMENTS OF ASSURED GUARANTY MUNICIPAL CORP.

Exhibit 99.1

Assured Guaranty Municipal Corp.

Consolidated Financial Statements

(Unaudited)

September 30, 2016

ASSURED GUARANTY MUNICIPAL CORP.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Assured Guaranty Municipal Corp.

Consolidated Balance Sheets (unaudited)

(dollars in millions except per share and share amounts)

	As of September 30, 2016	As of December 31, 2015
Assets		
Investment portfolio:		
Fixed-maturity securities, available-for-sale, at fair value (amortized cost of $5,682 and $5,901)	$ 5,911	$ 6,090
Short-term investments, at fair value	203	257
Other invested assets (includes Surplus Note from affiliate of $300 and $300)	361	360
Total investment portfolio	6,475	6,707
Cash	14	22
Premiums receivable	352	425
Ceded unearned premium reserve	788	845
Reinsurance recoverable on unpaid losses	190	154
Salvage and subrogation recoverable	319	109
Credit derivative assets	8	63
Deferred tax asset, net	79	103
Financial guaranty variable interest entities' assets, at fair value	640	735
Other assets	131	132
Total assets	**$ 8,996**	**$ 9,295**
Liabilities and shareholder's equity		
Unearned premium reserve	$ 2,535	$ 2,933
Loss and loss adjustment expense reserve	630	488
Reinsurance balances payable, net	145	118
Notes payable	11	13
Credit derivative liabilities	130	154
Current income tax payable	89	16
Financial guaranty variable interest entities' liabilities with recourse, at fair value	624	713
Financial guaranty variable interest entities' liabilities without recourse, at fair value	107	121
Other liabilities	283	295
Total liabilities	**4,554**	**4,851**
Commitments and contingencies (See Note 13)		
Preferred stock ($1,000 par value, 5,000.1 shares authorized; 0 shares issued and outstanding)	—	—
Common stock ($45,455 par value, 330 shares authorized; issued and outstanding)	15	15
Additional paid-in capital	976	975
Retained earnings	3,023	2,967
Accumulated other comprehensive income, net of tax of $80 and $66	135	110
Total shareholder's equity attributable to Assured Guaranty Municipal Corp.	**4,149**	**4,067**
Noncontrolling interest	293	377
Total shareholder's equity	**4,442**	**4,444**
Total liabilities and shareholder's equity	**$ 8,996**	**$ 9,295**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Operations (unaudited)

(in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues				
Net earned premiums	$ 105	$ 117	$ 342	$ 319
Net investment income	55	77	182	206
Net realized investment gains (losses):				
Other-than-temporary impairment losses	(3)	(12)	(22)	(22)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	1	0	(2)	2
Net impairment loss	(4)	(12)	(20)	(24)
Other net realized investment gains (losses)	2	(8)	8	0
Net realized investment gains (losses)	(2)	(20)	(12)	(24)
Net change in fair value of credit derivatives:				
Realized gains (losses) and other settlements	3	5	13	27
Net unrealized gains (losses)	9	82	18	91
Net change in fair value of credit derivatives	12	87	31	118
Fair value gains (losses) on committed capital securities	(11)	(7)	(23)	5
Fair value gains (losses) on financial guaranty variable interest entities	(12)	3	2	(1)
Other income (loss)	9	(8)	38	29
Total revenues	156	249	560	652
Expenses				
Loss and loss adjustment expenses	11	37	101	101
Amortization of deferred ceding commissions	(3)	(3)	(10)	(10)
Other operating expenses	28	28	87	78
Total expenses	36	62	178	169
Income (loss) before income taxes	120	187	382	483
Provision (benefit) for income taxes				
Current	2	37	79	81
Deferred	26	17	21	55
Total provision (benefit) for income taxes	28	54	100	136
Net income (loss)	**92**	**133**	**282**	**347**
Less: Noncontrolling interest	11	10	34	30
Net income (loss) attributable to Assured Guaranty Municipal Corp.	**$ 81**	**$ 123**	**$ 248**	**$ 317**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Comprehensive Income (unaudited)

(in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income (loss)	**$ 92**	**$ 133**	**$ 282**	**$ 347**
Unrealized holding gains (losses) arising during the period on:				
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $(14), $10, $23 and $(27)	(27)	19	40	(49)
Investments with other-than-temporary impairment, net of tax provision (benefit) of $3, $(5), $(12) and $(7)	3	(8)	(21)	(13)
Unrealized holding gains (losses) arising during the period, net of tax	(24)	11	19	(62)
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $0, $(4), $(3) and $(5)	(2)	(7)	(6)	(10)
Other comprehensive income (loss)	(22)	18	25	(52)
Comprehensive income (loss)	**70**	**151**	**307**	**295**
Less: Comprehensive income (loss) attributable to noncontrolling interest	9	13	34	30
Comprehensive income (loss) attributable to Assured Guaranty Municipal Corp.	**$ 61**	**$ 138**	**$ 273**	**$ 265**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Shareholder’s Equity (unaudited)

For the Nine Months Ended September 30, 2016

(dollars in millions, except share data)

	Common Shares Outstanding	Common Stock Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholder's Equity Attributable to Assured Guaranty Municipal Corp.	Noncontrolling Interest	Total Shareholder's Equity
Balance at December 31, 2015	**330**	**$ 15**	**$ 975**	**$ 2,967**	**$ 110**	**$ 4,067**	**$ 377**	**$ 4,444**
Net income	—	—	—	248	—	248	34	282
Dividends	—	—	—	(192)	—	(192)	(114)	(306)
Other comprehensive income (loss)	—	—	—	—	25	25	0	25
Return of capital	—	—	—	—	—	—	(4)	(4)
Other	—	—	1	—	—	1	—	1
Balance at September 30, 2016	**330**	**$ 15**	**$ 976**	**$ 3,023**	**$ 135**	**$ 4,149**	**$ 293**	**$ 4,442**

For the Nine Months Ended September 30, 2015
(dollars in millions, except share data)

	Common Shares Outstanding	Common Stock Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholder's Equity Attributable to Assured Guaranty Municipal Corp.	Noncontrolling Interest	Total Shareholder's Equity
Balance at December 31, 2014	**330**	**15**	**1,000**	**2,752**	**184**	**3,951**	**339**	**4,290**
Net income	—	—	—	317	—	317	30	347
Dividends	—	—	—	(163)	—	(163)	—	(163)
Other comprehensive income (loss)	—	—	—	—	(52)	(52)	0	(52)
Return of capital	—	—	(25)	—	—	(25)	—	(25)
Balance at September 30, 2015	**330**	**$ 15**	**$ 975**	**$ 2,906**	**$ 132**	**$ 4,028**	**$ 369**	**$ 4,397**

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

Assured Guaranty Municipal Corp.

Consolidated Statements of Cash Flows (unaudited)

(in millions)

	Nine Months Ended September 30,	
	2016	2015
Net cash flows provided by (used in) operating activities	**$ (20)**	**$ 21**
Investing activities		
Fixed-maturity securities:		
Purchases	(481)	(888)
Sales	218	508
Maturities	560	306
Net sales (purchases) of short-term investments	53	231
Net proceeds from paydowns on financial guaranty variable interest entities’ assets	89	85
Other	(12)	32
Net cash flows provided by (used in) investing activities	**427**	**274**
Financing activities		
Dividends paid to Assured Guaranty Municipal Holdings Inc.	(192)	(163)
Dividends paid to AGC (see Note 10)	(114)	—
Return of capital to AGC (see Note 10)	(4)	—
Repayment of notes payable	(2)	(3)
Net paydowns of financial guaranty variable interest entities' liabilities	(101)	(102)
Repayment of Surplus Notes	—	(25)
Net cash flows provided by (used in) financing activities	**(413)**	**(293)**
Effect of foreign exchange rate changes	(2)	(1)
Increase (decrease) in cash	**(8)**	**1**
Cash at beginning of period	22	23
Cash at end of period	**$ 14**	**$ 24**
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$ 1	$ 71

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

1. Business and Basis of Presentation

Business

Assured Guaranty Municipal Corp. (“AGM,” or together with its direct and indirect subsidiaries, the “Company”), a New York domiciled insurance company, is a wholly owned subsidiary of Assured Guaranty Municipal Holdings Inc. (“AGMH”). AGMH is an indirect and wholly owned subsidiary of Assured Guaranty Ltd. (“AGL” and, together with its subsidiaries, “Assured Guaranty”). AGL is a Bermuda-based holding company that provides, through its operating subsidiaries, credit protection products to the United States (“U.S.”) and international public finance (including infrastructure) and structured finance markets. AGM was formerly known as Financial Security Assurance Inc.

The Company applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guaranty insurance that protects holders of debt instruments and other monetary obligations from defaults in scheduled payments. If an obligor defaults on a scheduled payment due on an obligation, including a scheduled principal or interest payment (“debt service”), the Company is required under its unconditional and irrevocable financial guaranty to pay the amount of the shortfall to the holder of the obligation. Obligations insured by the Company include bonds issued by U.S. state or municipal governmental authorities and notes issued to finance international infrastructure projects. AGM had previously offered insurance and reinsurance in the global structured finance market, but has not done so since mid-2008. AGM and its indirect subsidiary Municipal Assurance Corp. ("MAC") each markets its financial guaranty insurance directly to issuers and underwriters of public finance securities as well as to investors in such obligations. The Company guarantees obligations issued principally in the U.S. and the United Kingdom ("U.K."), and also guarantees obligations issued in other countries and regions, including Australia and Western Europe.

In the past, the Company sold credit protection by issuing policies that guaranteed payment obligations under credit derivatives, primarily credit default swaps (“CDS”). Financial guaranty contracts accounted for as credit derivatives are generally structured such that the circumstances giving rise to the Company’s obligation to make loss payments are similar to those for financial guaranty insurance contracts. The Company’s credit derivative transactions are governed by International Swaps and Derivative Association, Inc. (“ISDA”) documentation. The Company has not entered into any new CDS in order to sell credit protection since 2008. Regulatory guidelines were issued in 2009 that limited the terms under which such protection could be sold. The capital and margin requirements applicable under the Dodd-Frank Wall Street Reform and Consumer Protection Act also contributed to the Company not entering into new CDS. The Company actively pursues opportunities to terminate existing CDS, which have the effect of reducing future fair value volatility in income and/or reducing rating agency capital charges.

Basis of Presentation

The unaudited interim consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) and, in the opinion of management, reflect all adjustments that are of a normal recurring nature, necessary for a fair statement of the financial condition, results of operations and cash flows of the Company and its consolidated financial guaranty variable interest entities (“FG VIEs”) for the periods presented. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. These unaudited interim consolidated financial statements are as of September 30, 2016 and cover the three-month period ended September 30, 2016 ("Third Quarter 2016"), the three-month period ended September 30, 2015 ("Third Quarter 2015"), the nine-month period ended September 30, 2016 ("Nine Months 2016") and the nine-month period ended September 30, 2015 ("Nine Months 2015"). Certain financial information that is normally included in annual financial statements prepared in accordance with GAAP, but is not required for interim reporting purposes, has been condensed or omitted. The year-end balance sheet data was derived from audited financial statements.

The unaudited interim consolidated financial statements include the accounts of AGM, its direct and indirect subsidiaries (collectively, the “Subsidiaries”), and its consolidated FG VIEs. Intercompany accounts and transactions between and among all consolidated entities have been eliminated. Certain prior year balances have been reclassified to conform to the current year's presentation.

These unaudited interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements of AGM included in Exhibit 99.1 in AGL's Form 8-K dated March 30, 2015, filed with the U.S. Securities and Exchange Commission (the “SEC”).

AGM's direct and indirect subsidiaries are as follows:

- Assured Guaranty (Europe) Ltd. (“AGE”), organized in the U.K. and 100% owned by AGM;
- Municipal Assurance Holdings Inc. (“MAC Holdings”), incorporated in Delaware and 60.7% owned by AGM and 39.3% owned by AGM's affiliate, Assured Guaranty Corp. ("AGC"); and
- MAC, domiciled in New York and 100% owned by MAC Holdings.

Future Application of Accounting Standards

Income Taxes

In October 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-16, Income Taxes (Topic 740) - Intra-Entity Transfers of Assets Other Than Inventory, which removes the current prohibition against immediate recognition of the current and deferred income tax effects of intra-entity transfers of assets other than inventory. Under the ASU, the selling (transferring) entity is required to recognize a current income tax expense or benefit upon transfer of the asset. Similarly, the purchasing (receiving) entity is required to recognize a deferred tax asset or deferred tax liability, as well as the related deferred tax benefit or expense, upon receipt of the asset. The ASU is effective for annual periods beginning after December 15, 2017, including interim periods within those annual periods, and early adoption is permitted. The ASU’s amendments are to be applied on a modified retrospective basis recognizing the effects in retained earnings as of the beginning of the year of adoption. The Company is currently evaluating the effect on its Consolidated Financial Statements of adopting this ASU.

Statement of Cash Flows

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* (a consensus of the Emerging Issues Task Force), which addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. The issues addressed in the new guidance include debt prepayment or debt extinguishment costs, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, distributions received from equity method investments, beneficial interests in securitization transactions and separately identifiable cash flows and application of the predominance principle. The amendments in this ASU are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The Company is currently evaluating the effect on its Consolidated Financial Statements of adopting this ASU.

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 amendments in this ASU are intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The ASU requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions will use forward-looking information to better inform their credit loss estimates as a result of the ASU. While many of the loss estimation techniques applied today will still be permitted, the inputs to those techniques will change to reflect the full amount of expected credit losses. The ASU requires enhanced disclosures to help investors and other financial statement users to better understand significant estimates and judgments used in estimating credit losses, as well as credit quality and underwriting standards of an organization’s portfolio.

In addition, the ASU amends the accounting for credit losses on available-for-sale securities and purchased financial assets with credit deterioration. The ASU makes targeted improvements to the existing “other than temporary” impairment model for certain available-for-sale debt securities to eliminate the concept of “other than temporary” from that model. Accordingly, the ASU states that an entity must use an allowance approach, must limit the allowance to an amount at which the security’s fair value is less than its amortized cost basis, may not consider the length of time fair value has been less than amortized cost, and may not consider recoveries in fair value after the balance sheet date when assessing whether a credit loss exists. For purchased financial assets with credit deterioration, the ASU requires an entity’s method for measuring credit losses to be consistent with its method for measuring expected losses for originated and purchased non-credit-deteriorated assets.

The ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. For most debt instruments, 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 and changes to purchased financial assets with credit deterioration are to be applied prospectively. For the Company, this would be as of January 1, 2020. Early adoption is permitted for fiscal years, and interim periods with those fiscal years, beginning after December 15, 2018. The Company is currently evaluating the effect on its Consolidated Financial Statements of adopting this ASU.

Share-Based Payments

In March 2016, the FASB issued ASU 2016-09, *Compensation - Stock Compensation (Topic 718) - Improvements to Employee Share-Based Payment*, which simplifies several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The new guidance will require all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. It also will allow an employer to repurchase more of an employee’s shares than it can today for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur. The ASU is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and early adoption is permitted. The Company does not expect that the ASU will have a material effect on its Consolidated Financial Statements.

2. Rating Actions

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

The Company periodically assesses the value of each rating assigned to each of its companies, and as a result of such assessment may request that a rating agency add or drop a rating from certain of its companies. For example, the Kroll Bond Rating Agency ("KBRA") ratings were first assigned to MAC in 2013 and to AGM in 2014, while a Moody's Investors Service, Inc. ("Moody's") rating was never requested for MAC.

In the last several years, S&P Global Ratings, a division of Standard & Poor's Financial Services LLC ("S&P") and Moody’s have changed, multiple times, their financial strength ratings of AGM and AGE. More recently, KBRA has assigned financial strength ratings to MAC and AGM. The rating agencies' most recent actions related to AGM and its subsidiaries are:

- On August 8, 2016, Moody's affirmed its existing insurance financial strength ratings of A2 (stable outlook) on AGM and AGE.

- On July 27, 2016, S&P affirmed the AA (stable) financial strength and financial enhancement ratings of AGM, AGE and MAC.

- On July 8, 2016, and December 10, 2015, KBRA affirmed the AA+ (stable outlook) insurance financial strength ratings of MAC and AGM, respectively.

There can be no assurance that any of the rating agencies will not take negative action on the financial strength ratings of AGM or its insurance subsidiaries in the future.

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

- Note 5, Financial Guaranty Insurance
- Note 12, Reinsurance and Other Monoline Exposures
- Note 14, Notes Payable and Credit Facilities (regarding the impact on AGM's insured leveraged lease transactions)

3. Outstanding Exposure

The Company's financial guaranty contracts are written in either insurance or credit derivative form, but collectively are considered financial guaranty contracts. The Company seeks to limit its exposure to losses by underwriting obligations that it views as investment grade at inception, although, as part of its loss mitigation strategy for existing troubled credits, it may underwrite new issuances that it views as below-investment-grade ("BIG"). The Company diversifies its insured portfolio across asset classes and, in the structured finance portfolio, requires rigorous subordination or collateralization requirements. Reinsurance may be used in order to reduce net exposure to certain insured transactions.

The Company has issued financial guaranty insurance policies on public finance obligations and, prior to mid-2008, structured finance obligations. Public finance obligations insured by the Company consist primarily of general obligation bonds supported by the taxing powers of U.S. state or municipal governmental authorities, as well as tax-supported bonds, revenue bonds and other obligations supported by covenants from state or municipal governmental authorities or other municipal obligors to impose and collect fees and charges for public services or specific infrastructure projects. The Company also includes within public finance obligations those obligations backed by the cash flow from leases or other revenues from projects serving substantial public purposes, including utilities, toll roads, health care facilities and government office buildings. The Company also includes within public finance similar obligations issued by territorial and non-U.S. sovereign and sub-sovereign issuers and governmental authorities.

Structured finance obligations insured by the Company are generally issued by special purpose entities, including VIEs, and backed by pools of assets having an ascertainable cash flow or market value or other specialized financial obligations. Some of these VIEs are consolidated as described in Note 8, Consolidated Variable Interest Entities. Unless otherwise specified, the outstanding par and debt service amounts presented in this note include outstanding exposures on VIEs whether or not they are consolidated. While AGM has ceased insuring new originations of asset-backed securities, a significant portfolio of such obligations remains outstanding. AGM's wholly owned subsidiary, AGE, provides financial guarantees in the international public finance market and intends to provide such guarantees in the international structured finance market, subject to regulatory approval.

Debt service and par outstanding exposures presented in these financial statements are presented on a consolidated basis. That is, amounts presented include 100% of the exposures of AGM, AGE and MAC, despite the fact that AGM indirectly owns only 60.7% of MAC.

Surveillance Categories

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

The Company monitors its investment grade credits to determine whether any need to be internally downgraded to BIG and refreshes its internal credit ratings on individual credits in quarterly, semi-annual or annual cycles based on the Company's view of the credit's quality, loss potential, volatility and sector. Ratings on credits in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter.

Credits identified as BIG are subjected to further review to determine the probability of a loss. See Note 4, Expected Loss to be Paid, for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. For surveillance purposes, the Company calculates present value using a discount rate of 5%. (A risk-free rate is used for calculating the expected loss for financial statement measurement purposes.)

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

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

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

- BIG Category 3: Below-investment-grade transactions for which future losses are expected and on which claims (other than liquidity claims) have been paid.

Components of Outstanding Exposure

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

The Company purchases securities that it has insured, and for which it has expected losses to be paid, in order to mitigate the economic effect of insured losses ("loss mitigation securities"). The Company excludes amounts attributable to loss mitigation securities (unless otherwise indicated) from par and debt service outstanding, because it manages such securities as investments and not insurance exposure. The following table presents the gross and net debt service for all financial guaranty contracts.

Financial Guaranty
Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding(1)	
	September 30, 2016	December 31, 2015	September 30, 2016	December 31, 2015
	(in millions)			
Public finance	$ 367,765	$ 415,968	$ 263,330	$ 302,557
Structured finance	17,501	22,880	15,833	20,479
Total financial guaranty	$ 385,266	$ 438,848	$ 279,163	$ 323,036

(1) Includes $84.3 billion and $104.5 billion of net debt service outstanding, as of September 30, 2016 and December 31, 2015, respectively, from MAC, which represents 100% of MAC's net debt service outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

Financial Guaranty Portfolio by Internal Rating
As of September 30, 2016

Rating Category	Public Finance U.S. Net Par Outstanding	Public Finance U.S. %	Public Finance Non-U.S. Net Par Outstanding	Public Finance Non-U.S. %	Structured Finance U.S. Net Par Outstanding	Structured Finance U.S. %	Structured Finance Non-U.S. Net Par Outstanding	Structured Finance Non-U.S. %	Total Net Par Outstanding	Total %
					(dollars in millions)					
AAA	$ 1,761	1.1%	$ 542	3.2%	$ 5,989	53.6%	$ 1,240	57.6%	$ 9,532	5.0%
AA	35,595	22.3	169	1.0	2,764	24.7	28	1.3	38,556	20.2
A	86,134	53.8	4,739	27.9	69	0.6	150	7.0	91,092	47.9
BBB	33,745	21.1	10,708	63.0	81	0.7	328	15.2	44,862	23.6
BIG	2,775	1.7	826	4.9	2,279	20.4	407	18.9	6,287	3.3
Total net par outstanding (1) (2)	$ 160,010	100.0%	$ 16,984	100.0%	$ 11,182	100.0%	$ 2,153	100.0%	$ 190,329	100.0%

____

(1) As of September 30, 2016, excludes $674 million of net par as a result of loss mitigation strategies, including loss mitigation securities held in the investment portfolio, which are primarily BIG.

(2) Includes $61.2 billion of net par outstanding as of September 30, 2016, from MAC, which represents 100% of MAC's net par outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2015

Rating Category	Public Finance U.S. Net Par Outstanding	Public Finance U.S. %	Public Finance Non-U.S. Net Par Outstanding	Public Finance Non-U.S. %	Structured Finance U.S. Net Par Outstanding	Structured Finance U.S. %	Structured Finance Non-U.S. Net Par Outstanding	Structured Finance Non-U.S. %	Total Net Par Outstanding	Total %
					(dollars in millions)					
AAA	$ 2,431	1.3%	$ 553	3.0%	$ 8,529	57.6%	$ 1,786	66.1%	$ 13,299	6.1%
AA	47,028	25.9	134	0.7	3,421	23.1	35	1.3	50,618	23.3
A	98,954	54.6	5,126	27.7	41	0.3	153	5.7	104,274	48.0
BBB	30,443	16.8	11,832	64.1	123	0.9	329	12.1	42,727	19.6
BIG	2,522	1.4	837	4.5	2,681	18.1	401	14.8	6,441	3.0
Total net par outstanding (1) (2)	$ 181,378	100.0%	$ 18,482	100.0%	$ 14,795	100.0%	$ 2,704	100.0%	$ 217,359	100.0%

____

(1) As of December 31, 2015, excludes $659 million of net par as a result of loss mitigation strategies, including loss mitigation securities held in the investment portfolio, which are primarily BIG.

(2) Includes $73.5 billion of net par outstanding as of December 31, 2015, from MAC, which represents 100% of MAC's net par outstanding. However, AGM's indirect ownership of MAC is only 60.7%.

In addition to amounts shown in the tables above, AGM had outstanding commitments to provide guaranties of $1.15 billion for public finance obligations as of September 30, 2016. The expiration dates for the public finance commitments range between October 1, 2016 and February 25, 2017, with $1.1 billion expiring prior to the date of this filing. The commitments are contingent on the satisfaction of all conditions set forth in them and may expire unused or be canceled at the counterparty’s request. Therefore, the total commitment amount does not necessarily reflect actual future guaranteed amounts.

Components of BIG Portfolio

Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of September 30, 2016

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
U.S. public finance	$ 953	$ 1,082	$ 740	$ 2,775	$ 160,010
Non-U.S. public finance	826	—	—	826	16,984
Structured finance:					
First lien U.S. residential mortgage-backed securities ("RMBS"):					
Prime first lien	—	43	—	43	44
Alt-A first lien	20	—	349	369	458
Option ARM	6	—	33	39	79
Subprime	11	159	710	880	1,927
Second lien U.S. RMBS	16	54	794	864	927
Total U.S. RMBS	53	256	1,886	2,195	3,435
Other structured finance	407	49	35	491	9,900
Total	$ 2,239	$ 1,387	$ 2,661	$ 6,287	$ 190,329

Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of December 31, 2015

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
U.S. public finance	$ 1,559	$ 902	$ 61	$ 2,522	$ 181,378
Non-U.S. public finance	622	215	—	837	18,482
Structured finance:					
First lien U.S. RMBS:					
Prime first lien	—	17	—	17	49
Alt-A first lien	26	30	438	494	644
Option ARM	2	—	45	47	101
Subprime	45	143	807	995	2,200
Second lien U.S. RMBS	341	18	626	985	1,108
Total U.S. RMBS	414	208	1,916	2,538	4,102
Other structured finance	451	54	39	544	13,397
Total	$ 3,046	$ 1,379	$ 2,016	$ 6,441	$ 217,359

BIG Net Par Outstanding
and Number of Risks
As of September 30, 2016

Description	Net Par Outstanding: Financial Guaranty Insurance(1)	Net Par Outstanding: Credit Derivative	Net Par Outstanding: Total	Number of Risks(2): Financial Guaranty Insurance(1)	Number of Risks(2): Credit Derivative	Number of Risks(2): Total
	(dollars in millions)					
BIG:						
Category 1	$ 2,182	$ 57	$ 2,239	57	3	60
Category 2	1,387	—	1,387	11	—	11
Category 3	2,661	—	2,661	48	—	48
Total BIG	$ 6,230	$ 57	$ 6,287	116	3	119

BIG Net Par Outstanding
and Number of Risks
As of December 31, 2015

Description	Net Par Outstanding: Financial Guaranty Insurance(1)	Net Par Outstanding: Credit Derivative	Net Par Outstanding: Total	Number of Risks(2): Financial Guaranty Insurance(1)	Number of Risks(2): Credit Derivative	Number of Risks(2): Total
	(dollars in millions)					
BIG:						
Category 1	$ 2,955	$ 91	$ 3,046	59	2	61
Category 2	1,379	—	1,379	14	—	14
Category 3	2,000	16	2,016	43	2	45
Total BIG	$ 6,334	$ 107	$ 6,441	116	4	120

(1) Includes net par outstanding for VIEs.

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

Exposure to Puerto Rico

The Company has insured exposure to general obligation bonds of the Commonwealth of Puerto Rico ("Puerto Rico" or the "Commonwealth") and various obligations of its related authorities and public corporations aggregating $2.0 billion net par as of September 30, 2016, $1.9 billion of which is rated BIG.

Puerto Rico has experienced significant general fund budget deficits in recent years. In addition to high debt levels, Puerto Rico faces a challenging economic environment; the economy has declined nearly every year since 2007, while the population has shrunk every year since 2006 as residents have emigrated.

On June 28, 2015, Governor García Padilla of Puerto Rico (the "Governor") publicly stated that the Commonwealth's public debt, considering the current level of economic activity, was unpayable and that a comprehensive debt restructuring might be necessary.

On November 30, 2015 and December 8, 2015, the Governor issued executive orders ("Clawback Orders") directing the Puerto Rico Department of Treasury and the Puerto Rico Tourism Company to retain or transfer certain taxes pledged to secure the payment of bonds issued by the Puerto Rico Highways and Transportation Authority ("PRHTA"), Puerto Rico Infrastructure Financing Authority ("PRIFA"), and Puerto Rico Convention Center District Authority ("PRCCDA"). On January 7, 2016, the Company sued various Puerto Rico governmental officials in the United States District Court, District of Puerto Rico, asserting that this attempt to "claw back" pledged taxes is unconstitutional, and demanding declaratory and injunctive

relief. The Puerto Rico credits insured by the Company subject to the Clawback Orders are shown in the table "Puerto Rico Net Par Outstanding" below.

On January 1, 2016, PRIFA defaulted on payment of a portion of the interest due on its bonds on that date, resulting in a claim on the Company for those PRIFA bonds the Company insures. There have been additional payment defaults on this and other Puerto Rico credits since then, including, on July 1, 2016, a default on the payment of the Commonwealth's general obligation bonds. The Company has now paid claims on several Puerto Rico credits as shown in the table "Puerto Rico Net Par Outstanding" below.

On April 6, 2016, the Governor signed into law the Puerto Rico Emergency Moratorium & Financial Rehabilitation Act (the "Moratorium Act"). The Moratorium Act purportedly empowers the Governor to declare, entity by entity, states of emergencies and moratoriums on debt service payments on obligations of the Commonwealth and its related authorities and public corporations, as well as instituting a stay against related litigation, among other things. The Governor has used the authority of the Moratorium Act to take a number of actions related to issuers of obligations the Company insures. National Public Finance Guarantee Corporation ("National") (another financial guarantor), holders of the Commonwealth general obligation bonds and certain Puerto Rico residents (the "National Plaintiffs") have filed suits to invalidate the Moratorium Act, and after the passage of the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"), the National Plaintiffs sought a relief from the stay of litigation imposed by PROMESA to pursue the action. On July 21, 2016, the Company filed a motion and form of complaint in the U.S. District Court for the District of Puerto Rico seeking relief from the stay of litigation imposed by PROMESA to seek a declaration that the Moratorium Act is preempted by Federal bankruptcy law. In November 2016 the Court denied both the Company's and the National Plaintiffs' motions for relief from stay in the respective actions. The PROMESA stay expires on February 15, 2017, although it may be extended.

On June 13, 2016, the Supreme Court of the United States affirmed rulings of lower courts finding that the Puerto Rico Public Corporation Debt Enforcement and Recovery Act, which was enacted by Puerto Rico in June 2014 in order to provide a legislative framework for certain public corporations experiencing severe financial stress to restructure their debt, was preempted by the U.S. Bankruptcy Code and therefore void.

On June 30, 2016, PROMESA was signed into law by the President of the United States. PROMESA establishes a seven-member federal financial oversight board ("Oversight Board") with authority to require that balanced budgets and fiscal plans be adopted and implemented by Puerto Rico. PROMESA provides a legal framework under which the debt of the Commonwealth and its related authorities and public corporations may be voluntarily restructured, and grants the Oversight Board the sole authority to file restructuring petitions in a federal court to restructure the debt of the Commonwealth and its related authorities and public corporations if voluntary negotiations fail, provided that any such restructuring must be in accordance with an Oversight Board approved fiscal plan that respects the liens and priorities provided under Puerto Rico law. PROMESA also appears to preempt at least portions of the Moratorium Act and appears to stay debt-related litigation, possibly including the Company's litigation regarding the Clawback Orders. On August 31, 2016, the President of the United States appointed the seven members of the Oversight Board.

The Oversight Board has begun meeting. Press reports indicate that the Oversight Board has set a target of mid-January 2017 for hiring an executive director and is considering intervening in certain litigation relating to the Moratorium Act or otherwise related to Puerto Rico's debt problems. On October 28, 2016, the Oversight Board filed a motion to intervene in the litigation noted above initiated by the Company on July 21, 2016, and seeking relief from the PROMESA stay. That motion was denied on November 1, 2016, without prejudice, on procedural grounds. The Oversight Board also may seek in the future to intervene in litigation initiated by the Company. The Oversight Board has announced its intention to certify a fiscal plan for the Commonwealth and its tax-supported authorities and public corporations under PROMESA by no later than January 31, 2017.

The final shape, timing and validity of responses to Puerto Rico's distress eventually enacted or implemented under the auspices of PROMESA and the Oversight Board or otherwise, and the impact of any such responses on obligations insured by the Company, is uncertain.

The Company groups its Puerto Rico exposure into three categories:

- *Constitutionally Guaranteed.* The Company includes in this category public debt benefiting from Article VI of the Constitution of the Commonwealth, which expressly provides that interest and principal payments on the public debt are to be paid before other disbursements are made.

- *Public Corporations – Certain Revenues Potentially Subject to Clawback.* The Company includes in this category the debt of public corporations for which applicable law permits the Commonwealth to claw back, subject to certain conditions and for the payment of public debt, at least a portion of the revenues supporting the bonds the Company insures. As a Constitutional condition to clawback, available Commonwealth revenues for any fiscal year must be insufficient to pay Commonwealth debt service before the payment of any appropriations for that year. The Company believes that this condition has not been satisfied to date, and accordingly that the Commonwealth has not to date been entitled to clawback revenues supporting debt insured by the Company. As noted above, the Company sued various Puerto Rico governmental officials in the United States District Court, District of Puerto Rico asserting that Puerto Rico's recent attempt to "claw back" pledged taxes is unconstitutional, and demanding declaratory and injunctive relief.

- *Other Public Corporations.* The Company includes in this category the debt of public corporations that are supported by revenues it does not believe are subject to clawback.

Constitutionally Guaranteed

General Obligation. As of September 30, 2016, the Company had $680 million insured net par outstanding of the general obligations of Puerto Rico, which are supported by the good faith, credit and taxing power of the Commonwealth. On July 1, 2016, despite the requirements of Article VI of its Constitution but pursuant to an executive order issued by the Governor under the Moratorium Act, the Commonwealth defaulted on most of the debt service payment due that day, and the Company made its first claim payments on these bonds

Puerto Rico Public Buildings Authority ("PBA"). As of September 30, 2016, the Company had $11 million insured net par outstanding of PBA bonds, which are supported by a pledge of the rents due under leases of government facilities to departments, agencies, instrumentalities and municipalities of the Commonwealth, and that benefit from a Commonwealth guaranty supported by a pledge of the Commonwealth's good faith, credit and taxing power. On July 1, 2016, despite the requirements of Article VI of its Constitution but pursuant to an executive order issued by the Governor under the Moratorium Act, the PBA defaulted on most of the debt service payment due that day, and the Company made its first claim payments on these bonds.

Public Corporations - Certain Revenues Potentially Subject to Clawback

PRHTA. As of September 30, 2016, the Company had $273 million insured net par outstanding of PRHTA (Transportation revenue) bonds and $213 million insured net par of PRHTA (Highways revenue) bonds. The transportation revenue bonds are secured by a subordinate gross pledge of gasoline and gas oil and diesel oil taxes, motor vehicle license fees and certain tolls, plus a first lien on up to $120 million annually of taxes on crude oil, unfinished oil and derivative products. The highways revenue bonds are secured by a gross pledge of gasoline and gas oil and diesel oil taxes, motor vehicle license fees and certain tolls. The Clawback Orders cover Commonwealth-derived taxes that are allocated to PRHTA. The Company believes that such sources represented a substantial majority of PRHTA's revenues in 2015. The PRHTA bonds are subject to executive orders issued pursuant to the Moratorium Act. As noted above, the Company filed a motion and form of complaint in the U.S. District Court for the District of Puerto Rico seeking relief from the PROMESA stay to seek a declaration that the Moratorium Act is preempted by Federal bankruptcy law and that certain gubernatorial executive orders diverting PRHTA pledged toll revenues (which are not subject to the Clawback Orders) are preempted by PROMESA and violate the U.S. Constitution, and also seeking damages and injunctive relief. That motion was denied on November 2, 2016, on procedural grounds. The PROMESA stay expires on February 15, 2017. There were sufficient funds in the PRHTA bond accounts to make the July 1, 2016, PRHTA debt service payments guaranteed by the Company, and those payments were made in full.

Other Public Corporations

Puerto Rico Electric Power Authority ("PREPA"). As of September 30, 2016, the Company had $417 million insured net par outstanding of PREPA obligations, which are payable from a pledge of net revenues of the electric system.

On December 24, 2015, AGM and AGC entered into a Restructuring Support Agreement ("RSA") with PREPA, an ad hoc group of uninsured bondholders and a group of fuel-line lenders that would, subject to certain conditions, result in, among other things, modernization of the utility and a restructuring of current debt. Upon finalization of the contemplated restructuring transaction, insured PREPA revenue bonds (with no reduction to par or stated interest rate or extension of maturity) will be supported by securitization bonds issued by a special purpose corporation and secured by a transition charge assessed on ratepayers. To facilitate the securitization transaction and in exchange for a market premium, Assured Guaranty will issue surety insurance policies in an aggregate amount not expected to exceed $113 million ($14 million for AGC and $99 million for

AGM) to support a portion of the reserve fund for the securitization bonds. Certain of the creditors also agreed, subject to certain conditions, to participate in a bridge financing, which was closed in two tranches on May 19, 2016 and June 22, 2016. AGM's and AGC's share of the bridge financing was approximately $15 million ($2 million for AGC and $13 million for AGM). Legislation meeting the requirements of the RSA was enacted on February 16, 2016, and a transition charge to be paid by PREPA rate payers for debt service on the securitization bonds as contemplated by the RSA was approved by the Puerto Rico Energy Commission on June 20, 2016. The closing of the restructuring transaction and the issuance of the surety bonds are subject to certain conditions, including execution of acceptable documentation and legal opinions. The RSA expires by its terms on December 15, 2016. Negotiations to extend the RSA are in progress, but no assurance can be given that the RSA will be extended.

On July 1, 2016, PREPA made full payment of the $41 million of principal and interest due on PREPA revenue bonds insured by AGM and AGC. That payment was funded in part by AGM’s purchase of $26 million of PREPA bonds maturing in 2020. Upon finalization of the transactions contemplated by the RSA, these new PREPA revenue bonds will be supported by securitization bonds contemplated by the RSA. In early 2016, PREPA repaid in full the $74 million in aggregate principal amount of PREPA revenue bonds purchased by AGM and AGC in July 2015 to replenish some of the operating funds PREPA used to make the July 2015 payments on the PREPA revenue bonds insured by AGM and AGC.

There can be no assurance that the RSA will be extended, the conditions in the RSA will be met or that, if the conditions are met, the RSA's other provisions, including those related to the insured PREPA revenue bonds, will be implemented. In addition, the impact of PROMESA and the Moratorium Act or any attempt to exercise the power purportedly granted by the Moratorium Act on the implementation of the RSA is uncertain. PREPA, during the pendency of the agreements, has suspended deposits into its debt service fund.

Municipal Finance Agency ("MFA"). As of September 30, 2016, the Company had $175 million net par outstanding of bonds issued by MFA secured by a pledge of local property tax revenues. There were sufficient funds in the MFA bond accounts to make the July 1, 2016 MFA bond payments guaranteed by the Company, and those payments were made in full.

Puerto Rico Sales Tax Financing Corporation (“COFINA”). As of September 30, 2016, the Company had $262 million insured net par outstanding of junior COFINA bonds, which are secured primarily by a second lien on certain sales and use taxes. There were no debt service payments due on July 1, 2016 on Company-insured COFINA bonds, and, as of the date of this filing, all payments on Company-insured COFINA bonds had been made.

All Puerto Rico exposures are internally rated triple-C or below, except the General Obligation, PBA and PRHTA (Transportation revenue) second-to-pay policies on an affiliate exposure which are rated AA based on the obligation of the Company's affiliate to pay under its insurance policy if the obligor fails to pay. The following tables show the Company’s insured exposure to general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations.

Puerto Rico
Gross Par and Gross Debt Service Outstanding

	Gross Par Outstanding		Gross Debt Service Outstanding	
	September 30, 2016	December 31, 2015	September 30, 2016	December 31, 2015
	(in millions)			
Exposure to Puerto Rico	$ 3,541	$ 3,761	$ 5,675	$ 6,081

Puerto Rico
Net Par Outstanding

	As of September 30, 2016	As of December 31, 2015
	(in millions)	
Commonwealth Constitutionally Guaranteed		
Commonwealth of Puerto Rico - General Obligation Bonds (1)	$ 677	$ 720
Commonwealth of Puerto Rico - General Obligation Bonds ("Second-to-pay policies on affiliate exposure")	3	—
Commonwealth of Puerto Rico - General Obligation Bonds total	680	720
PBA (1)	—	14
PBA ("Second-to-pay policies on affiliate exposure")	11	—
PBA total	11	14
Public Corporations - Certain Revenues Potentially Subject to Clawback		
PRHTA (Transportation revenue)	190	209
PRHTA (Transportation revenue) ("Second-to-pay policies on affiliate exposure")	83	80
PRHTA (Transportation revenue) total	273	289
PRHTA (Highways revenue)	213	219
Other Public Corporations		
PREPA	417	431
COFINA	262	261
MFA	175	206
Total net exposure to Puerto Rico	$ 2,031	$ 2,140

____
(1) As of the date of this filing, the Company has paid claims on these credits.

The following table shows the scheduled amortization of the insured general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations rated BIG by the Company. The Company guarantees payments of interest and principal when those amounts are scheduled to be paid and cannot be required to pay on an accelerated basis. In the event that obligors default on their obligations, the Company would only be required to pay the shortfall between the principal and interest due in any given period and the amount paid by the obligors.

Amortization Schedule of Puerto Rico BIG Net Par Outstanding and Net Debt Service Outstanding As of September 30, 2016

	Scheduled BIG Net Par Amortization	Scheduled BIG Net Debt Service Amortization
	(in millions)	
2016 (October 1 – December 31)	$ 0	$ 2
2017 (January 1 - March 31)	0	47
2017 (April 1 - June 30)	0	2
2017 (July 1 - September 30)	102	150
2017 (October 1 - December 31)	0	1
Subtotal 2017	102	200
2018	60	153
2019	90	180
2020	92	176
2021-2025	382	753
2026-2030	383	653
2031-2035	457	630
2036-2040	215	291
2041-2043	153	169
Total	$ 1,934	$ 3,207

Exposure to Selected European Countries

The European countries where the Company has exposure and believes heightened uncertainties exist are: Hungary, Italy, Portugal, and Spain (collectively, the "Selected European Countries"). The Company's direct economic exposure to the Selected European Countries (based on par for financial guaranty contracts and notional amount for financial guaranty contracts accounted for as derivatives) is shown in the following table, net of ceded reinsurance.

Net Direct Economic Exposure to Selected European Countries(1)
As of September 30, 2016

	Hungary	Italy	Portugal	Spain	Total
			(in millions)		
Sub-sovereign exposure(2)	$ 195	$ 649	$ 76	$ 282	$ 1,202
Non-sovereign exposure(3)	170	318	—	—	488
Total	$ 365	$ 967	$ 76	$ 282	$ 1,690
Total BIG (See Note 4)	$ 296	$ —	$ 76	$ 282	$ 654

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

(2) Sub-sovereign exposure in Selected European Countries includes transactions backed by receivables from or supported by sub-sovereigns, which are governmental or government-backed entities other than the ultimate governing body of the country.

(3) Non-sovereign exposure in Selected European Countries includes debt of regulated utilities and RMBS.

The Company has excluded from the exposure tables above its indirect economic exposure to the Selected European Countries through policies it provides on pooled corporate transactions. The Company calculates indirect exposure to a country by multiplying the par amount of a transaction insured by the Company times the percent of the relevant collateral pool reported as having a nexus to the country. On that basis, the Company has calculated exposure of $39 million to Selected European Countries in transactions with $2.2 billion of net par outstanding.

4. Expected Loss to be Paid

Loss Estimation Process

This note provides information regarding expected claim payments to be made under all contracts in the insured portfolio, regardless of the accounting model. The Company's loss reserve committees estimate expected loss to be paid for all contracts by reviewing analyses that consider various scenarios with corresponding probabilities assigned to them. Depending upon the nature of the risk, the Company's view of the potential size of any loss and the information available to the Company, that analysis may be based upon individually developed cash flow models, internal credit rating assessments and sector-driven loss severity assumptions or judgmental assessments.

The financial guaranties issued by the Company insure the credit performance of the guaranteed obligations over an extended period of time, in some cases over 30 years, and in most circumstances, the Company has no right to cancel such financial guaranties. The determination of expected loss to be paid is an inherently subjective process involving numerous estimates, assumptions and judgments by management, using both internal and external data sources with regard to frequency, severity of loss, economic projections, governmental actions, negotiations and other factors that affect credit performance. These estimates, assumptions and judgments, and the factors on which they are based, may change materially over a quarter, and as a result the Company's loss estimates may change materially over that same period.

The Company does not use traditional actuarial approaches to determine its estimates of 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 probable and estimable losses may be subject to considerable volatility and may not reflect the Company's ultimate claims paid. For information on the Company's loss estimation process, please refer to Note 4, Expected Losses to be Paid, of the annual consolidated financial statements of AGM for the year ended December 31, 2015 included in Exhibit 99.1 in AGL's Form 8-K dated March 30, 2016, filed with the SEC.

The following tables present a roll forward of the present value of net expected loss to be paid for all contracts, whether accounted for as insurance, credit derivatives or FG VIEs, by sector, after the benefit for expected recoveries for breaches of representations and warranties ("R&W") and other expected recoveries. The Company used weighted average risk-free rates for U.S. dollar denominated obligations that ranged from 0.0% to 2.42% as of September 30, 2016 and 0.0% to 3.25% as of December 31, 2015.

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

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Net expected loss to be paid, beginning of period	$ 493	$ 648	$ 565	$ 619
Economic loss development due to:				
Accretion of discount	2	4	8	11
Changes in discount rates	(10)	3	24	(12)
Changes in timing and assumptions	(5)	6	(25)	72
Total economic loss development	(13)	13	7	71
Paid losses	(70)	(97)	(162)	(126)
Net expected loss to be paid, end of period	$ 410	$ 564	$ 410	$ 564

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

	Net Expected Loss to be Paid (Recovered) as of June 30, 2016	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of September 30, 2016 (2)
		(in millions)		
Public Finance:				
U.S. public finance	$ 316	$ 13	$ (65)	$ 264
Non-U.S. public finance	25	(1)	—	24
Public Finance	341	12	(65)	288
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	(79)	3	2	(74)
Option ARM	(47)	1	1	(45)
Subprime	189	(17)	(15)	157
Total first lien	63	(13)	(12)	38
Second lien	70	(10)	7	67
Total U.S. RMBS	133	(23)	(5)	105
Other structured finance	19	(2)	0	17
Structured Finance	152	(25)	(5)	122
Total	$ 493	$ (13)	$ (70)	$ 410

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

	Net Expected Loss to be Paid (Recovered) as of June 30, 2015	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of September 30, 2015
Public Finance:				
U.S. public finance	$ 217	$ 18	$ (13)	$ 222
Non-U.S. public finance	31	(1)	—	30
Public Finance	248	17	(13)	252
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	206	(34)	(82)	90
Option ARM	(25)	(2)	5	(22)
Subprime	207	22	(14)	215
Total first lien	388	(14)	(91)	283
Second lien	(10)	11	7	8
Total U.S. RMBS	378	(3)	(84)	291
Other structured finance	22	(1)	0	21
Structured Finance	400	(4)	(84)	312
Total	$ 648	$ 13	$ (97)	$ 564

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

	Net Expected Loss to be Paid (Recovered) as of December 31, 2015(2)	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of September 30, 2016(2)
		(in millions)		
Public Finance:				
U.S. public finance	$ 214	$ 124	$ (74)	264
Non-U.S. public finance	26	(2)	—	24
Public Finance	240	122	(74)	288
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	89	(40)	(123)	(74)
Option ARM	(31)	(17)	3	(45)
Subprime	207	(33)	(17)	157
Total first lien	265	(90)	(137)	38
Second lien	37	(20)	50	67
Total U.S. RMBS	302	(110)	(87)	105
Other structured finance	23	(5)	(1)	17
Structured Finance	325	(115)	(88)	122
Total	$ 565	$ 7	$ (162)	$ 410

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

	Net Expected Loss to be Paid (Recovered) as of December 31, 2014	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of September 30, 2015
		(in millions)		
Public Finance:				
U.S. public finance	$ 142	$ 93	$ (13)	222
Non-U.S. public finance	34	(4)	—	30
Public Finance	176	89	(13)	252
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	237	(43)	(104)	90
Option ARM	(19)	(6)	3	(22)
Subprime	223	21	(29)	215
Total first lien	441	(28)	(130)	283
Second lien	(22)	13	17	8
Total U.S. RMBS	419	(15)	(113)	291
Other structured finance	24	(3)	0	21
Structured Finance	443	(18)	(113)	312
Total	$ 619	$ 71	$ (126)	$ 564

(1) Net of ceded paid losses, whether or not such amounts have been settled with reinsurers. Ceded paid losses are typically settled 45 days after the end of the reporting period. Such amounts are recorded in reinsurance recoverable on paid losses included in other assets. The Company paid $3 million and $3 million in loss adjustment expenses ("LAE") for Third Quarter 2016 and 2015, respectively, and $5 million and $6 million in LAE for Nine Months 2016 and 2015, respectively.

(2) Includes expected LAE to be paid of $2 million as of September 30, 2016 and $3 million as of December 31, 2015.

Future Net R&W Recoverable (Payable)(1)

	As of September 30, 2016	As of December 31, 2015
	(in millions)	
U.S. RMBS:		
First lien	$ (101)	$ (9)
Second lien	29	71
Total	$ (72)	$ 62

(1) The Company's agreements with R&W providers generally provide that, as the Company makes claim payments, the R&W providers reimburse it for those claims; if the Company later receives reimbursement through the transaction (for example, from excess spread), the Company repays the R&W providers. See the section "Breaches of Representations and Warranties" for information about the R&W agreements and eligible assets held in trust with respect to such agreements. When the Company projects receiving more reimbursements in the future than it projects paying in claims on transactions covered by R&W settlement agreements, the Company will have a net R&W payable.

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

Net Expected Loss to be Paid (Recovered)
By Accounting Model
As of September 30, 2016

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives (2)	Total
		(in millions)		
Public Finance:				
U.S. public finance	$ 264	$ —	$ —	$ 264
Non-U.S. public finance	24	—	—	24
Public Finance	288	—	—	288
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	(94)	20	—	(74)
Option ARM	(45)	—	—	(45)
Subprime	113	44	—	157
Total first lien	(26)	64	—	38
Second lien	43	29	(5)	67
Total U.S. RMBS	17	93	(5)	105
Other structured finance	15	—	2	17
Structured Finance	32	93	(3)	122
Total	$ 320	$ 93	$ (3)	$ 410

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

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives (2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$ 214	$ —	$ —	$ 214
Non-U.S. public finance	26	—	—	26
Public Finance	240	—	—	240
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	72	17	—	89
Option ARM	(31)	—	—	(31)
Subprime	147	60	—	207
Total first lien	188	77	—	265
Second lien	(4)	37	4	37
Total U.S. RMBS	184	114	4	302
Other structured finance	20	—	3	23
Structured Finance	204	114	7	325
Total	$ 444	$ 114	$ 7	$ 565

(1) Refer to Note 8, Consolidated Variable Interest Entities.

(2) Refer to Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives.

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

Net Economic Loss Development (Benefit)
By Accounting Model
Third Quarter 2016

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
		(in millions)		
Public Finance:				
U.S. public finance	$ 13	$ —	$ —	$ 13
Non-U.S. public finance	(1)	—	—	(1)
Public Finance	12	—	—	12
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	4	(1)	—	3
Option ARM	1	—	—	1
Subprime	(16)	(1)	—	(17)
Total first lien	(11)	(2)	—	(13)
Second lien	(1)	(1)	(8)	(10)
Total U.S. RMBS	(12)	(3)	(8)	(23)
Other structured finance	(2)	—	0	(2)
Structured Finance	(14)	(3)	(8)	(25)
Total	$ (2)	$ (3)	$ (8)	$ (13)

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

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$ 18	$ —	$ —	$ 18
Non-U.S. public finance	(1)	—	—	(1)
Public Finance	17	—	—	17
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	(34)	0	—	(34)
Option ARM	(2)	—	—	(2)
Subprime	17	5	—	22
Total first lien	(19)	5	—	(14)
Second lien	9	1	1	11
Total U.S. RMBS	(10)	6	1	(3)
Other structured finance	(1)	—	0	(1)
Structured Finance	(11)	6	1	(4)
Total	$ 6	$ 6	$ 1	$ 13

Net Economic Loss Development (Benefit)
By Accounting Model
Nine Months 2016

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$ 124	$ —	$ —	$ 124
Non-U.S. public finance	(2)	—	—	(2)
Public Finance	122	—	—	122
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	(42)	2	—	(40)
Option ARM	(17)	—	—	(17)
Subprime	(30)	(3)	—	(33)
Total first lien	(89)	(1)	—	(90)
Second lien	(8)	(4)	(8)	(20)
Total U.S. RMBS	(97)	(5)	(8)	(110)
Other structured finance	(5)	—	0	(5)
Structured Finance	(102)	(5)	(8)	(115)
Total	$ 20	$ (5)	$ (8)	$ 7

Net Economic Loss Development (Benefit)
By Accounting Model
Nine Months 2015

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
		(in millions)		
Public Finance:				
U.S. public finance	$ 93	$ —	$ —	$ 93
Non-U.S. public finance	(4)	—	—	(4)
Public Finance	89	—	—	89
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	(42)	(1)	—	(43)
Option ARM	(6)	—	—	(6)
Subprime	12	9	—	21
Total first lien	(36)	8	—	(28)
Second lien	13	(1)	1	13
Total U.S. RMBS	(23)	7	1	(15)
Other structured finance	(2)	—	(1)	(3)
Structured Finance	(25)	7	0	(18)
Total	$ 64	$ 7	$ 0	$ 71

____

(1) Refer to Note 8, Consolidated Variable Interest Entities.

(2) Refer to Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives.

Selected U.S. Public Finance Transactions

The Company insures general obligation bonds of the Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations aggregating $2.0 billion net par as of September 30, 2016, $1.9 billion of which is rated BIG. For additional information regarding the Company's exposure to general obligations of Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations, please refer to "Exposure to Puerto Rico" in Note 3, Outstanding Exposure.

On February 25, 2015, a plan of adjustment resolving the bankruptcy filing of the City of Stockton, California under chapter 9 of the U.S. Bankruptcy Code became effective. As of September 30, 2016, the Company’s net par subject to the plan consists of $60 million of pension obligation bonds. As part of the plan settlement, the City will repay the pension obligation bonds from certain fixed payments and certain variable payments contingent on the City's revenue growth.

The Company projects that its total net expected loss across its troubled U.S. public finance credits as of September 30, 2016, including those mentioned above, which incorporated the likelihood of the various outcomes, will be $264 million, compared with a net expected loss of $214 million as of December 31, 2015. Economic loss development in Third Quarter 2016 and Nine Months 2016 was $13 million and $124 million, respectively, which was primarily attributable to Puerto Rico exposures.

Certain Selected European Country Sub-Sovereign Transactions

The Company insures credits with sub-sovereign exposure to various Spanish and Portuguese issuers where a Spanish or Portuguese sovereign default may cause the related sub-sovereigns also to default. The Company's exposure net of reinsurance to these Spanish and Portuguese credits is $282 million and $76 million, respectively. The Company rates most of these issuers in the BB category due to the financial condition of Spain and Portugal and their dependence on the sovereign. The Company's Hungary exposure is to infrastructure bonds dependent on payments from Hungarian governmental entities. The Company's exposure net of reinsurance to these Hungarian credits is $195 million, all of which is rated BIG. The Company estimated net expected losses of $24 million related to these Spanish, Portuguese and Hungarian credits. The economic loss development during Third Quarter 2016 of approximately $1 million and the economic benefit of approximately $2 million during Nine Months 2016 was primarily related to changes in the exchange rate between the Euro and U.S. Dollar.

Approach to Projecting Losses in U.S. RMBS

The Company projects losses on its insured U.S. RMBS on a transaction-by-transaction basis by projecting the performance of the underlying pool of mortgages over time and then applying the structural features (i.e., payment priorities and tranching) of the RMBS and any R&W agreements to the projected performance of the collateral over time. The resulting projected claim payments or reimbursements are then discounted using risk-free rates.

Third Quarter and Nine Months 2016 U.S. RMBS Loss Projections

Based on its observation during the period of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general assumptions to project RMBS losses as of September 30, 2016 as it used as of June 30, 2016. For Nine Months 2016, the Company chose to use the same general assumptions to project RMBS losses as of September 30, 2016 as it used as of December 31, 2015, except it (1) increased severities for specific vintages of Alt-A first lien, Option ARM and subprime transactions, (2) decreased liquidation rates for certain vintages of subprime and (3) increased liquidation rates for second lien transactions based on observed data.

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

The majority of projected losses in first lien RMBS transactions are expected to come from non-performing mortgage loans (those that are or in the past twelve months have been two or more payments behind, have been modified, are in foreclosure, or have been foreclosed upon). Changes in the amount of non-performing loans from the amount projected in the previous period are one of the primary drivers of loss development in this portfolio. In order to determine the number of defaults resulting from these delinquent and foreclosed loans, the Company applies a liquidation rate assumption to loans in each of various non-performing categories. The Company arrived at its liquidation rates based on data purchased from a third party provider and assumptions about how delays in the foreclosure process and loan modifications may ultimately affect the rate at which loans are liquidated. Each quarter the Company reviews the most recent twelve months of this data and (if necessary) adjusts its liquidation rates based on its observations. The following table shows liquidation assumptions for various non-performing categories.

First Lien Liquidation Rates

	September 30, 2016	June 30, 2016	December 31, 2015
Current Loans Modified in the Previous 12 Months			
Alt-A	25%	25%	25%
Option ARM	25	25	25
Subprime	25	25	25
Current Loans Delinquent in the Previous 12 Months			
Alt-A	25	25	25
Option ARM	25	25	25
Subprime	25	25	25
30 - 59 Days Delinquent			
Alt-A	35	35	35
Option ARM	40	40	40
Subprime	45	45	45
60 - 89 Days Delinquent			
Alt-A	45	45	45
Option ARM	50	50	50
Subprime	50	50	55
90 + Days Delinquent			
Alt-A	55	55	55
Option ARM	60	60	60
Subprime	55	55	60
Bankruptcy			
Alt-A	45	45	45
Option ARM	50	50	50
Subprime	40	40	40
Foreclosure			
Alt-A	65	65	65
Option ARM	70	70	70
Subprime	65	65	70
Real Estate Owned			
All	100	100	100

While the Company uses liquidation rates as described above to project defaults of non-performing loans (including current loans modified or delinquent within the last 12 months), it projects defaults on presently current loans by applying a conditional default rate ("CDR") trend. The start of that CDR trend is based on the defaults the Company projects will emerge from currently nonperforming, recently nonperforming and modified loans. The total amount of expected defaults from the non-performing loans is translated into a constant CDR (*i.e.*, the CDR plateau), which, if applied for each of the next 36 months, would be sufficient to produce approximately the amount of defaults that were calculated to emerge from the various delinquency categories. The CDR thus calculated individually on the delinquent collateral pool for each RMBS is then used as the starting point for the CDR curve used to project defaults of the presently performing loans.

In the base case, after the initial 36-month CDR plateau period, each transaction's CDR is projected to improve over 12 months to an intermediate CDR (calculated as 20% of its CDR plateau); that intermediate CDR is held constant for 36 months and then trails off in steps to a final CDR of 5% of the CDR plateau. In the base case, the Company assumes the final CDR will be reached 6.75 years after the initial 36-month CDR plateau period. Under the Company's methodology, defaults projected to occur in the first 36 months represent defaults that can be attributed to loans that were modified or delinquent in the last 12 months or that are currently delinquent or in foreclosure, while the defaults projected to occur using the projected CDR trend after the first 36 month period represent defaults attributable to borrowers that are currently performing or are projected to reperform.

Another important driver of loss projections is loss severity, which is the amount of loss the transaction incurs on a loan after the application of net proceeds from the disposal of the underlying property. Loss severities experienced in first lien transactions have reached historically high levels, and the Company is assuming in the base case that these high levels generally will continue for another 18 months. The Company determines its initial loss severity based on actual recent experience. As a result, as of March 31, 2016, the Company updated severities for specific vintages of Alt-A first lien and subprime transactions based on observed data and as of June 30, 2016 the Company updated severities again for certain vintages of Alt-A, as well as Option ARM. The Company then assumes that loss severities begin returning to levels consistent with underwriting assumptions beginning after the initial 18 month period, declining to 40% in the base case over 2.5 years.

The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions used in the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 first lien U.S. RMBS.

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

	As of September 30, 2016		As of June 30, 2016		As of December 31, 2015	
	Range	Weighted Average	Range	Weighted Average	Range	Weighted Average
Alt-A First Lien						
Plateau CDR	3.9% - 10.7%	6.1%	3.8% - 11.9%	6.4%	4.0% - 12.0%	7.7%
Intermediate CDR	0.8% - 2.1%	1.2%	0.8% - 2.4%	1.3%	0.8% - 2.4%	1.5%
Period until intermediate CDR	48 months		48 months		48 months	
Final CDR	0.2% - 0.5%	0.3%	0.2% - 0.6%	0.3%	0.2% - 0.6%	0.4%
Initial loss severity:						
2005 and prior	60.0%		60.0%		60.0%	
2006	80.0%		80.0%		70.0%	
2007	70.0%		70.0%		65.0%	
Initial conditional prepayment rate ("CPR")	1.8% - 16.8%	6.7%	3.5% - 19.5%	6.3%	2.7% - 14.3%	6.2%
Final CPR(2)	15%		15%		15%	
Option ARM						
Plateau CDR	3.4% - 9.1%	7.2%	3.2% - 10.1%	7.7%	3.5% - 10.3%	7.9%
Intermediate CDR	0.7% - 1.8%	1.4%	0.6% - 2.0%	1.5%	0.7% - 2.1%	1.6%
Period until intermediate CDR	48 months		48 months		48 months	
Final CDR	0.2% - 0.5%	0.4%	0.2% - 0.5%	0.4%	0.2% - 0.5%	0.4%
Initial loss severity:						
2005 and prior	60.0%		60.0%		60.0%	
2006	70.0%		70.0%		70.0%	
2007	75.0%		75.0%		65.0%	
Initial CPR	1.7% - 7.5%	4.0%	2.0% - 6.5%	3.9%	1.5% - 6.5%	2.7%
Final CPR(2)	15%		15%		15%	
Subprime						
Plateau CDR	4.5% - 10.7%	8.2%	4.7% - 11.3%	8.6%	5.4% - 13.2%	9.7%
Intermediate CDR	0.9% - 2.1%	1.6%	0.9% - 2.3%	1.7%	1.1% - 2.6%	1.9%
Period until intermediate CDR	48 months		48 months		48 months	
Final CDR	0.2% - 0.5%	0.4%	0.2% - 0.6%	0.4%	0.3% - 0.7%	0.5%
Initial loss severity:						
2005 and prior	80.0%		80.0%		75.0%	
2006	90.0%		90.0%		90.0%	
2007	90.0%		90.0%		90.0%	
Initial CPR	0.4% - 7.6%	3.8%	0.6% - 7.3%	3.8%	0.0% - 6.7%	3.4%
Final CPR(2)	15%		15%		15%	

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

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

The rate at which the principal amount of loans is voluntarily prepaid may impact both the amount of losses projected (since that amount is a function of the CDR, the loss severity and the loan balance over time) as well as the amount of excess spread (the amount by which the interest paid by the borrowers on the underlying loan exceeds the amount of interest owed on the insured obligations). The assumption for the voluntary CPR follows a similar pattern to that of the CDR. The current level of voluntary prepayments is assumed to continue for the plateau period before gradually increasing over 12 months to the final CPR, which is assumed to be 15% in the base case. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. These CPR assumptions are the same as those the Company used for June 30, 2016 and December 31, 2015.

In estimating expected losses, the Company modeled and probability weighted sensitivities for first lien transactions by varying its assumptions of how fast a recovery is expected to occur. One of the variables used to model sensitivities was how quickly the CDR returned to its modeled equilibrium, which was defined as 5% of the initial CDR. The Company also stressed CPR and the speed of recovery of loss severity rates. The Company probability weighted a total of five scenarios as of September 30, 2016. The Company used a similar approach to establish its pessimistic and optimistic scenarios as of September 30, 2016 as it used as of June 30, 2016 and December 31, 2015, increasing and decreasing the periods of stress from those used in the base case.

In a somewhat more stressful environment than that of the base case, where the CDR plateau was extended six months (to be 42 months long) before the same more gradual CDR recovery and loss severities were assumed to recover over 4.5 rather than 2.5 years (and subprime loss severities were assumed to recover only to 60% and Option ARM and Alt A loss severities to only 45%), expected loss to be paid would increase from current projections by approximately $10 million for Alt-A first liens, $6 million for Option ARM and $31 million for subprime transactions.

In an even more stressful scenario where loss severities were assumed to rise and then recover over nine years and the initial ramp-down of the CDR was assumed to occur over 15 months and other assumptions were the same as the other stress scenario, expected loss to be paid would increase from current projections by approximately $24 million for Alt-A first liens, $12 million for Option ARM and $42 million for subprime transactions.

In a scenario with a somewhat less stressful environment than the base case, where CDR recovery was somewhat less gradual, expected loss to be paid would decrease from current projections by approximately $4 million for Alt-A first liens, $17 million for Option ARM and $11 million for subprime transactions.

In an even less stressful scenario where the CDR plateau was six months shorter (30 months, effectively assuming that liquidation rates would improve) and the CDR recovery was more pronounced (including an initial ramp-down of the CDR over nine months), expected loss to be paid would decrease from current projections by approximately $13 million for Alt-A first liens, $26 million for Option ARM and $30 million for subprime transactions.

U.S. Second Lien RMBS Loss Projections

Second lien RMBS transactions include both home equity lines of credit ("HELOC") and closed end second lien. The Company believes the primary variable affecting its expected losses in second lien RMBS transactions is the amount and timing of future losses in the collateral pool supporting the transactions. Expected losses are also a function of the structure of the transaction; the voluntary prepayment rate (typically also referred to as CPR of the collateral); the interest rate environment; and assumptions about the draw rate and loss severity.

In second lien transactions the projection of near-term defaults from currently delinquent loans is relatively straightforward because loans in second lien transactions are generally “charged off” (treated as defaulted) by the securitization’s servicer once the loan is 180 days past due. The Company estimates the amount of loans that will default over the next six months by calculating current representative liquidation rates. A liquidation rate is the percent of loans in a given cohort (in this instance, delinquency category) that ultimately default. Similar to first liens, the Company then calculates a CDR for six months, which is the period over which the currently delinquent collateral is expected to be liquidated. That CDR is then used as the basis for the plateau CDR period that follows the embedded five months of losses. Liquidation rates assumed as of September 30, 2016 were from 25% to 100%, which were the same as of June 30, 2016 and December 31, 2015.

For the base case scenario, the CDR (the “plateau CDR”) was held constant for six months. Once the plateau period has ended, the CDR is assumed to gradually trend down in uniform increments to its final long-term steady state CDR. (The long-term steady state CDR is calculated as the constant CDR that would have yielded the amount of losses originally expected at underwriting.) In the base case scenario, the time over which the CDR trends down to its final CDR is 28 months. Therefore,

the total stress period for second lien transactions is 34 months, comprising five months of delinquent data, a one month plateau period and 28 months of decrease to the steady state CDR, the same as of June 30, 2016 and December 31, 2015.

HELOC loans generally permit the borrower to pay only interest for an initial period (often ten years) and, after that period, require the borrower to make both the monthly interest payment and a monthly principal payment, and so increase the borrower's aggregate monthly payment. Some of the HELOC loans underlying the Company's insured HELOC transactions have reached their principal amortization period. The Company has observed that the increase in monthly payments occurring when a loan reaches its principal amortization period, even if mitigated by borrower relief offered by the servicer, is associated with increased borrower defaults. Thus, most of the Company's HELOC projections incorporate an assumption that a percentage of loans reaching their amortization periods will default around the time of the payment increase. These projected defaults are in addition to those generated using the CDR curve as described above. This assumption is similar to the one used as of June 30, 2016 and December 31, 2015. For September 30, 2016 the Company used the same general approach as of June 30, 2016 and December 31, 2015.

When a second lien loan defaults, there is generally a very low recovery. The Company had assumed as of September 30, 2016 that it will generally recover only 2% of the collateral defaulting in the future and declining additional amounts of post-default receipts on previously defaulted collateral. This is the same assumption used as of June 30, 2016 and December 31, 2015.

The rate at which the principal amount of loans is prepaid may impact both the amount of losses projected as well as the amount of excess spread. In the base case, an average CPR (based on experience of the past year) is assumed to continue until the end of the plateau before gradually increasing to the final CPR over the same period the CDR decreases. The final CPR is assumed to be 15% for second lien transactions, which is lower than the historical average but reflects the Company’s continued uncertainty about the projected performance of the borrowers in these transactions. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. This pattern is generally consistent with how the Company modeled the CPR as of June 30, 2016 and December 31, 2015. To the extent that prepayments differ from projected levels it could materially change the Company’s projected excess spread and losses.

The Company uses a number of other variables in its second lien loss projections, including the spread between relevant interest rate indices. These variables have been relatively stable and in the relevant ranges have less impact on the projection results than the variables discussed above. However, in a number of HELOC transactions the servicers have been modifying poorly performing loans from floating to fixed rates, and, as a result, rising interest rates would negatively impact the excess spread available from these modified loans to support the transactions. The Company incorporated these modifications in its assumptions.

In estimating expected losses, the Company modeled and probability weighted five possible CDR curves applicable to the period preceding the return to the long-term steady state CDR. The Company used five scenarios at September 30, 2016 and December 31, 2015. The Company believes that the level of the elevated CDR and the length of time it will persist, the ultimate prepayment rate, and the amount of additional defaults because of the expiry of the interest only period, are the primary drivers behind the likely amount of losses the collateral will suffer. The Company continues to evaluate the assumptions affecting its modeling results.

Most of the Company's projected second lien RMBS losses are from HELOC transactions. The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions for the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 HELOCs.

Key Assumptions in Base Case Expected Loss Estimates
HELOCs(1)

	As of September 30, 2016		As of June 30, 2016		As of December 31, 2015	
	Range	Weighted Average	Range	Weighted Average	Range	Weighted Average
Plateau CDR	5.1% - 20.6%	12.8%	2.5%-26.3%	12.6%	4.9% - 23.5%	11.0%
Final CDR trended down to	0.6% - 3.2%	1.2%	0.6%-3.2%	1.2%	0.6% - 3.2%	1.2%
Period until final CDR	34 months		34 months		34 months	
Initial CPR	11.5% - 17.7%	12.7%	11.0%-15.4%	11.2%	10.9%	
Final CPR(2)	15.0% - 17.7%	15.4%	10.0%-15.4%	13.3%	10.0% - 15.0%	13.3%
Loss severity	98%		98%		98.0%	

____

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

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

The Company’s base case assumed a six month CDR plateau and a 28 month ramp-down (for a total stress period of 34 months). The Company also modeled a scenario with a longer period of elevated defaults and another with a shorter period of elevated defaults. Increasing the CDR plateau to eight months and increasing the ramp-down by three months to 31-months (for a total stress period of 39 months), and doubling the defaults relating to the end of the interest only period would increase the expected loss by approximately $29 million for HELOC transactions. On the other hand, reducing the CDR plateau to four months and decreasing the length of the CDR ramp-down to 25 months (for a total stress period of 29 months), and lowering the ultimate prepayment rate to 10% would decrease the expected loss by approximately $19 million for HELOC transactions.

Breaches of Representations and Warranties

The Company entered into agreements with R&W providers under which those providers made payments to the Company, agreed to make payments to the Company in the future, and / or repurchased loans from the transactions, all in return for releases of related liability by the Company.

As of September 30, 2016, the Company had a net R&W payable of $72 million to R&W counterparties, compared to an R&W recoverable of $62 million as of December 31, 2015. The decrease represents improvements in underlying collateral performance and the termination of the Deutsche Bank agreement described below. The Company’s agreements with providers of R&W generally provide for reimbursement to the Company as claim payments are made and, to the extent the Company later receives reimbursements of such claims from excess spread or other sources, for the Company to provide reimbursement to the R&W providers. When the Company projects receiving more reimbursements in the future than it projects to pay in claims on transactions covered by R&W settlement agreements, the Company will have a net R&W payable. Most of the amount projected to be received pursuant to agreements with R&W providers benefits from eligible assets placed in trusts to collateralize the R&W provider’s future reimbursement obligation, with the amount of such collateral subject to increase or decrease from time to time as determined by rating agency requirements. Currently the Company has agreements with two counterparties where a future reimbursement obligation is collateralized by eligible assets held in trust:

- **Bank of America**. Under Assured Guaranty's agreement with Bank of America Corporation and certain of its subsidiaries (“Bank of America”), Bank of America agreed to reimburse Assured Guaranty for 80% of claims on the first lien transactions covered by the agreement that Assured Guaranty pays in the future, until the aggregate lifetime collateral losses (not insurance losses or claims) on those transactions reach $6.6 billion. As of September 30, 2016 aggregate lifetime collateral losses on those transactions was $4.5 billion ($4.17 billion for AGM and $0.36 billion for AGC), and Assured Guaranty was projecting in its base case that such collateral losses would eventually reach $5.2 billion ($4.72 billion for AGM and $0.43 billion for AGC). Bank of America's reimbursement obligation is secured by

$143 million of collateral held in trust for AGM's benefit and $370 million of collateral held in trust that is available for either AGM or AGC.

- **UBS.** Under Assured Guaranty's agreement with UBS Real Estate Securities Inc. and affiliates ("UBS"), UBS agreed to reimburse the Company for 85% of future losses on three first lien RMBS transactions, and such reimbursement obligation is secured by $38 million of collateral held in trust for the Company's benefit.

Under Assured Guaranty's previous agreement with Deutsche Bank AG and certain of its affiliates (collectively, "Deutsche Bank"), Deutsche Bank agreed to reimburse Assured Guaranty for certain claims it pays in the future on eight first and second lien transactions, including 80% of claims it pays on those transactions until the aggregate lifetime claims (before reimbursement) reach $319 million. In May 2016, Deutsche Bank's reimbursement obligations under the May 2012 agreement were terminated in return for cash payments to Assured Guaranty.

The Company uses the same RMBS projection scenarios and weightings to project its future R&W benefit as it uses to project RMBS losses on its portfolio. To the extent the Company increases its loss projections, the R&W benefit generally will also increase, subject to the agreement limits and thresholds described above. Similarly, to the extent the Company decreases its loss projections, the R&W benefit generally will also decrease, subject to the agreement limits and thresholds described above.

Other structured finance

The Company's other structured finance includes $491 million net par rated BIG, including transactions backed by manufactured housing loans. The Company has expected loss to be paid of $17 million as of September 30, 2016. The economic benefit during Third Quarter 2016 was $2 million, which was attributable primarily to improved performance of various credits. The economic benefit during Nine Months 2016 was $5 million, which was attributable primarily to improved performance of various credits.

Recovery Litigation

On January 7, 2016, AGM, AGC and Ambac Assurance Corporation ("Ambac") commenced an action for declaratory judgment and injunctive relief in the U.S. District Court for the District of Puerto Rico to invalidate the executive orders issued by the Governor on November 30, 2015 and December 8, 2015 directing that the Secretary of the Treasury of the Commonwealth of Puerto Rico and the Puerto Rico Tourism Company retain or transfer (in other words, "claw back") certain taxes and revenues pledged to secure the payment of bonds issued by the PRHTA, the PRCCDA and the PRIFA. The Commonwealth defendants filed a motion to dismiss the action for lack of subject matter jurisdiction, which the Court denied on October 4, 2016. On October 14, 2016, the Commonwealth defendants filed a notice of PROMESA automatic stay.

On July 21, 2016, AGC and AGM filed a motion and form of complaint in the U.S. District Court for the District of Puerto Rico seeking relief from the stay provided by PROMESA. Upon a grant of relief from the PROMESA stay, the lawsuit further seeks a declaration that the Moratorium Act is preempted by Federal bankruptcy law and that certain gubernatorial executive orders diverting PRHTA pledged toll revenues (which are not subject to the Clawback) are preempted by PROMESA and violate the U.S. Constitution. Additionally, it seeks damages for the value of the PRHTA toll revenues diverted and injunctive relief prohibiting the defendants from taking any further action under these executive orders. On October 28, 2016, the Oversight Board filed a motion seeking leave to intervene in the action, which motion was denied on November 1, 2016, without prejudice, on procedural grounds. On November 2, 2016, the Court denied AGC's and AGM's motion for relief from the PROMESA stay. The PROMESA stay expires on February 15, 2017, although it may be extended.

5. Financial Guaranty Insurance

Financial Guaranty Insurance Premiums

The portfolio of outstanding exposures discussed in Note 3, Outstanding Exposure, includes financial guaranty contracts that meet the definition of insurance contracts as well as those that meet the definition of a derivative under GAAP. Amounts presented in this note relate only to financial guaranty insurance contracts. See Note 7, Financial Guaranty Contracts Accounted for as Credit Derivatives for amounts that relate to CDS and Note 8, Consolidated Variable Interest Entities for amounts that relate to FG VIEs.

Net Earned Premiums

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Scheduled net earned premiums	$ 51	$ 59	$ 157	$ 187
Accelerations:				
Refundings	38	35	125	104
Terminations	14	21	55	22
Total Accelerations	52	56	180	126
Accretion of discount on net premiums receivable	2	2	5	6
Net earned premiums (1)	$ 105	$ 117	$ 342	$ 319

(1) Excludes $4 million and $5 million for Third Quarter 2016 and 2015 , respectively, and $12 million and $14 million for Nine Months 2016 and 2015, respectively, related to consolidated FG VIEs.

Components of Unearned Premium Reserve

	As of September 30, 2016			As of December 31, 2015		
	Gross	Ceded	Net(1)	Gross	Ceded	Net(1)
	(in millions)					
Deferred premium revenue	$ 2,569	$ 794	$ 1,775	$ 2,943	$ 853	$ 2,090
Contra-paid(2)	(34)	(6)	(28)	(10)	(8)	(2)
Unearned premium reserve	$ 2,535	$ 788	$ 1,747	$ 2,933	$ 845	$ 2,088

(1) Excludes $85 million and $97 million of deferred premium revenue, and $28 million and $30 million of contra-paid related to FG VIEs as of September 30, 2016 and December 31, 2015, respectively.

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

Gross Premium Receivable
Roll Forward

	Nine Months	
	2016	2015
	(in millions)	
Beginning of period, December 31	$ 425	$ 450
Gross written premiums	109	78
Gross premiums received	(129)	(116)
Adjustments:		
Changes in the expected term	(30)	(4)
Accretion of discount	1	10
Foreign exchange translation	(24)	(16)
Consolidation/deconsolidation of FG VIEs	—	(4)
End of period, September 30 (1)	$ 352	$ 398

(1) Excludes $4 million and $8 million as of September 30, 2016 and September 30, 2015, respectively, related to consolidated FG VIEs.

Foreign exchange translation relates to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 86%, 82% and 79% of installment premiums at September 30, 2016, December 31, 2015 and September 30, 2015, respectively, are denominated in currencies other than the U.S. dollar, primarily the Euro and British Pound Sterling.

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

Expected Collections of
Financial Guaranty Insurance Gross Premiums Receivable
(Undiscounted)

	As of September 30, 2016
	(in millions)
2016 (October 1 – December 31)	$ 17
2017	41
2018	33
2019	30
2020	28
2021-2025	114
2026-2030	83
2031-2035	59
After 2035	53
Total (1)	$ 458

(1) Excludes expected cash collections on FG VIEs of $6 million.

Scheduled Financial Guaranty Insurance Net Earned Premiums

	As of September 30, 2016
	(in millions)
2016 (October 1 – December 31)	$ 48
2017	174
2018	159
2019	140
2020	126
2021-2025	481
2026-2030	302
2031-2035	182
After 2035	163
Net deferred premium revenue(1)	1,775
Future accretion	70
Total future net earned premiums	$ 1,845

(1) Excludes scheduled net earned premiums on consolidated FG VIEs of $85 million.

Selected Information for Financial Guaranty Insurance Policies Paid in Installments

	As of September 30, 2016	As of December 31, 2015
	(dollars in millions)	
Premiums receivable	$ 352	$ 425
Gross deferred premium revenue	780	966
Weighted-average risk-free rate used to discount premiums	3.1%	3.2%
Weighted-average period of premiums receivable (in years)	9.7	10.0

Financial Guaranty Insurance Losses

Insurance Contracts' Loss Information

The following table provides information on loss and LAE reserves and salvage and subrogation recoverable, net of reinsurance. The Company used weighted average risk-free rates for U.S. dollar denominated financial guaranty insurance obligations that ranged from 0.0% to 2.42% as of September 30, 2016 and 0.0% to 3.25% as of December 31, 2015.

Loss and LAE Reserve and Salvage and Subrogation Recoverable Net of Reinsurance

	As of September 30, 2016			As of December 31, 2015		
	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)
	(in millions)					
Public Finance:						
U.S. public finance	$ 261	$ 31	$ 230	$ 178	$ 0	$ 178
Non-U.S. public finance	15	—	15	15	—	15
Public Finance	276	31	245	193	0	193
Structured Finance:						
U.S. RMBS:						
First lien:						
Alt-A first lien	18	134	(116)	13	—	13
Option ARM	5	51	(46)	7	40	(33)
Subprime	136	18	118	159	15	144
First lien	159	203	(44)	179	55	124
Second lien	48	38	10	15	47	(32)
Total U.S. RMBS	207	241	(34)	194	102	92
Other structured finance	14	—	14	19	1	18
Structured Finance	221	241	(20)	213	103	110
Subtotal	497	272	225	406	103	303
Effect of consolidating FG VIEs	(57)	—	(57)	(72)	0	(72)
Total (1)	$ 440	$ 272	$ 168	$ 334	$ 103	$ 231

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

Components of Net Reserves (Salvage)

	As of September 30, 2016	As of December 31, 2015
	(in millions)	
Loss and LAE reserve	$ 630	$ 488
Reinsurance recoverable on unpaid losses	(190)	(154)
Loss and LAE reserve, net	440	334
Salvage and subrogation recoverable	(319)	(109)
Salvage and subrogation payable(1)	47	6
Salvage and subrogation recoverable, net	(272)	(103)
Net reserves (salvage)	$ 168	$ 231

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

The table below provides a reconciliation of net expected loss to be paid to net expected loss to be expensed. Expected loss to be paid differs from expected loss to be expensed due to: (i) the contra-paid which represent the claim payments made and recoveries received that have not yet been recognized in the statement of operations, (ii) salvage and subrogation recoverable for transactions that are in a net recovery position where the Company has not yet received recoveries on claims previously paid (having the effect of reducing net expected loss to be paid by the amount of the previously paid claim and the expected recovery), but will have no future income effect (because the previously paid claims and the corresponding recovery of those claims will offset in income in future periods), and (iii) loss reserves that have already been established (and therefore expensed but not yet paid).

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

	As of September 30, 2016
	(in millions)
Net expected loss to be paid - financial guaranty insurance (1)	320
Contra-paid, net	28
Salvage and subrogation recoverable, net of reinsurance	272
Loss and LAE reserve, net of reinsurance	(440)
Net expected loss to be expensed (present value)(2)	$ 180

(1) See "Net Expected Loss to be Paid (Recovered) by Accounting Model" table in Note 4, Expected Loss to be Paid.

(2) Excludes $64 million as of September 30, 2016, related to consolidated FG VIEs.

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

Net Expected Loss to be Expensed
Financial Guaranty Insurance Contracts

	As of September 30, 2016
	(in millions)
2016 (October 1 – December 31)	$ 8
Subtotal 2016	8
2017	20
2018	20
2019	18
2020	16
2021-2025	52
2026-2030	26
2031-2035	14
After 2035	6
Net expected loss to be expensed	180
Future accretion	82
Total expected future loss and LAE	$ 262

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

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Public Finance:				
U.S. public finance	$ 15	$ 16	$ 126	$ 79
Non-U.S. public finance	1	(1)	(1)	3
Public finance	16	15	125	82
Structured Finance:				
U.S. RMBS:				
First lien:				
Alt-A first lien	1	(12)	4	(16)
Option ARM	0	0	(17)	(1)
Subprime	(7)	30	(14)	30
First lien	(6)	18	(27)	13
Second lien	2	15	10	24
Total U.S. RMBS	(4)	33	(17)	37
Other structured finance	(2)	(1)	(4)	(1)
Structured finance	(6)	32	(21)	36
Loss and LAE on insurance contracts before FG VIE consolidation	10	47	104	118
Effect of consolidating FG VIEs	1	(10)	(3)	(17)
Loss and LAE	$ 11	$ 37	$ 101	$ 101

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

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of September 30, 2016

	BIG Categories								
	BIG 1		BIG 2		BIG 3				
	Gross	Ceded	Gross	Ceded	Gross	Ceded	Total BIG, Net	Effect of Consolidating VIEs	Total
	(dollars in millions)								
Number of risks(1)	57	(50)	11	(11)	48	(48)	116	—	116
Remaining weighted-average contract period (in years)	8.7	7.6	11.0	9.5	8.3	9.9	9.1	—	9.1
Outstanding exposure:								—	
Principal	$ 3,146	$ (964)	$ 2,195	$ (808)	$ 3,549	$ (888)	$ 6,230	$ —	$ 6,230
Interest	1,530	(404)	1,244	(391)	1,506	(447)	3,038	—	3,038
Total(2)	$ 4,676	$ (1,368)	$ 3,439	$ (1,199)	$ 5,055	$ (1,335)	$ 9,268	$ —	$ 9,268
Expected cash outflows (inflows)	$ 127	$ (41)	$ 678	$ (178)	$ 959	$ (147)	$ 1,398	$ (271)	$ 1,127
Potential recoveries									
Undiscounted R&W	138	(4)	—	—	(29)	1	106	—	106
Other(3)	(491)	49	(95)	8	(575)	110	(994)	163	(831)
Total potential recoveries	(353)	45	(95)	8	(604)	111	(888)	163	(725)
Subtotal	(226)	4	583	(170)	355	(36)	510	(108)	402
Discount	34	(6)	(112)	25	(29)	(9)	(97)	15	(82)
Present value of expected cash flows	$ (192)	$ (2)	$ 471	$ (145)	$ 326	$ (45)	$ 413	$ (93)	$ 320
Deferred premium revenue	$ 43	$ (11)	$ 66	$ (11)	$ 310	$ (51)	$ 346	$ (85)	$ 261
Reserves (salvage)(4)	$ (217)	$ 7	$ 422	$ (136)	$ 163	$ (14)	$ 225	$ (57)	$ 168

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

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	59	(52)	14	(14)	43	(43)	116	—	116
Remaining weighted-average contract period (in years)	10.2	9.8	10.0	8.7	6.8	7.1	9.3	—	9.3
Outstanding exposure:									
Principal	$ 4,718	$ (1,763)	$ 1,923	$ (544)	$ 2,325	$ (325)	$ 6,334	$ —	$ 6,334
Interest	2,665	(952)	983	(234)	786	(101)	3,147	—	3,147
Total(2)	$ 7,383	$ (2,715)	$ 2,906	$ (778)	$ 3,111	$ (426)	$ 9,481	$ —	$ 9,481
Expected cash outflows (inflows)	$ 274	$ (84)	$ 531	$ (136)	$ 1,044	$ (115)	$ 1,514	$ (290)	$ 1,224
Potential recoveries									
Undiscounted R&W	72	(2)	(47)	3	(77)	7	(44)	—	(44)
Other(3)	(336)	19	(134)	16	(441)	71	(805)	146	(659)
Total potential recoveries	(264)	17	(181)	19	(518)	78	(849)	146	(703)
Subtotal	10	(67)	350	(117)	526	(37)	665	(144)	521
Discount	30	10	(62)	21	(98)	(8)	(107)	30	(77)
Present value of expected cash flows	$ 40	$ (57)	$ 288	$ (96)	$ 428	$ (45)	$ 558	$ (114)	$ 444
Deferred premium revenue	$ 168	$ (44)	$ 69	$ (8)	$ 343	$ (47)	$ 481	$ (95)	$ 386
Reserves (salvage)(4)	$ (13)	$ (37)	$ 240	$ (90)	$ 224	$ (21)	$ 303	$ (72)	$ 231

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

(2) Includes BIG amounts related to FG VIEs.

(3) Includes excess spread.

(4) See table "Components of net reserves (salvage)."

Ratings Impact on Financial Guaranty Business

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

For example, AGM has issued financial guaranty insurance policies in respect of the obligations of municipal obligors under interest rate swaps. AGM insures periodic payments owed by the municipal obligors to the bank counterparties. In certain cases, AGM also insures termination payments that may be owed by the municipal obligors to the bank counterparties. If (i) AGM has been downgraded below the rating trigger set forth in a swap under which it has insured the termination payment, which rating trigger varies on a transaction by transaction basis; (ii) the municipal obligor has the right to cure by, but has failed in, posting collateral, replacing AGM or otherwise curing the downgrade of AGM; (iii) the transaction documents include as a condition that an event of default or termination event with respect to the municipal obligor has occurred, such as the rating of the municipal obligor being downgraded past a specified level, and such condition has been met; (iv) the bank counterparty has elected to terminate the swap; (v) a termination payment is payable by the municipal obligor; and (vi) the municipal obligor has failed to make the termination payment payable by it, then AGM would be required to pay the

termination payment due by the municipal obligor, in an amount not to exceed the policy limit set forth in the financial guaranty insurance policy. At AGM's current financial strength ratings, if the conditions giving rise to the obligation of AGM to make a termination payment under the swap termination policies were all satisfied, then AGM could pay claims in an amount not exceeding approximately $191 million in respect of such termination payments. Taking into consideration whether the rating of the municipal obligor is below any applicable specified trigger, if the financial strength ratings of AGM were further downgraded below "A" by S&P or below "A2" by Moody's, and the conditions giving rise to the obligation of AGM to make a payment under the swap policies were all satisfied, then AGM could pay claims in an additional amount not exceeding approximately $439 million in respect of such termination payments.

As another example, with respect to variable rate demand obligations ("VRDOs") for which a bank has agreed to provide a liquidity facility, a downgrade of AGM may provide the bank with the right to give notice to bondholders that the bank will terminate the liquidity facility, causing the bondholders to tender their bonds to the bank. Bonds held by the bank accrue interest at a “bank bond rate” that is higher than the rate otherwise borne by the bond (typically the prime rate plus 2.00% - 3.00%, and capped at the lesser of 25% and the maximum legal limit). In the event the bank holds such bonds for longer than a specified period of time, usually 90-180 days, the bank has the right to demand accelerated repayment of bond principal, usually through payment of equal installments over a period of not less than five years. In the event that a municipal obligor is unable to pay interest accruing at the bank bond rate or to pay principal during the shortened amortization period, a claim could be submitted to AGM under its financial guaranty policy. As of September 30, 2016, the Company had insured approximately $4.4 billion net par of VRDOs, of which approximately $0.2 billion of net par constituted VRDOs issued by municipal obligors rated BBB- or lower pursuant to the Company’s internal rating. The specific terms relating to the rating levels that trigger the bank’s termination right, and whether it is triggered by a downgrade by one rating agency or a downgrade by all rating agencies then rating the insurer, vary depending on the transaction.

In addition, AGM may be required to pay claims in respect of AGMH’s former financial products business if Dexia SA and its affiliates, from which Assured Guaranty had purchased AGMH and its subsidiaries, do not comply with their obligations following a downgrade of the financial strength rating of AGM. Most of the guaranteed investment contracts ("GICs") insured by AGM allow the GIC holder to terminate the GIC and withdraw the funds in the event of a downgrade of AGM below A3 or A-, with no right of the GIC issuer to avoid such withdrawal by posting collateral or otherwise enhancing its credit. Each GIC contract stipulates the thresholds below which the GIC issuer must post eligible collateral, along with the types of securities eligible for posting and the collateralization percentage applicable to each security type. These collateralization percentages range from 100% of the GIC balance for cash posted as collateral to, typically, 108% for asset-backed securities. If the entire aggregate accreted GIC balance of approximately $1.6 billion as of September 30, 2016 were terminated, the assets of the GIC issuers (which had an aggregate market value which exceed the liabilities by $0.9 billion) would be sufficient to fund the withdrawal of the GIC funds.

6. Fair Value Measurement

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

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

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

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

The categorization within the fair value hierarchy is determined based on whether the inputs to valuation techniques used to measure fair value are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Company estimates of market assumptions. The fair value hierarchy prioritizes model inputs into three broad levels as follows, with Level 1 being the highest and Level 3 the lowest. An asset or liability's categorization is based on the lowest level of significant input to its valuation.

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

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

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

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

Measured and Carried at Fair Value

Fixed-Maturity Securities and Short-Term Investments

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

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

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

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

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

- reviews methodologies, any model updates and inputs and compares such information to management's own market information and, where applicable, the internal models,
- reviews internally developed analytic packages that highlight, at a CUSIP level, price changes from the previous quarter to the current quarter, and evaluates, documents, and resolves any significant pricing differences with the assistance of the third party pricing source, and
- compares prices received from different third party pricing sources, and evaluates, documents the rationale for, and resolves any significant pricing differences.

As of September 30, 2016, the Company used models to price 28 fixed-maturity securities (which were purchased or obtained for loss mitigation or other risk management purposes), which were 11.6% or $709 million of the Company's fixed-maturity securities and short-term investments at fair value. Most Level 3 securities were priced with the assistance of an independent third-party. The pricing is based on a discounted cash flow approach using the third-party's proprietary pricing models. The models use inputs such as projected prepayment speeds; severity assumptions; recovery lag assumptions; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); home price 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 bond including collateral type, weighted average life, sensitivity to losses, vintage, and convexity, in conjunction with market data on comparable securities. Significant changes to any of these inputs could materially change the expected timing of cash flows within these securities which is a significant factor in determining the fair value of the securities.

Other Invested Assets

As of September 30, 2016 and December 31, 2015, other invested assets include investments carried and measured at fair value on a recurring basis of $53 million and $51 million, respectively, and include primarily an investment in the global property catastrophe risk market and an investment in a fund that invests primarily in senior loans and bonds. Fair values for the majority of these investments are based on their respective net asset value ("NAV") per share or equivalent.

Other Assets

Committed Capital Securities ("CCS")

The fair value of AGM Committed Preferred Trust Securities (the "AGM CPS"), which is recorded in "other assets" on the consolidated balance sheets, represents the difference between the present value of remaining expected put option premium payments under AGM CPS agreements, and the estimated present value that the Company would hypothetically have to pay currently for a comparable security (see Note 14, Notes Payable and Credit Facilities). The AGM CPS are carried at fair value with changes in fair value recorded in the consolidated statement of operations. The estimated current cost of the AGM CPS is based on several factors, including AGM CDS spreads, the U.S. dollar forward swap curve, London Interbank Offered Rate ("LIBOR") curve projections and the term the securities are estimated to remain outstanding.

Financial Guaranty Contracts Accounted for as Credit Derivatives

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

are not completed at fair value but instead for an amount that approximates the present value of future premiums or for a negotiated amount.

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

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

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

The fair value of the Company's credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay and the estimated present value of premiums that a financial guarantor of comparable credit-worthiness would hypothetically charge or pay at the reporting date for the same protection. The fair value of the Company's credit derivatives depends on a number of factors, including notional amount of the contract, expected term, credit spreads, changes in interest rates, the credit ratings of referenced entities, the Company's own credit risk and remaining contractual cash flows. The expected remaining contractual premium cash flows are the most readily observable inputs since they are based on the CDS contractual terms. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. Consistent with previous years, market conditions at September 30, 2016 were such that market prices of the Company's CDS contracts were not available.

Management considers factors such as current prices charged for similar agreements, when available, performance of underlying assets, life of the instrument, and the nature and extent of activity in the financial guaranty credit derivative marketplace. The assumptions that management uses to determine the fair value may change in the future due to market conditions. Due to the inherent uncertainties of the assumptions used in the valuation models, actual experience may differ from the estimates reflected in the Company's consolidated financial statements and the differences may be material.

Assumptions and Inputs

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

- Gross spread.
- The allocation of gross spread among:
    - the profit the originator, usually an investment bank, realizes for putting the deal together and funding the transaction ("bank profit");
    - premiums paid to the Company for the Company's credit protection provided ("net spread"); and
    - the cost of CDS protection purchased by the originator to hedge their counterparty credit risk exposure to the Company ("hedge cost").
- The weighted average life which is based on debt service schedules.

The rates used to discount future expected premium cash flows ranged from 0.90% to 1.33% at September 30, 2016 and 0.54% to 2.38% at December 31, 2015.

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

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

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

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

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

- Credit spreads interpolated based upon market indices.

- Credit spreads provided by the counterparty of the CDS.

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

As of September 30, 2016 and December 31, 2015, all of the Company's CDS contracts were fair valued utilizing credit spreads interpolated based upon market indices.

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

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

asset in question. These quotes are validated by cross-referencing quotes received from one market source with those quotes received from another market source to ensure reasonableness.

The premium the Company receives is referred to as the “net spread.” The Company’s pricing model takes into account not only how credit spreads on risks that it assumes affect pricing, but also how the Company’s own credit spread affects the pricing of its deals. The Company’s own credit risk is factored into the determination of net spread based on the impact of changes in the quoted market price for credit protection bought on the Company, as reflected by quoted market prices on CDS referencing AGM. For credit spreads on the Company’s name the Company obtains the quoted price of CDS contracts traded on AGM from market data sources published by third parties. The cost to acquire CDS protection referencing AGM affects the amount of spread on CDS deals that the Company retains and, hence, their fair value. As the cost to acquire CDS protection referencing AGM increases, the amount of premium the Company retains on a deal generally decreases. As the cost to acquire CDS protection referencing AGM decreases, the amount of premium the Company retains on a deal generally increases. In the Company’s valuation model, the premium the Company captures is not permitted to go below the minimum rate that the Company would currently charge to assume similar risks. This assumption can have the effect of mitigating the amount of unrealized gains that are recognized on certain CDS contracts. Given the current market conditions and the Company’s own credit spreads, approximately 32%, 21% and 14% based on number of deals, of the Company's CDS contracts are fair valued using this minimum premium as of September 30, 2016, June 30, 2016 and December 31, 2015, respectively. The percentage of deals that price using the minimum premiums fluctuates due to changes in AGM's credit spreads. In general when AGM's credit spreads narrow, the cost to hedge AGM's name declines and more transactions price above previously established floor levels. Meanwhile, when AGM's credit spreads widen, the cost to hedge AGM's name increases causing more transactions to price at previously established floor levels. The Company corroborates the assumptions in its fair value model, including the portion of exposure to AGM hedged by its counterparties, with independent third parties each reporting period. The current level of AGM’s own credit spread has resulted in the bank or deal originator hedging a significant portion of its exposure to AGM. This reduces the amount of contractual cash flows AGM can capture as premium for selling its protection.

The amount of premium a financial guaranty insurance market participant can demand is inversely related to the cost of credit protection on the insurance company as measured by market credit spreads assuming all other assumptions remain constant. This is because the buyers of credit protection typically hedge a portion of their risk to the financial guarantor, due to the fact that the contractual terms of the Company's contracts typically do not require the posting of collateral by the guarantor. The extent of the hedge depends on the types of instruments insured and the current market conditions.

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

Example

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

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

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

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

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

Strengths and Weaknesses of Model

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

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

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

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

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

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

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

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

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

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

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

Fair Value Option on FG VIEs' Assets and Liabilities

The Company elected the fair value option for all the FG VIEs' assets and liabilities. See Note 8, Consolidated Variable Interest Entities.

The FG VIEs issued securities collateralized by first lien and second lien RMBS. The lowest level input that is significant to the fair value measurement of these assets and liabilities was a Level 3 input (i.e., unobservable), therefore management classified them as Level 3 in the fair value hierarchy. Prices are generally determined with the assistance of an independent third-party, based on a discounted cash flow approach. The models to price the FG VIEs’ liabilities used, where appropriate, inputs such as estimated prepayment speeds; market values of the assets that collateralize the securities; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); yields implied by market prices for similar securities; house price depreciation/appreciation rates based on macroeconomic forecasts and, for those liabilities insured by the Company, the benefit from the Company’s insurance policy guaranteeing the timely payment of principal and interest, taking into account the timing of the potential default and the Company’s own credit rating. The third-party also utilizes an internal

model to determine an appropriate yield at which to discount the cash flows of the security, by factoring in collateral types, weighted-average lives, and other structural attributes specific to the security being priced. The expected yield is further calibrated by utilizing algorithms designed to aggregate market color, received by the third-party, on comparable bonds.

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

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

Not Carried at Fair Value

Financial Guaranty Insurance Contracts

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

Notes Payable

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

Other Invested Assets

Other invested assets primarily consist of a surplus note issued by AGC to AGM. The fair value of the surplus note was determined by calculating the effect of changes in U.S. Treasury yield adjusted for a credit factor at the end of each reporting period. The fair value measurement of the surplus note was classified as Level 3.

Other Assets and Other Liabilities

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

Financial Instruments Carried at Fair Value

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

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of September 30, 2016

	Fair Value	Fair Value Hierarchy		
		Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$ 3,895	$ —	$ 3,855	$ 40
U.S. government and agencies	47	—	47	—
Corporate securities	653	—	595	58
Mortgage-backed securities:				
RMBS	524	—	182	342
Commercial mortgage-backed securities ("CMBS")	281	—	281	—
Asset-backed securities	344	—	75	269
Foreign government securities	167	—	167	—
Total fixed-maturity securities	5,911	—	5,202	709
Short-term investments	203	161	42	—
Other invested assets (1)	9	—	4	5
Credit derivative assets	8	—	—	8
FG VIEs’ assets, at fair value	640	—	—	640
Other assets	6	—	—	6
Total assets carried at fair value	$ 6,777	$ 161	$ 5,248	$ 1,368
Liabilities:				
Credit derivative liabilities	$ 130	$ —	$ —	$ 130
FG VIEs’ liabilities with recourse, at fair value	624	—	—	624
FG VIEs’ liabilities without recourse, at fair value	107	—	—	107
Total liabilities carried at fair value	$ 861	$ —	$ —	$ 861

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2015

	Fair Value	Fair Value Hierarchy Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$ 4,041	$ —	$ 4,033	$ 8
U.S. government and agencies	51	—	51	—
Corporate securities	668	—	597	71
Mortgage-backed securities:				
RMBS	532	—	208	324
CMBS	223	—	223	—
Asset-backed securities	394	—	64	330
Foreign government securities	181	—	181	—
Total fixed-maturity securities	6,090	—	5,357	733
Short-term investments	257	176	21	60
Other invested assets (1)	10	—	5	5
Credit derivative assets	63	—	—	63
FG VIEs' assets, at fair value	735	—	—	735
Other assets	29	—	—	29
Total assets carried at fair value	$ 7,184	$ 176	$ 5,383	$ 1,625
Liabilities:				
Credit derivative liabilities	$ 154	$ —	$ —	$ 154
FG VIEs' liabilities with recourse, at fair value	713	—	—	713
FG VIEs' liabilities without recourse, at fair value	121	—	—	121
Total liabilities carried at fair value	$ 988	$ —	$ —	$ 988

(1) Excluded from the table above are investments funds of $48 million and $45 million as of September 30, 2016 and December 31, 2015, respectively, measured using NAV per share. Includes Level 3 mortgage loans that are recorded at fair value on a non-recurring basis.

Changes in Level 3 Fair Value Measurements

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

Fair Value Level 3 Rollforward
Recurring Basis
Third Quarter 2016

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Short-Term Investments	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)									
Fair value as of June 30, 2016	$ 39	$ 58	$ 325	$ 260	$ —	$ 675	$ 18	$ (82)	$ (635)	$ (113)
Total pretax realized and unrealized gains/(losses) recorded in:(1)										
Net income (loss)	1 (2)	0 (2)	1 (2)	2 (2)	— (2)	14 (3)	(11) (4)	(38) (6)	(17) (3)	(17) (3)
Other comprehensive income (loss)	0	0	3	7	—	—	0	—	—	—
Purchases	—	—	24	—	—	—	—	—	—	—
Settlements	0	—	(11)	—	—	(29)	—	(2)	28	3
FG VIE deconsolidations	—	—	—	—	—	(20)	—	—	—	20
Fair value as of September 30, 2016	$ 40	$ 58	$ 342	$ 269	$ —	$ 640	$ 7	$ (122)	$ (624)	$ (107)
Change in unrealized gains/(losses) related to financial instruments held as of September 30, 2016	$ 0	$ 0	$ 2	$ 7	$ —	$ 24	$ (11)	$ 9	$ (15)	$ (17)

Fair Value Level 3 Rollforward
Recurring Basis
Third Quarter 2015

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Short-Term Investments	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
					(in millions)					
Fair value as of June 30, 2015	$ 7	$ 77	$ 306	$ 98	$ —	$ 910	$ 31	$ (199)	$ (811)	$ (128)
Total pretax realized and unrealized gains/(losses) recorded in:(1)										
Net income (loss)	1 (2)	2 (2)	0 (2)	(2) (2)	8 (2)	(4) (3)	(8) (4)	87 (6)	1 (3)	0 (3)
Other comprehensive income (loss)	0	0	(1)	0	(4)	—	0	—	—	—
Purchases	—	—	38	278	52 (7)	—	—	—	—	—
Settlements	0	—	(8)	0	(6)	(31)	0	(5)	34	2
FG VIE consolidations	—	—	—	—	—	—	—	—	—	—
Fair value as of September 30, 2015	$ 8	$ 79	$ 335	$ 374	$ 50	$ 875	$ 23	$ (117)	$ (776)	$ (126)
Change in unrealized gains/(losses) related to financial instruments held as of September 30, 2015	$ 0	$ 0	$ (2)	$ 0	$ (4)	$ 7	$ (7)	$ (17)	$ 3	$ 0

Fair Value Level 3 Rollforward
Recurring Basis
Nine Months 2016

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Short-Term Investments	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)									
Fair value as of December 31, 2015	$ 8	$ 71	$ 324	$ 330	$ 60	$ 735	$ 30	$ (91)	$ (713)	$ (121)
Total pretax realized and unrealized gains/(losses) recorded in:(1)										
Net income (loss)	1 (2)	4 (2)	3 (2)	12 (2)	0 (2)	14 (3)	(23) (4)	(19) (6)	(4) (3)	(14) (3)
Other comprehensive income (loss)	1	(17)	2	3	0	—	0	—	—	—
Purchases	31	—	59	—	—	—	—	—	—	—
Settlements	(1)	—	(46)	(76)	(60)	(89)	—	(12)	93	8
FG VIE deconsolidations	—	—	—	—	—	(20)	—	—	—	20
Fair value as of September 30, 2016	$ 40	$ 58	$ 342	$ 269	$ —	$ 640	$ 7	$ (122)	$ (624)	$ (107)
Change in unrealized gains/(losses) related to financial instruments held as of September 30, 2016	$ 1	$ (17)	$ 1	$ 3	$ —	$ 41	$ (23)	$ 11	$ (5)	$ (14)

Fair Value Level 3 Rollforward
Recurring Basis
Nine Months 2015

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Short-Term Investments	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)									
Fair value as of December 31, 2014	$ 8	$ 79	$ 399	$ 95	$ —	$ 823	$ 19	$ (208)	$ (830)	$ (114)
Total pretax realized and unrealized gains/ (losses) recorded in:(1)										
Net income (loss)	1 (2)	1 (2)	15 (2)	2 (2)	8 (2)	33 (3)	4 (4)	118 (6)	90 (3)	(19) (3)
Other comprehensive income (loss)	0	(1)	(4)	0	(4)	—	0	—	—	—
Purchases	—	—	46	278	52 (7)	—	—	—	—	—
Settlements	(1)	—	(121)	(1)	(6)	(85)	—	(27)	95	7
FG VIE consolidations	—	—	—	—	—	104	—	—	(131)	—
Fair value as of September 30, 2015	$ 8	$ 79	$ 335	$ 374	$ 50	$ 875	$ 23	$ (117)	$ (776)	$ (126)
Change in unrealized gains/ (losses) related to financial instruments held as of September 30, 2015	$ 0	$ (1)	$ (2)	$ 0	$ (4)	$ 66	$ 5	$ (8)	$ (14)	$ (9)

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

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

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

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

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

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

(7) Primarily non-cash transaction.

(8) Includes CCS and other invested assets.

Level 3 Fair Value Disclosures

Quantitative Information About Level 3 Fair Value Inputs
At September 30, 2016

Financial Instrument Description (1)	Fair Value at September 30, 2016 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets (2):				
Fixed-maturity securities:				
Obligations of state and political subdivisions	$ 40	Yield	4.3% 17.2%	11.9%
Corporate securities	58	Yield	20.5%	
RMBS	342	CPR	1.8% - 8.4%	3.1%
		CDR	3.9% - 10.5%	7.2%
		Loss severity	60.0% - 100.0%	75.2%
		Yield	4.0% - 7.7%	5.2%
Asset-backed securities:				
Triple-X life insurance transactions	269	Yield	5.8%	
FG VIEs' assets, at fair value	640	CPR	3.5% - 9.3%	5.4%
		CDR	1.3% - 21.6%	5.9%
		Loss severity	50.0% - 100.0%	81.0%
		Yield	3.2% - 22.1%	6.5%
Other assets	6	Estimated pricing	$80	
		Term (years)	5 years	
Liabilities:				
Credit derivative liabilities, net	(122)	Hedge cost (in bps)	7.6 - 127.5	10.5
		Bank profit (in bps)	3.9 - 701.3	29.1
		Internal floor (in bps)	7.0 - 100.0	10.9
		Internal credit rating	AAA - CCC	AAA
FG VIEs' liabilities, at fair value	(731)	CPR	3.5% - 9.3%	5.4%
		CDR	1.3% - 21.6%	5.9%
		Loss severity	50.0% - 100.0%	81.0%
		Yield	2.9% - 22.1%	5.1%

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

(2) Excludes several investments recorded in other invested assets with fair value of $5 million.

Quantitative Information About Level 3 Fair Value Inputs
At December 31, 2015

Financial Instrument Description (1)	Fair Value at December 31, 2015 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets (2):				
Fixed-maturity securities (3):				
Corporate securities	$ 71	Yield	21.8%	
RMBS	324	CPR	0.3% - 9.0%	2.2%
		CDR	4.2% - 9.3%	7.1%
		Loss severity	60.0% - 100.0%	74.5%
		Yield	4.7% - 8.2%	5.9%
Asset-backed securities:				
Investor owned utility	69	Cash flow receipts	100.0%	
		Collateral recovery period	2.9 years	
		Discount factor	7.0%	
Triple-X life insurance transactions	261	Yield	4.8%	
Short-term investments	60	Yield	17.0%	
FG VIEs' assets, at fair value	735	CPR	2.3% - 8.3%	3.9%
		CDR	2.3% - 16.0%	4.9%
		Loss severity	40.0% - 100.0%	83.7%
		Yield	3.1% - 20.0%	6.7%
Other assets	29	Quotes from third party pricing	$45	
		Term (years)	5 years	
Liabilities:				
Credit derivative liabilities, net	(91)	Hedge cost (in bps)	32.8 - 274.5	37.8
		Bank profit (in bps)	3.9 - 1,017.5	74.4
		Internal floor (in bps)	7.0 - 100.0	34.9
		Internal credit rating	AAA - CCC	AAA
FG VIEs' liabilities, at fair value	(834)	CPR	2.3% - 8.3%	3.9%
		CDR	2.3% - 16.0%	4.9%
		Loss severity	40.0% - 100.0%	83.7%
		Yield	3.1% - 20.0%	5.7%

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

(2) Excludes several investments recorded in other invested assets with fair value of $4 million.

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

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

Fair Value of Financial Instruments

	As of September 30, 2016		As of December 31, 2015	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in millions)			
Assets:				
Fixed-maturity securities	$ 5,911	$ 5,911	$ 6,090	$ 6,090
Short-term investments	203	203	257	257
Other invested assets(1)	361	389	360	428
Credit derivative assets	8	8	63	63
FG VIEs’ assets, at fair value	640	640	735	735
Other assets	71	71	91	91
Liabilities:				
Financial guaranty insurance contracts (2)	1,670	4,215	2,016	3,528
Notes payable	11	10	13	12
Credit derivative liabilities	130	130	154	154
FG VIEs’ liabilities with recourse, at fair value	624	624	713	713
FG VIEs’ liabilities without recourse, at fair value	107	107	121	121
Other liabilities	63	63	2	2

(1) Includes investments not carried at fair value with a carrying value of $304 million and $305 million as of September 30, 2016 and December 31, 2015, respectively.

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

7. Financial Guaranty Contracts Accounted for as Credit Derivatives

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

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

Credit Derivative Net Par Outstanding by Sector

The estimated remaining weighted average life of credit derivatives was 2.3 years at September 30, 2016 and 2.3 years at December 31, 2015. The components of the Company's credit derivative net par outstanding are presented below.

Credit Derivatives
Subordination and Ratings

	As of September 30, 2016				As of December 31, 2015			
Asset Type	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating
				(dollars in millions)				
Pooled corporate obligations:								
Collateralized loan obligations/ collateralized bond obligations	$ 1,704	28.5%	41.3%	AAA	$ 3,980	29.1%	40.6%	AAA
Synthetic investment grade pooled corporate	4,871	21.8%	19.4%	AAA	4,859	21.8	19.4	AAA
Trust preferred securities collateralized debt obligations ("TruPS CDOs")	2	56.0%	97.3%	AAA	2	56.0	96.9	AAA
Market value CDOs of corporate obligations	—	—	—	—	946	17.0	30.1	AAA
Total pooled corporate obligations	6,577	23.5	25.1	AAA	9,787	24.3	29.1	AAA
U.S. RMBS:								
Subprime first lien	39	—	—	AAA	47	—	—	AAA
Closed-end second lien	46	—	—	A	51	—	—	BBB+
Total U.S. RMBS	85	—	—	AA	98	—	—	AA-
Other	1,765	—	—	A-	1,756	—	—	A-
Total	$ 8,427			AAA	$ 11,641			AAA

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

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

The $1.8 billion of exposure in "Other" CDS contracts as of September 30, 2016 comprises numerous deals typically structured with significant underlying credit enhancement and spread across various asset classes, such as commercial receivables, international RMBS, infrastructure, regulated utilities and healthcare.

Distribution of Credit Derivative Net Par Outstanding by Internal Rating

Ratings	As of September 30, 2016 Net Par Outstanding	As of September 30, 2016 % of Total	As of December 31, 2015 Net Par Outstanding	As of December 31, 2015 % of Total
	(dollars in millions)			
AAA	$ 6,120	72.6%	$ 9,089	78.1%
AA	805	9.6	985	8.5
A	792	9.4	853	7.3
BBB	653	7.7	607	5.2
BIG	57	0.7	107	0.9
Credit derivative net par outstanding	$ 8,427	100.0%	$ 11,641	100.0%

Fair Value of Credit Derivatives

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

	Third Quarter 2016	Third Quarter 2015	Nine Months 2016	Nine Months 2015
	(in millions)			
Realized gains on credit derivatives	$ 4	$ 5	$ 15	$ 27
Net credit derivative losses (paid and payable) recovered and recoverable and other settlements	(1)	0	(2)	0
Realized gains (losses) and other settlements	3	5	13	27
Net unrealized gains (losses):				
Pooled corporate obligations	9	(5)	12	(25)
U.S. RMBS	(1)	0	(2)	1
Other	1	87	8	115
Net unrealized gains (losses)	9	82	18	91
Net change in fair value of credit derivatives	$ 12	$ 87	$ 31	$ 118

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

	Third Quarter 2016	Third Quarter 2015	Nine Months 2016	Nine Months 2015
	(in millions)			
Net par of terminated credit derivative contracts	$ —	$ 369	$ 1,086	$ 485
Realized gains on credit derivatives (1)	—	0	2	11
Net unrealized gains (losses) on credit derivatives	0	98	7	98

(1) CDS terminations in Nine Months 2015 included a payment received from the resolution of a dispute related to a termination of a CDS in 2008.

During Third Quarter 2016, unrealized fair value gains were generated primarily as a result of price improvements on the underlying CDS collateral and the run-off of outstanding exposure as the Company's transactions approach maturity. These were the primary drivers of the unrealized fair value gains in the pooled corporate CLO sector. The unrealized fair value gains were partially offset by unrealized losses resulting from wider implied net spreads across all sectors. The wider implied net spreads were primarily a result of the decreased cost to buy protection in AGM's name, particularly for the one year CDS spread, as the market cost of AGM's credit protection decreased during the period. For those CDS transactions that were pricing at or above their floor levels, when the cost of purchasing CDS protection on AGM decreased, the implied spreads that the Company would expect to receive on these transactions increased.

During Nine Months 2016, unrealized fair value gains were generated primarily as a result of CDS terminations, price improvements on the underlying CDS collateral, and the run-off of outstanding exposure as the Company's transactions approach maturity. The Company reached a settlement agreement with two CDS counterparties to terminate several CDS transactions. This was the primary driver of the unrealized fair value gains in the pooled corporate CLO and Other sectors. The unrealized fair value gains were partially offset by unrealized losses resulting from wider implied net spreads across all sectors. The wider implied net spreads were primarily a result of the decreased cost to buy protection in AGM's name, particularly for the one year CDS spread, as the market cost of AGM's credit protection decreased significantly during the period. For those CDS transactions that were pricing at or above their floor levels, when the cost of purchasing CDS protection on AGM decreased, the implied spreads that the Company would expect to receive on these transactions increased.

During Third Quarter 2015, unrealized fair value gains were driven primarily by the termination of a Triple-X life-securitization transaction in the Other sector. These unrealized gains were partially offset by wider implied net spreads in the Company's pooled corporate CLO sector. The wider implied net spreads were primarily a result of the decreased cost to buy protection in AGM's name, particularly for the one year and five year CDS spreads, as the market cost of AGM's credit protection decreased during the period. For those CDS transactions that were pricing at or above their floor levels, when the cost of purchasing CDS protection on AGM, which management refers to as the CDS spread on AGM, decreased the implied spreads that the Company would expect to receive on these transactions increased.

During Nine Months 2015, unrealized fair value gains were generated primarily in the Other sector. The unrealized gains were a result of the termination of a Triple-X life securitization transaction and improvements in the credit rating of one of the Company's reinsurers. The improvement in credit rating increased the Company's credit value adjustment for this particular reinsurer, leading to an unrealized mark to market gain on several policies. The unrealized gains were partially offset by unrealized losses in the pooled corporate sector as a result of implied net spreads on these transactions widening during the period. The net spreads widened as a result of declines in pricing on the underlying collateral of the Company's pooled corporate transactions.

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

CDS Spread on AGM
Quoted price of CDS contract (in basis points)

	As of September 30, 2016	As of June 30, 2016	As of December 31, 2015	As of September 30, 2015	As of June 30, 2015	As of December 31, 2014
Five-year CDS spreads	170	265	366	337	410	325
One-year CDS spreads	31	47	131	104	125	85

Fair Value of Credit Derivatives Assets (Liabilities)
and Effect of AGM
Credit Spreads

	As of September 30, 2016		As of December 31, 2015	
	(in millions)			
Fair value of credit derivatives before effect of AGM credit spread	$	(131)	$	(145)
Plus: Effect of AGM credit spread		9		54
Net fair value of credit derivatives	$	(122)	$	(91)

The fair value of CDS contracts at September 30, 2016, before considering the implications of AGM's credit spreads, is a direct result of continued wide credit spreads in the fixed income security markets and ratings downgrades. The asset classes that remain most affected are pooled corporate obligations. Comparing September 30, 2016 with December 31, 2015, there were several CDS terminations as well as a narrowing of spreads primarily related to the Company's non-U.S. Public Finance obligations in the Other sector, which resulted in mark to market benefit.

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

The following table presents the fair value and the present value of expected claim payments or recoveries (i.e. net expected loss to be paid as described in Note 4) for contracts accounted for as derivatives.

Net Fair Value and Expected Losses
of Credit Derivatives by Sector

	Fair Value of Credit Derivative Asset (Liability), net				Expected Loss to be (Paid) Recovered			
Asset Type	As of September 30, 2016		As of December 31, 2015		As of September 30, 2016		As of December 31, 2015	
			(in millions)					
Pooled corporate obligations	$	4	$	(7)	$	—	$	—
U.S. RMBS		(7)		(6)		5		(4)
Other		(119)		(78)		(2)		(3)
Total	$	(122)	$	(91)	$	3	$	(7)

Sensitivity to Changes in Credit Spread

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

Effect of Changes in Credit Spread
As of September 30, 2016

Credit Spreads(1)	Estimated Net Fair Value (Pre-Tax)	Estimated Change in Gain/(Loss) (Pre-Tax)
	(in millions)	
100% widening in spreads	$ (223)	$ (101)
50% widening in spreads	(173)	(51)
25% widening in spreads	(149)	(27)
10% widening in spreads	(134)	(12)
Base Scenario	(122)	—
10% narrowing in spreads	(114)	8
25% narrowing in spreads	(102)	20
50% narrowing in spreads	(80)	42

____

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

8. Consolidated Variable Interest Entities

Consolidated FG VIEs

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

AGM is not primarily liable for the debt obligations issued by the VIEs it insures and would only be required to make payments on those insured debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due and only for the amount of the shortfall. AGM's creditors do not have any rights with regard to the collateral supporting the debt issued by the FG VIEs. Proceeds from sales, maturities, prepayments and interest from such underlying collateral may only be used to pay debt service on VIE liabilities. Net fair value gains and losses on FG VIEs are expected to reverse to zero at maturity of the VIE debt, except for net premiums received and net claims paid by AGM under the financial guaranty insurance contract. The Company's estimate of expected loss to be paid for FG VIEs is included in Note 4, Expected Loss to be Paid.

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

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

Number of FG VIEs Consolidated

	Nine Months	
	2016	**2015**
Beginning of the period, December 31	24	25
Consolidated(1)	—	1
Deconsolidated(1)	(1)	—
End of the period, September 30	23	26

____

(1) There was no gain or loss on deconsolidation in Nine Months 2016. Net loss on consolidation was $26 million in Nine Months 2015 and recorded in “fair value gains (losses) on FG VIEs” in the consolidated statement of operations.

The total unpaid principal balance for the FG VIEs' assets that were over 90 days or more past due was approximately $115 million at September 30, 2016 and $136 million at December 31, 2015. The aggregate unpaid principal of the FG VIEs' assets was approximately $400 million greater than the aggregate fair value at September 30, 2016. The aggregate unpaid principal of the FG VIEs' assets was approximately $610 million greater than the aggregate fair value at December 31, 2015.

The change in the instrument-specific credit risk of the FG VIEs' assets held as of September 30, 2016 that was recorded in the consolidated statements of operations for Third Quarter 2016 and Nine Months 2016 were gains of $2 million and gains of $28 million, respectively. The change in the instrument-specific credit risk of the FG VIEs' assets held as of September 30, 2015 that was recorded in the consolidated statements of operations for Third Quarter 2015 and Nine Months 2015 were were gains of $7 million and gains of $4 million, respectively. To calculate the instrument specific credit risk, the changes in the fair value of the FG VIE assets are allocated between changes that are due to the instrument specific credit risk and changes due to other factors, including interest rates. The instrument specific credit risk amount is determined by using expected contractual cash flows versus current expected cash flows discounted at original contractual rate. The net present value is calculated by discounting the expected cash flows of the underlying security, excluding the Company’s financial guaranty insurance, at the relevant effective interest rate.

The unpaid principal for FG VIE liabilities with recourse, which represent obligations insured by AGM, was $684 million and $802 million as of September 30, 2016 and December 31, 2015, respectively. FG VIE liabilities with recourse will mature at various dates ranging from 2025 to 2038. The aggregate unpaid principal balance of the FG VIE liabilities with and without recourse was approximately $95 million greater than the aggregate fair value of the FG VIEs’ liabilities as of September 30, 2016. The aggregate unpaid principal balance was approximately $285 million greater than the aggregate fair value of the FG VIEs’ liabilities as of December 31, 2015.

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

Consolidated FG VIEs
By Type of Collateral

	As of September 30, 2016		As of December 31, 2015	
	Assets	Liabilities	Assets	Liabilities
	(in millions)			
With recourse:				
U.S. RMBS first lien	$ 399	$ 444	$ 449	$ 494
U.S. RMBS second lien	134	180	159	219
Total with recourse	533	624	608	713
Without recourse	107	107	127	121
Total	$ 640	$ 731	$ 735	$ 834

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

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

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Net earned premiums	$ (4)	$ (5)	$ (12)	$ (14)
Net investment income	(1)	(2)	(4)	(6)
Net realized investment gains (losses)	0	3	1	2
Fair value gains (losses) on FG VIEs	(12)	3	2	(1)
Loss and LAE	0	10	3	17
Effect on income before tax	(17)	9	(10)	(2)
Less: tax provision (benefit)	(5)	3	(3)	(1)
Effect on net income (loss)	$ (12)	$ 6	$ (7)	$ (1)
Effect on cash flows from operating activities	$ 11	$ 10	$ 21	$ 41

	As of September 30, 2016	As of December 31, 2015
	(in millions)	
Effect on shareholders' equity (decrease) increase	$ (15)	$ (9)

Fair value gains (losses) on FG VIEs represent the net change in fair value on the consolidated FG VIEs' assets and liabilities. During Third Quarter 2016 and Nine Months 2016, the Company recorded a pre-tax net fair value loss on consolidated FG VIEs of $12 million and gains of $2 million, respectively. The primary driver of the loss was the net mark-to-market losses due to price depreciation on the FG VIE assets and price appreciation of the FG VIE recourse liabilities during the quarter. The primary driver of the Nine Months 2016 gains was mark-to-market gains due to price appreciation on the FG VIE assets during the nine months period resulting from improvements in the underlying collateral.

During Third Quarter 2015 the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of $3 million. The primary driver of the gain was mark-to-market gains due to price appreciation on the FG VIE assets during the quarter resulting from improvements in the underlying collateral. During Nine Months 2015, the Company recorded a pre-tax net fair value loss on consolidated FG VIE's of $1 million. The primary driver of the loss was a pre-tax loss of $26 million on the consolidation of one new FG VIE which was mostly offset by net mark-to-market gains due to price appreciation on the FG VIE assets resulting from improvements in the underlying collateral.

Non-Consolidated VIEs

As of September 30, 2016 and December 31, 2015 the Company had financial guaranty contracts outstanding for approximately 300 and 360 VIEs, respectively, that it did not consolidate. To date, the Company's analyses have indicated that it does not have a controlling financial interest in any other VIEs and, as a result, they are not consolidated. The Company's exposure provided through its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 3, Outstanding Exposure.

9. Investments and Cash

Net Investment Income and Realized Gains (Losses)

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. Accrued investment income, which is recorded in Other Assets, was $65 million and $62 million as of September 30, 2016 and December 31, 2015, respectively.

Net Investment Income

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Income from fixed-maturity securities managed by third parties	$ 41	$ 47	$ 128	$ 144
Income from internally managed securities:				
Fixed maturities	11	12	43	33
Other	4	18	14	32
Gross investment income	56	77	185	209
Investment expenses	(1)	0	(3)	(3)
Net investment income	$ 55	$ 77	$ 182	$ 206

Net Realized Investment Gains (Losses)

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Gross realized gains on available-for-sale securities	$ 1	$ 2	$ 8	$ 11
Gross realized losses on available-for-sale securities	0	0	(1)	(2)
Net realized gains (losses) on other invested assets	1	(10)	1	(9)
Other-than-temporary impairment	(4)	(12)	(20)	(24)
Net realized investment gains (losses)	$ (2)	$ (20)	$ (12)	$ (24)

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

Roll Forward of Credit Losses in the Investment Portfolio

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Balance, beginning of period	$ 97	$ 93	$ 97	$ 104
Additions for credit losses on securities for which an other-than-temporary-impairment was not previously recognized	1	2	3	2
Reductions for securities sold during the period	—	—	(4)	(17)
Additions for credit losses on securities for which an other-than-temporary-impairment was previously recognized	1	1	3	7
Balance, end of period	$ 99	$ 96	$ 99	$ 96

Investment Portfolio

Fixed-Maturity Securities and Short-Term Investments
by Security Type
As of September 30, 2016

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI (2) Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Rating(3)
	(dollars in millions)						
Fixed-maturity securities:							
Obligations of state and political subdivisions	62%	$ 3,642	$ 254	$ (1)	$ 3,895	$ 2	AA
U.S. government and agencies	1	43	4	0	47	—	AA+
Corporate securities	11	661	31	(39)	653	(29)	BBB
Mortgage-backed securities(4):							
RMBS	9	526	11	(13)	524	(7)	BB+
CMBS	5	265	16	0	281	—	AAA
Asset-backed securities	6	357	0	(13)	344	(13)	AA
Foreign government securities	3	188	—	(21)	167	—	AA
Total fixed-maturity securities	97	5,682	316	(87)	5,911	(47)	AA-
Short-term investments	3	203	0	0	203	—	AAA
Total investment portfolio	100%	$ 5,885	$ 316	$ (87)	$ 6,114	$ (47)	AA-

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

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Rating(3)
				(dollars in millions)			
Fixed-maturity securities:							
Obligations of state and political subdivisions	62%	$ 3,820	$ 222	$ (1)	$ 4,041	$ 1	AA
U.S. government and agencies	1	47	4	0	51	—	AA+
Corporate securities	11	675	11	(18)	668	(13)	BBB+
Mortgage-backed securities(4):							
RMBS	9	538	11	(17)	532	(7)	BBB-
CMBS	3	219	4	0	223	—	AAA
Asset-backed securities	7	410	1	(17)	394	(16)	AA-
Foreign government securities	3	192	0	(11)	181	—	AA+
Total fixed-maturity securities	96	5,901	253	(64)	6,090	(35)	AA-
Short-term investments	4	257	0	—	257	—	A+
Total investment portfolio	100%	$ 6,158	$ 253	$ (64)	$ 6,347	$ (35)	AA-

(1) Based on amortized cost.

(2) Accumulated OCI ("AOCI"). See also Note 15, Other Comprehensive Income.

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

(4) Government-agency obligations were approximately 25% of mortgage backed securities as of September 30, 2016 and 29% as of December 31, 2015 based on fair value.

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

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

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 September 30, 2016

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
			(dollars in millions)			
Obligations of state and political subdivisions	$ 107	$ (1)	$ —	$ —	$ 107	$ (1)
U.S. government and agencies	5	0	—	—	5	0
Corporate securities	82	(5)	85	(34)	167	(39)
Mortgage-backed securities:						
RMBS	38	(1)	141	(12)	179	(13)
CMBS	36	0	—	—	36	0
Asset-backed securities	10	0	268	(13)	278	(13)
Foreign government securities	93	(7)	74	(14)	167	(21)
Total	$ 371	$ (14)	$ 568	$ (73)	$ 939	$ (87)
Number of securities (1)		93		39		125
Number of securities with other-than-temporary impairment		3		10		13

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2015

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
			(dollars in millions)			
Obligations of state and political subdivisions	$ 90	$ (1)	$ 3	$ 0	$ 93	$ (1)
U.S. government and agencies	3	0	—	—	3	0
Corporate securities	153	(4)	90	(14)	243	(18)
Mortgage-backed securities:						
RMBS	150	(3)	74	(14)	224	(17)
CMBS	49	0	—	—	49	0
Asset-backed securities	269	(17)	—	—	269	(17)
Foreign government securities	92	(4)	82	(7)	174	(11)
Total	$ 806	$ (29)	$ 249	$ (35)	$ 1,055	$ (64)
Number of securities (1)		116		32		139
Number of securities with other-than-temporary impairment		6		4		10

(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.

Of the securities in an unrealized loss position for 12 months or more as of September 30, 2016, 26 securities had unrealized losses greater than 10% of book value. The total unrealized loss for these securities as of September 30, 2016 was $57 million. As of December 31, 2015, of the securities in an unrealized loss position for 12 months or more, nine securities had unrealized losses greater than 10% of book value with unrealized loss amount of $26 million. The Company has determined that the unrealized losses recorded as of September 30, 2016 and December 31, 2015 were yield related and not the result of other-than-temporary-impairment.

The amortized cost and estimated fair value of available-for-sale fixed-maturity securities by contractual maturity as of September 30, 2016 are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Distribution of Fixed-Maturity Securities
by Contractual Maturity
As of September 30, 2016

	Amortized Cost	Estimated Fair Value
	(in millions)	
Due within one year	$ 54	$ 54
Due after one year through five years	959	967
Due after five years through 10 years	1,268	1,314
Due after 10 years	2,610	2,771
Mortgage-backed securities:		
RMBS	526	524
CMBS	265	281
Total	$ 5,682	$ 5,911

The investment portfolio contains securities and cash that are either held in trust for the benefit of third party reinsurers in accordance with statutory requirements, placed on deposit to fulfill state licensing requirements, or otherwise restricted in the amount of $20 million and $33 million as of September 30, 2016 and December 31, 2015, respectively, based on fair value. In addition, the total collateral required to be funded into a reinsurance trust account by AGM for the benefit of AGE as of September 30, 2016 and December 31, 2015 was approximately $212 million and $244 million, respectively, based on fair value.

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

Internally Managed Portfolio

The investment portfolio tables shown above include both assets managed externally and internally. In the table below, more detailed information is provided for the component of the total investment portfolio that is internally managed (excluding short-term investments and surplus note from affiliate). The internally managed portfolio, as defined below, represents approximately 14% of the investment portfolio, on a fair value basis as of both September 30, 2016 and December 31, 2015. The internally managed portfolio consists primarily of the Company's investments in securities for (i) loss mitigation purposes, (ii) other risk management purposes and (iii) where the Company believes a particular security presents an attractive investment opportunity.

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

Internally Managed Portfolio
Carrying Value

	As of September 30, 2016	As of December 31, 2015
	(in millions)	
Assets purchased for loss mitigation and other risk management purposes:		
Fixed-maturity securities, at fair value	$ 855	$ 870
Other invested assets	13	15
Other	48	45
Total	$ 916	$ 930

Other Invested Assets

Surplus Note from AGC

On December 18, 2009, AGC issued a surplus note with a principal amount of $300 million to AGM. This note carries a simple interest rate of 5.0% per annum and matures on December 31, 2029. Principal is payable at the option of AGC prior to the final maturity of the note in 2029 and interest is payable on the note annually in arrears as of December 31 of each year, commencing December 31, 2010. Payments of principal and interest are subject to AGC having policyholders' surplus in excess of statutory minimum requirements after such payment and to prior written approval by the Maryland Insurance Administration. On April 11, 2016, the surplus note agreement was amended to reduce the simple interest rate to 3.5% per annum effective January 1, 2016. There was no principal paydown on the surplus note by AGC.

10. Insurance Company Regulatory Requirements

Dividend Restrictions and Capital Requirements

Under New York insurance law, AGM may only pay dividends out of "earned surplus," which is the portion of the company's surplus that represents the net earnings, gains or profits (after deduction of all losses) that have not been distributed to shareholders as dividends or transferred to stated capital or capital surplus, or applied to other purposes permitted by law, but does not include unrealized appreciation of assets. AGM may pay dividends without the prior approval of the New York Superintendent of Financial Services ("New York Superintendent") that, together with all dividends declared or distributed by it during the preceding 12 months, does not exceed the lesser of 10% of its policyholders' surplus (as of its last annual or quarterly statement filed with the New York Superintendent) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGM to distribute as dividends without regulatory approval is estimated to be approximately $247 million, of which approximately $55 million is estimated to be available for distribution in the fourth quarter of 2016.

MAC is a New York domiciled insurance company subject to the same dividend limitations described above for AGM. Assured Guaranty does not currently anticipate that MAC will distribute any dividends. On June 30, 2016, MAC obtained approval from the New York State Department of Financial Services to repay its $300 million surplus note to MAC Holdings and its $100 million surplus note (plus accrued interest) to AGM. Accordingly, on June 30, 2016, MAC transferred cash and/or marketable securities to (i) MAC Holdings in an aggregate amount equal to $300 million, and (ii) AGM in an aggregate amount of $102.5 million. MAC Holdings, upon receipt of such $300 million from MAC, distributed cash and/or marketable securities in an aggregate amount of $300 million to its shareholders, AGM and AGC, in proportion to their respective 60.7% and 39.3% ownership interests such that AGM received $182 million and AGC received $118 million.

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

Dividends and Surplus Note
By Insurance Company

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)		(in millions)	
Dividends paid by AGM to AGMH	$ 65	$ 57	$ 192	$ 163
Repayment of surplus note by AGM to AGMH	—	—	—	25
Repayment of surplus note by MAC to AGM	—	—	100	—
Repayment of surplus note by MAC to MAC Holdings (1)	—	—	300	—

(1) MAC Holdings returned $300 million to AGM and AGC, in proportion to their ownership percentages, in the second quarter of 2016.

Stock Redemption Plan

On November 25, 2016, the Superintendent approved AGM's request to repurchase 125 of its shares of common stock from its direct parent, AGMH, for approximately $300 million. AGM intends to implement the stock redemption plan in December 2016. Each share repurchased by AGM will be retired and cease to be an authorized share. Pursuant to AGM's Amended and Restated Charter, the par value of AGM's remaining shares of common stock issued and outstanding will increase automatically in order to maintain AGM's total paid-in capital at $15 million and its authorized capital at $20 million.

11. Income Taxes

Overview

The Company files its US federal tax return as a part of the consolidated group for Assured Guaranty US Holdings Inc. (“AGUS”), an indirect parent holding company. Each member of the AGUS consolidated tax group is part of a tax sharing agreement and pays or receives its proportionate share of the consolidated regular federal tax liability for the group as if each company filed on a separate return basis.

Provision for Income Taxes

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

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

Effective Tax Rate Reconciliation

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Expected tax provision (benefit) at statutory rate	$ 42	$ 65	$ 134	$ 169
Tax-exempt interest	(9)	(10)	(28)	(31)
Change in liability for uncertain tax position	5	8	5	8
Provision to file true-up	(6)	(8)	(6)	(8)
Other	(4)	(1)	(5)	(2)
Total provision (benefit) for income taxes	$ 28	$ 54	$ 100	$ 136
Effective tax rate	23.9%	28.7%	26.3%	28.1%

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

Valuation Allowance

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

Audits

AGUS has open tax years with the U.S. Internal Revenue Service ("IRS") for 2009 forward and is currently under audit for the 2009 - 2012 tax years. The Company's U.K. subsidiary, AGE, is not currently under examination and has open tax years of 2014 forward.

Uncertain Tax Positions

The Company's policy is to recognize interest and penalties related to uncertain tax positions in income tax expense and has accrued $0.6 million for Nine Months 2016 and $0.5 million for 2015. As of September 30, 2016 and December 31, 2015, the Company has accrued $3.4 million and $2.8 million of interest, respectively.

The total amount of unrecognized tax benefits as of September 30, 2016 and December 31, 2015, that would affect the effective tax rate, if recognized, was $26.3 million and $20.9 million, respectively.

12. Reinsurance and Other Monoline Exposures

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

Ceded and Assumed Business

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

AGM is also party to reinsurance agreements as a reinsurer to its affiliated financial guaranty insurance companies. In 2013, MAC assumed a book of U.S. public finance business from AGM and AGC.

The Company has assumed business primarily from its affiliate, AGC. Under this relationship, the Company assumes a portion of the ceding company's insured risk in exchange for a premium. The Company may be exposed to risk in this portfolio in that the Company may be required to pay losses without a corresponding premium in circumstances where the ceding company is experiencing financial distress and is unable to pay premiums. The Company's agreement with AGC is generally subject to termination at the option of the ceding company if the Company fails to meet certain financial and regulatory criteria or to maintain a specified minimum financial strength rating. Upon termination under these conditions, the Company may be required to return to the ceding company unearned premiums and loss reserves calculated on a statutory basis of accounting, attributable to the reinsurance assumed, after which the Company would be released from liability with respect

to the Assumed Business. Upon the occurrence of the conditions set forth above, whether or not an agreement is terminated, the Company may be obligated to increase the level of ceding commission paid.

In Nine Months 2016, the Company entered into a commutation agreement to reassume previously ceded U.S. structured finance business. In Nine Months 2015, the Company entered into a commutation agreement to reassume previously ceded U.S. public finance business. For such reassumption, the Company received the statutory unearned premium outstanding as of the commutation date plus a commutation premium.

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

Effect of Reinsurance on Statement of Operations

	Third Quarter		Nine Months	
	2016	2015	2016	2015
	(in millions)			
Premiums Written:				
Direct	$ 14	$ 42	$ 80	$ 75
Assumed (1)	0	(1)	(1)	(1)
Ceded	(9)	(15)	(53)	(27)
Net	$ 5	$ 26	$ 26	$ 47
Premiums Earned:				
Direct	$ 127	$ 152	$ 414	$ 411
Assumed	16	11	41	28
Ceded	(38)	(46)	(113)	(120)
Net	$ 105	$ 117	$ 342	$ 319
Loss and LAE:				
Direct	$ 38	$ 67	$ 166	$ 177
Ceded	(27)	(30)	(65)	(76)
Net	$ 11	$ 37	$ 101	$ 101

(1) Negative assumed premiums written were due to changes in expected debt service schedules.

Other Monoline Exposures

In addition to assumed and ceded reinsurance arrangements, the Company may also have exposure to some financial guaranty reinsurers (i.e., monolines) in other areas. Second-to-pay insured par outstanding represents transactions the Company has insured that were previously insured by other monolines. The Company underwrites such transactions based on the underlying insured obligation without regard to the primary insurer. Another area of exposure is in the investment portfolio where the Company holds fixed-maturity securities that are wrapped by monolines and whose value may change based on the rating of the monoline. As of September 30, 2016, based on fair value, the Company had fixed-maturity securities in its investment portfolio consisting of $122 million insured by National, $96 million insured by Ambac, $61 million insured by AGC, $269 million insured by the Company's affiliate Assured Guaranty (UK) Ltd., and $8 million insured by other guarantors.

In addition, the Company acquired bonds for loss mitigation or other risk management purposes. As of September 30, 2016 these bonds had a fair value of $135 million insured by FGIC UK Limited.

Monoline and Reinsurer Exposure by Company

	Ratings at December 6, 2016		Par Outstanding As of September 30, 2016		
Reinsurer	Moody's Reinsurer Rating	S&P Reinsurer Rating	Ceded Par Outstanding(1)	Second-to-Pay Insured Par Outstanding(1)	Assumed Par Outstanding
				(dollars in millions)	
Affiliated Companies: (3)					
AGC (2), (10)	A3	AA	$ 2,839	$ 172	$ 17,719
Assured Guaranty Re Ltd. ("AG Re") (2)	WR (4)	AA	54,359	—	—
Affiliated Companies			57,198	172	17,719
Non-Affiliated Companies:					
Tokio Marine & Nichido Fire Insurance Co., Ltd. (2)	Aa3 (5)	A+ (5)	3,685	—	—
American Overseas Reinsurance Company Limited (2)	WR	WR	3,415	—	30
Syncora Guarantee Inc. (2)	WR	WR	2,185	464	481
Mitsui Sumitomo Insurance Co. Ltd. (2)	A1	A+ (5)	1,394	—	—
ACA Financial Guaranty Corp.	NR (6)	WR	637	—	—
National (7)	A3	AA-	—	3,173	—
Ambac	WR	WR	—	1,919	—
MBIA	(8)	(8)	—	854	—
FGIC	(9)	(9)	—	668	—
Ambac Assurance Corp. Segregated Account	NR	NR	—	75	—
Other	Various	Various	21	—	0
Non-Affiliated Companies			11,337	7,153	511
Total			$ 68,535	$ 7,325	$ 18,230

(1) Includes par related to insured credit derivatives.

(2) The total collateral posted by all affiliated and non-affiliated reinsurers required or agreeing to post collateral as of September 30, 2016, was approximately $1.0 billion. The collateral excludes amounts for the benefit of AGE.

(3) MAC is rated AA+ (stable outlook) from KBRA and of AA (stable outlook) from S&P. Assumed par outstanding includes $17,689 million assumed by MAC from AGC.

(4) Represents "Withdrawn Rating."

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

(6) Represents "Not Rated."

(7) Rated AA+ by KBRA.

(8) MBIA includes subsidiaries MBIA Insurance Corporation, rated CCC by S&P and Caa1 by Moody's, and MBIA UK Insurance Ltd., rated BB by S&P and Ba2 by Moody's. On September 29, 2016, Assured Guaranty Ltd. announced that the Company's affiliate, AGC, entered into an agreement to acquire MBIA UK Insurance Limited, the European operating subsidiary of MBIA Insurance Corporation.

(9) FGIC includes subsidiaries Financial Guaranty Insurance Company and FGIC UK Limited, both of whose financial strength ratings have been withdrawn by the rating agencies.

(10) On September 20, 2016, KBRA assigned a financial strength rating of AA (stable outlook) to AGC.

Amounts Due (To) From Reinsurers
As of September 30, 2016

	Assumed Premium	Ceded Premium, net of Commissions	Ceded Expected Loss to be Paid
		(in millions)	
AGC	$ 1	$ (10)	$ 29
AG Re	—	(43)	72
American Overseas Reinsurance Company Limited	—	(4)	30
Tokio Marine & Nichido Fire Insurance Co., Ltd.	—	(10)	45
Syncora Guarantee Inc.	13	(19)	(7)
Mitsui Sumitomo Insurance Co. Ltd.	—	(3)	20
Other	—	(10)	—
Total	$ 14	$ (99)	$ 189

Excess of Loss Reinsurance Facility

AGC, AGM and MAC entered into a $360 million aggregate excess of loss reinsurance facility with a number of reinsurers, effective as of January 1, 2016. This facility replaces a similar $450 million aggregate excess of loss reinsurance facility that AGC, AGM and MAC had entered into effective January 1, 2014 and which terminated on December 31, 2015. The new facility covers losses occurring either from January 1, 2016 through December 31, 2023, or January 1, 2017 through December 31, 2024, at the option of AGC, AGM and MAC. It terminates on January 1, 2018, unless AGC, AGM and MAC choose to extend it. The new facility covers certain U.S. public finance credits insured or reinsured by AGC, AGM and MAC as of September 30, 2015, excluding credits that were rated non-investment grade as of December 31, 2015 by Moody's or S&P or internally by AGC, AGM or MAC and is subject to certain per credit limits. Among the credits excluded are those associated with the Commonwealth of Puerto Rico and its related authorities and public corporations. The new facility attaches when AGC's, AGM's and MAC's net losses (net of AGC's and AGM's reinsurance (including from affiliates) and net of recoveries) exceed $1.25 billion in the aggregate. The new facility covers a portion of the next $400 million of losses, with the reinsurers assuming pro rata in the aggregate $360 million of the $400 million of losses and AGC, AGM and MAC jointly retaining the remaining $40 million. The reinsurers are required to be rated at least AA- or to post collateral sufficient to provide AGC, AGM and MAC with the same reinsurance credit as reinsurers rated AA-. AGC, AGM and MAC are obligated to pay the reinsurers their share of recoveries relating to losses during the coverage period in the covered portfolio. AGC, AGM and MAC paid approximately $9 million of premiums in 2016 (of which AGM and MAC paid approximately $8 million) for the term January 1, 2016 through December 31, 2016 and deposited approximately $9 million of securities into trust accounts for the benefit of the reinsurers to be used to pay the premium for January 1, 2017 through December 31, 2017. The main differences between the new facility and the prior facility that terminated on December 31, 2015 are the reinsurance attachment point ($1.25 billion versus $1.5 billion), the total reinsurance coverage ($360 million part of $400 million versus $450 million part of $500 million) and the annual premium ($9 million versus $19 million).

13. Commitments and Contingencies

Leases

In 2015, AGM entered into an operating lease for new office space comprising one full floor and one partial floor at 1633 Broadway in New York City. On September 23, 2016, AGM entered into an amendment to that lease to include the remaining portion of the partial floor for the remainder of the lease term. The fixed annual rent, which commences after an initial rent holiday, begins at $1.1 million per annum, rising in two steps to $1.3 million for the last five years of the initial term.

Legal Proceedings

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

In addition, in the ordinary course of their respective businesses, the Company and its affiliates assert claims in legal proceedings against third parties to recover losses paid in prior periods or prevent losses in the future, as described in the "Recovery Litigation" section of Note 4, Expected Loss to be Paid. For example, in January 2016, the Company commenced an action for declaratory judgment and injunctive relief in the U.S. District Court for the District of Puerto Rico to invalidate executive orders issued by the Governor of Puerto Rico directing the retention or transfer of certain taxes and revenues pledged to secure the payment of certain bonds insured by the Company, and in July 2016, the Company filed a motion and form of complaint in the U.S. District Court for the District of Puerto Rico seeking relief from the PROMESA stay in order to file a complaint to protect its interest in certain pledged PRHTA toll revenues. The amounts, if any, the Company will recover in these and other proceedings to recover losses are uncertain, and recoveries, or failure to obtain recoveries, in any one or more of these proceedings during any quarter or year could be material to the Company's results of operations in that particular quarter or year.

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

Litigation

Proceedings Relating to the Company's Financial Guaranty Business

AGM and AGMH receive subpoenas *duces tecum* and interrogatories from regulators from time to time.

On September 25, 2013, Wells Fargo Bank, N.A., as trust administrator of the MASTR Adjustable Rate Mortgages Trust 2007-3, filed an interpleader complaint in the U.S. District Court for the Southern District of New York seeking adjudication of a dispute between Wales LLC and Assured Guaranty Municipal Corp. as to whether AGM is entitled to reimbursement payments from certain cashflows for principal claims paid in respect of insured certificates. On September 30, 2016, the court issued an opinion denying the motion for judgment on the pleadings filed by Wales. The Company estimates that an adverse outcome to the interpleader proceeding could increase losses on the transaction by approximately \$10 - \$20 million, net of expected settlement payments and reinsurance in force.

Proceedings Related to AGMH's Former Financial Products Business

The following is a description of legal proceedings involving AGMH's former Financial Products Business. Although Assured Guaranty did not acquire AGMH's former Financial Products Business, which included AGMH's former GIC business, medium term notes business and portions of the leveraged lease businesses, certain legal proceedings relating to those businesses are against entities that Assured Guaranty did acquire. While Dexia SA and Dexia Crédit Local S.A (together, "Dexia") have paid all expenses and settlement amounts due to date as a result of the proceedings described below, such indemnification might not be sufficient to fully hold the Company harmless against any injunctive relief or civil or criminal sanction that is imposed against the Company as a result of any potential newly asserted claims related to these matters.

Governmental Investigations into Former Financial Products Business

AGMH and/or AGM received subpoenas *duces tecum* and interrogatories or civil investigative demands from the Attorneys General of the States of Connecticut, Florida, Illinois, Massachusetts, Missouri, New York, Texas and West Virginia relating to their investigations of alleged bid rigging of municipal GICs. In addition, AGMH received a subpoena from the Antitrust Division of the Department of Justice in November 2006 issued in connection with an ongoing criminal investigation of bid rigging of awards of municipal GICs and other municipal derivatives. AGMH responded to such requests when they were received several years ago. While it is possible AGMH may receive additional inquiries from these or other regulators, the Company is not currently aware that any governmental authority, including such Attorneys General or the Department of Justice, are actively pursuing or contemplating legal proceedings with respect to AGMH's former Financial Products Business.

Lawsuits Relating to Former Financial Products Business

From 2008 through 2010, complaints were brought on behalf of a purported class of state, local and municipal government entities alleging federal antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. These actions were consolidated before one judge in the Southern District of New York as Municipal Derivatives Antitrust Litigation ("MDL 1950"). Following motions to dismiss, amended class action complaints were filed on behalf of a putative class of plaintiffs. The most recently amended, operative class action complaint does not list AGMH or its affiliates as defendants or co-conspirators. On July 8, 2016, the MDL 1950 Court entered an order approving settlement of the remaining class claims, resolving the putative class case.

In addition, the Attorney General of the State of West Virginia filed a lawsuit that, as amended, named AGM and Assured Guaranty US Holdings as defendants and alleged a conspiracy to decrease the returns that West Virginia public entities earned on municipal derivative instruments. Also, approximately 19 California and New York government entities brought individual lawsuits that were not a part of the class action and that did not dismiss AGMH or its affiliates. All these cases were transferred to the Southern District of New York and consolidated with MDL 1950 for pretrial purposes. In June and July 2016, Dexia executed settlement agreements covering the action brought by the Attorney General of the State of West Virginia and the actions brought by the individual California and New York plaintiffs, and on July 1, 2016 and July 27, 2016, respectively, the MDL 1950 court dismissed with prejudice the claims against Assured Guaranty US Holdings and AGM in all such actions. Those settlements release all claims as to Assured Guaranty US Holdings, AGMH and AGM, as well as their parents, subsidiaries and affiliates.

14. Notes Payable and Credit Facilities

Notes Payable

Notes Payable represents debt issued by VIEs consolidated by AGM to one of the Financial Products Companies that were transferred to Dexia Holdings Inc. prior to the acquisition of AGMH. The funds borrowed were used to finance the purchase of the underlying obligations of AGM-insured obligations which had breached triggers allowing AGM to exercise its right to accelerate payment of a claim in order to mitigate loss. The assets purchased are classified as assets acquired in refinancing transactions and recorded in “other invested assets.” The terms of the notes payable match the terms of the assets acquired in refinancing transactions.

The principal and carrying values of the Company's notes payable are presented in the table below.

Principal and Carrying Amounts of Notes Payable

	As of September 30, 2016		As of December 31, 2015	
	Principal	Carrying Value	Principal	Carrying Value
	(in millions)			
Notes Payable	$ 10	$ 11	$ 12	$ 13

Interest expense incurred and paid on notes payable was less than $1 million for all periods presented.

Recourse Credit Facilities

2009 Strip Coverage Facility

In connection with the Company's acquisition of AGMH and its subsidiaries from Dexia Holdings Inc., AGM agreed to retain the risks relating to the debt and strip policy portions of the leveraged lease business.

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

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

Currently, all the leveraged lease transactions in which AGM acts as strip coverage provider are breaching a rating trigger related to AGM and are subject to early termination. However, early termination of a lease does not result in a draw on the AGM policy if the tax-exempt entity makes the required termination payment. If all the leases were to terminate early and the tax-exempt entities do not make the required early termination payments, then AGM would be exposed to possible liquidity claims on gross exposure of approximately $991 million as of September 30, 2016. To date, none of the leveraged lease transactions that involve AGM has experienced an early termination due to a lease default and a claim on the AGM policy. At September 30, 2016, approximately $1.5 billion of cumulative strip par exposure had been terminated since 2008 on a consensual basis. The consensual terminations have resulted in no claims on AGM.

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

There have never been any borrowings under the Strip Coverage Facility, the amount of the leveraged leases covered by the Strip Coverage Facility has declined since July 1, 2009, and, as noted above, to date none of the leveraged lease transactions in which AGM acts as the strip coverage provider has experienced an early termination due to a lease default. Consequently, and in view of the credit quality of the relevant tax-exempt entities and the cost of the Strip Coverage Facility, the Company determined that maintaining the Strip Coverage Facility was no longer warranted. On July 29, 2016, the parties terminated the facility.

AGM CPS Securities

In June 2003, $200 million of “AGM CPS”, money market preferred trust securities, were issued by trusts created for the primary purpose of issuing the AGM CPS, investing the proceeds in high-quality commercial paper and selling put options to AGM, allowing AGM to issue the trusts non-cumulative redeemable perpetual preferred stock (the “AGM Preferred Stock”) of AGM in exchange for cash. There are four trusts, each with an initial aggregate face amount of $50 million. These trusts hold auctions every 28 days, at which time investors submit bid orders to purchase AGM CPS. If AGM were to exercise a put option, the applicable trust would transfer the portion of the proceeds attributable to principal received upon maturity of its assets, net of expenses, to AGM in exchange for AGM Preferred Stock. AGM pays a floating put premium to the trusts, which represents the difference between the commercial paper yield and the winning auction rate (plus all fees and expenses of the trust). If an auction does not attract sufficient clearing bids, however, the auction rate is subject to a maximum rate of one-month LIBOR plus 200 basis points for the next succeeding distribution period. Beginning in August 2007, the AGM CPS required the maximum rate for each of the relevant trusts. AGM continues to have the ability to exercise its put option and cause the related trusts to purchase AGM Preferred Stock. The trusts provide AGM access to new capital at its sole discretion through the exercise of the put options. As of September 30, 2016, the put option had not been exercised.

See Note 6, Fair Value Measurement, –Other Assets–Committed Capital Securities, for a fair value measurement discussion.

15. Other Comprehensive Income

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

Changes in Accumulated Other Comprehensive Income by Component
Third Quarter 2016

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, June 30, 2016	$ 192	$ (37)	$ 155
Other comprehensive income (loss) attributable to AGM before reclassifications	(25)	3	(22)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(2)	4	2
Tax (provision) benefit	1	(1)	0
Total amount reclassified from AOCI, net of tax	(1)	3	2
Net current period other comprehensive income (loss) attributable to AGM	(26)	6	(20)
Balance, September 30, 2016	$ 166	$ (31)	$ 135

Changes in Accumulated Other Comprehensive Income by Component
Third Quarter 2015

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, June 30, 2015	$ 120	$ (3)	$ 117
Other comprehensive income (loss) attributable to AGM before reclassifications	16	(8)	8
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	8	12	20
Net investment income	(9)	—	(9)
Tax (provision) benefit	0	(4)	(4)
Total amount reclassified from AOCI, net of tax	(1)	8	7
Net current period other comprehensive income (loss) attributable to AGM	15	0	15
Balance, September 30, 2015	$ 135	$ (3)	$ 132

Changes in Accumulated Other Comprehensive Income by Component
Nine Months 2016

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, December 31, 2015	$ 133	$ (23)	$ 110
Other comprehensive income (loss) attributable to AGM before reclassifications	40	(21)	19
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(8)	20	12
Net investment income	(3)	—	(3)
Tax (provision) benefit	4	(7)	(3)
Total amount reclassified from AOCI, net of tax	(7)	13	6
Net current period other comprehensive income (loss) attributable to AGM	33	(8)	25
Balance, September 30, 2016	$ 166	$ (31)	$ 135

Changes in Accumulated Other Comprehensive Income by Component
Nine Months 2015

	Net Unrealized Gains (Losses) on Investments with no Other-Than-Temporary Impairment	Net Unrealized Gains (Losses) on Investments with Other-Than-Temporary Impairment	Total Accumulated Other Comprehensive Income
		(in millions)	
Balance, December 31, 2014	$ 186	$ (2)	$ 184
Other comprehensive income (loss) attributable to AGM before reclassifications	(49)	(13)	(62)
Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	6	18	24
Net investment income	(9)	—	(9)
Tax (provision) benefit	1	(6)	(5)
Total amount reclassified from AOCI, net of tax	(2)	12	10
Net current period other comprehensive income (loss) attributable to AGM	(51)	(1)	(52)
Balance, September 30, 2015	$ 135	$ (3)	$ 132

16. Subsequent Events

Subsequent events have been considered through December 12, 2016, the date on which these financial statements were issued.

APPENDIX 6

ANNUAL REPORT AND FINANCIAL STATEMENTS OF PROJECTCO

Registered number: 8038090

ULIVING@ESSEX LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2015

ULIVING@ESSEX LIMITED

COMPANY INFORMATION

Directors	M Davies (resigned 15 July 2015) M Fowkes N Guerin (resigned 17 December 2015) I Smith N Swiderski (resigned 17 December 2015) P Sheldrake S Veal (appointed 15 July 2015)
Company secretary	D Adams (appointed 1 February 2016)
Registered number	8038090
Registered office	Welken House 10-11 Charterhouse Square London EC1M 6EH
Independent auditors	Grant Thornton UK LLP Statutory Auditor & Chartered Accountants Grant Thornton House Melton Street Euston Square London NW1 2EP

ULIVING@ESSEX LIMITED

CONTENTS

STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

Introduction

The directors present their strategic report of ULiving@Essex Limited (the "Company") for the year ended 31 December 2015.

Business review

The profit for the year before taxation was £124k (2014: loss £730k).

Having completed the construction phase of the Meadows building in 2013, the directors consider that the operating phase of the project is performing satisfactorily.

Principal activities

The principal activity of the Company is to design, build, finance and manage student accommodation for the period of 51 years from August 2012 to August 2063 pursuant to a project agreement dated 7 August 2012. The construction of the new accommodation achieved practical completion on 18 September 2013.

The directors do not recommend the payment of a dividend (2014: £nil).

Financial key performance indicators

The directors consider revenue, operating profit, profit before tax and profit after tax and achievement of milestones under the PFI/PPP concessions to be the key performance indicators of the Company.

Principal risks and uncertainties

Under the terms of the PFI/PPP concession contracts, the Company is required to meet certain key performance targets. The directors review actual performance against those targets on a regular basis to mitigate risks arising from contract activities.

The Company's main commercial risks during the period are attributable to the collection of rent and repayment of senior loan facility.

The Company has committed term loan facilities which are secured on the assets and future revenues of the Company.

The Company's cash flow risk is managed by monitoring cash flow as part of the day-to-day control procedures. The Directors consider cash flow projections to ensure appropriate facilities are available to be drawn as necessary.

This report was approved by the board and signed on its behalf.

P Sheldrake
Director

Date: 7 June 2016

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

The directors present their report and the financial statements for the year ended 31 December 2015.

Results and dividends

The profit for the year, after taxation, amounted to £124k *(2014 - loss £730k).*

Directors

The directors who served during the year were:

M Davies (resigned 15 July 2015)
M Fowkes
N Guerin (resigned 17 December 2015)
I Smith
N Swiderski (resigned 17 December 2015)
P Sheldrake
S Veal (appointed 15 July 2015)

Going concern

The Company meets its day to day working capital requirements principally through a mixture of shareholder loans and project related bank term loans. The bank term loans are in place to 2047 and interest payments are fixed for the term of the loan.

The Company's forecasts and projections, taking into account of reasonably possible changes in trading performance show that the Company should be able to operate within the level of its current facilities,

The directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly the Directors continue to adopt the going concern basis on preparing the financial statements.

Principal risks and uncertainties

Under the terms of the PFI/PPP concession contracts, the Company is required to meet certain key performance targets. The directors review actual performance against those targets on a regular basis to mitigate risks arising from contract activities.

The Company's main commercial risks during the period are attributable to the collection of rent and repayment of senior loan facility.

The Company has committed term loan facilities which are secured on the assets and future revenues of the Company.

The Company's cash flow risk is managed by monitoring cash flow as part of the day-to-day control procedures. The Directors consider cash flow projections to ensure appropriate facilities are available to be drawn as necessary.

The Company managed its liquidity risk based on business needs, tax, capital or regulatory consideration, if applicable, through numerous sources of finance in order to maintain flexibility.

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

Future developments

The Directors of the Company are not aware of any circumstances by which the principal activity of the Company would alter or cease.

Disclosure of information to auditors

Each of the persons who are directors at the time when this Directors' Report is approved has confirmed that:

- so far as that director is aware, there is no relevant audit information of which the Company's auditors are unaware, and
- that director has taken all the steps that ought to have been taken as a director in order to be aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Auditors

The auditors, Grant Thornton UK LLP, will be proposed for reappointment in accordance with section 485 of the Companies Act 2006.

This report was approved by the board and signed on its behalf.

P Sheldrake
Director

Date: 7 June 2016

DIRECTORS' RESPONSIBILITIES STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2015

The directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland'. Under Company law the directors must not approve the financial statements unless they are satisfied that they give give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies for the Company financial statements and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ULIVING@ESSEX LIMITED

We have audited the financial statements of ULiving@Essex Limited for the year ended 31 December 2015, which comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Cash Flows, the Statement of Changes in Equity. and the related notes. The financial reporting framework that has been applied in their preparation is applicable law including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland'.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an Auditors' Report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Financial Reporting Council's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2015 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements and the directors' report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ULIVING@ESSEX LIMITED

Richard Hagley

Richard Hagley (Senior Statutory Auditor)

for and on behalf of
Grant Thornton UK LLP

Statutory Auditor
Chartered Accountants

Grant Thornton House
Melton Street
Euston Square
London
NW1 2EP

7 June 2016

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2015

	Note	2015 £000	*2014 £000*
Turnover	3	**7,583**	*7,284*
Cost of sales		**(2,180)**	*(2,442)*
Gross profit		**5,403**	*4,842*
Administrative expenses		**(1,356)**	*(1,350)*
Operating profit	4	**4,047**	*3,492*
Interest receivable and similar income	6	**1**	*2*
Interest payable and expenses	7	**(3,924)**	*(4,224)*
Profit/(loss) on ordinary activities before tax		**124**	*(730)*
Profit/(loss) for the year		**124**	*(730)*
Other comprehensive income for the year			
Total comprehensive income for the year		**124**	*(730)*

The notes on pages pages 12 to 23 form part of these financial statements.

There were no recognised gains and losses other than those included in the statement of comprehensive income.

The statement of comprehensive income has been prepared on the basis that all operations are continuing operations.

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2015

	Note		2015 £000		*2014 £000*
Fixed assets					
Tangible assets	9		**61,616**		*62,972*
			61,616		*62,972*
Current assets					
Debtors: amounts falling due within one year	10	**759**		*1,908*	
Cash at bank and in hand	11	**2,266**		*1,942*	
		3,025		*3,850*	
Creditors: amounts falling due within one year	12	**(2,467)**		*(3,763)*	
Net current assets			**558**		*87*
Total assets less current liabilities			**62,174**		*63,059*
Creditors: amounts falling due after more than one year	13		**(62,939)**		*(63,948)*
Net liabilities			**(765)**		*(889)*
Capital and reserves					
Called up share capital	16		**15**		*15*
Profit and loss account			**(780)**		*(904)*
			(765)		*(889)*

The financial statements were approved and authorised for issue by the board and were signed on its behalf by:

P Sheldrake
Director

Date: 7 June 2016

The notes on pages 12 to 23 form part of these financial statements.

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2015

	Share capital	Retained earnings	Total equity
	£000	£000	£000
At 1 January 2015	15	(904)	(889)
Comprehensive income for the year			
Profit for the year	-	124	124
At 31 December 2015	15	(780)	(765)

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2014

	Share capital	Retained earnings	Total equity
	£000	£000	£000
At 1 January 2014	15	(174)	(159)
Comprehensive income for the year			
Loss for the year	-	(730)	(730)
At 31 December 2014	15	(904)	(889)

The notes on pages 12 to 23 form part of these financial statements.

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2015

	2015 £000	*2014 £000*
Cash flows from operating activities		
Profit/(loss) for the financial year	**124**	*(730)*
Adjustments for:		
Amortisation of debt issue costs	**28**	*29*
Depreciation of tangible assets	**1,356**	*1,350*
Interest paid	**3,924**	*4,224*
Interest received	**(1)**	*(2)*
Increase in debtors	**1,148**	*778*
(Decrease)/increase in creditors	**(1,379)**	*221*
Net cash generated from operating activities	**5,200**	*5,870*
Cash flows from investing activities		
Purchase of tangible fixed assets	**-**	*(338)*
Interest received	**1**	*2*
Net cash from investing activities	**1**	*(336)*
Cash flows from financing activities		
Repayment of loans	**(810)**	*(780)*
Loans from group companies repaid	**(143)**	*(73)*
Interest paid	**(3,924)**	*(4,224)*
Net cash used in financing activities	**(4,877)**	*(5,077)*
Net increase in cash and cash equivalents	**324**	*457*
Cash and cash equivalents at beginning of year	**1,942**	*1,485*
Cash and cash equivalents at the end of year	**2,266**	*1,942*
Cash and cash equivalents at the end of year comprise:		
Cash at bank and in hand	**2,266**	*1,942*
	2,266	*1,942*

1. Accounting policies

1.1 Basis of preparation of financial statements

The financial statements have been prepared under the historical cost convention and in accordance with Financial Reporting Standard 102, the Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland and the Companies Act 2006.

The preparation of financial statements in compliance with FRS 102 requires the use of certain critical accounting estimates. It also requires management to exercise judgment in applying the Company's accounting policies (see note 2).

The Company is registered in England and Wales under the Companies Act 2006.

The presentational currency is sterling (£).

The following principal accounting policies have been applied:

1.2 Going concern

The directors have, at the time of approving the financial statements, a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the financial statements. Further details are contained in the Directors' Report.

1.3 Revenue

Turnover represents income received in the ordinary course of business for services provided and excludes value added tax.

Revenue is recognised on a straight-line basis over the term of the relevant lease.

1.4 Tangible fixed assets

The property achieved practical completion in September 2013 and is being carried at cost, which includes professional fees and borrowing costs capitalised in accordance with the Company's accounting policy. Depreciation commenced in September 2013 with a full month charge in that month.

Land and buildings are stated at cost, net of depreciation and any provision for impairment. Depreciation is provided on tangible fixed assets, except freehold land, at rates calculated to write off the cost, less estimated residual value, on a straight-line basis over their expected useful lives.

Depreciation is provided on the following basis:

Freehold property	- 50 years
Capitalised fees	- 10 years

Residual value is £nil as the head lease passes back to the University for a nominal value £1 at the end of the concession. No depreciation was provided during construction.

1. Accounting policies (continued)

1.5 Debtors

Short term debtors are measured at transaction price, less any impairment. Loans receivable are measured initially at fair value, net of transaction costs, and are measured subsequently at amortised cost using the effective interest method, less any impairment.

1.6 Cash and cash equivalents

Cash is represented by cash in hand and deposits with financial institutions repayable without penalty on notice of not more than 24 hours. Cash equivalents are highly liquid investments that mature in no more than three months from the date of acquisition and that are readily convertible to known amounts of cash with insignificant risk of change in value.

1.7 Financial instruments

Financial assets and financial liabilities are recognised in the Company's balance sheet when the Company becomes a party to the contractual provisions of the instrument. The Company has not classified any of its financial assets as held to maturity or available-for-sale.

Financial assets

All financial assets are recognised and derecognised on a trade date where the purchase or sale of a financial asset is under a contract whose terms require delivery of the financial asset within the time frame established by the market concerned, and are initially measured at fair value.

Loans and receivables

These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise principally through the provision of goods and services to customers (trade receivables) under PFI contracts but also incorporate other types of contractual monetary asset. They are carried at cost less any provision for impairment.

Impairment of financial asset

Impairment of financial assets relates to trade receivables. They are assessed for indicators of impairment at each balance sheet date. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

Derecognition of financial assets

The Company derecognises a financial asset only when the contractual rights to the cash flows from the asset expire or when it transfers the financial asset and substantially all the risk and rewards of ownership of the asset to another entity.

Financial liabilities and equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

1. Accounting policies (continued)

1.7 Financial instruments (continued)

An Equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recognised at the proceeds received.

Derecognition of financial liabilities

The Company derecognises financial liabilities when, and only when, the Company's obligations are discharged, cancelled or they expire.

1.8 Creditor

Short term creditors are measured at the transaction price. Other financial liabilities, including bank loans, are measured initially at fair value, net of transaction costs, and are measured subsequently at amortised cost using the effective interest method.

1.9 Finance costs

Upfront finance costs of procuring senior debt facilities are capitalised during construction and subsequently amortized over the life of the relevant loans and charged to the profit and loss account. Arrangement fees for these facilities have been capitalised against the cost of the loan.

Finance costs that are directly attributable to the cost of construction of the fixed assets are capitalised as part of the cost of those assets. The commencement of capitalisation begins when both finance costs and expenditure for the assets are being incurred and activities that are necessary to get the assets ready for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to get the assets ready for use are complete.

1.10 Taxation

Current and deferred tax, including UK corporation tax, is provided at amounts expected to be paid using the tax rates and laws that have been enacted or subsequently enacted by the balance sheet date.

Deferred tax assets and liabilities are recognised where the carrying amount of an asset or liability in the balance sheet differs from its tax base, except for differences arising on the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting, nor taxable profit.

Recognition of deferred tax assets is restricted to those instances where it is probable that taxable profit will be available against which the differences can be utilised.

The amount of the asset or liability is determined using tax rates that have been enacted or substantively enacted by the reporting date and are expected to apply when the deferred tax assets are recovered.

Deferred tax assets and liabilities are offset when the Company has a legally enforceable right to offset current tax assets and liabilities and the deferred tax assets and liabilities relate to taxes levied by the same tax authority on the same taxable company.

2. Judgments in applying accounting policies and key sources of estimation uncertainty

The estimates and judgements that have a significant risk of causing a material adjustment to the carrying
amounts of assets and liabilities within the financial year are as follows:

Classification of asset

The Company has entered into a Project Agreement with the University of Essex as well as a lease and leaseback arrangement for two sites upon which student accommodation has been built. The Project Agreement governs the relationship between the University and the Company including terms of use of the University brand in marketing material, the general actions of the Company and University as landlord and operator. Management consider that as the Company takes full occupancy and demand risk associated with the provision of the accommodation, that the building will be fully depreciated during the concession and therefore full value of these assets will be exhausted during the concession, and that the Company has the ability to exercise control over the user of the asset, then the Company should account for the asset of the concession on its balance sheet.

Capitalisation of costs

During the period of construction, all costs incurred as a direct result of financing, designing and constructing the student accommodation, including finance costs, have been capitalised. The directors consider this to be appropriate since the risks and rewards of ownership rest with the Company.

Intercompany agreement – Interest rate

Shareholder loan notes carried an interest rate of 10.5% to 31st August 2013, 7.01% from 1st September 2013 to 31st August 2022, 8.5% from 1st September 2022 to 31st August 2032 and 9.5% thereafter plus a variable element of interest based on annual changes in RPI. The Directors believe that the loan note value in these financial statements reflects its fair value at the balance sheet date.

3. Analysis of turnover

An analysis of turnover by class of business is as follows:

	2015	*2014*
	£000	*£000*
Rental income	**7,555**	*7,255*
Third party revenue	**23**	*29*
Pass through revenue	**5**	*-*
	7,583	*7,284*

	2015	*2014*
	£000	*£000*
United Kingdom	**7,583**	*7,284*
	7,583	*7,284*

4. Operating profit

The operating profit is stated after charging:

	2015 £000	*2014* *£000*
Depreciation of tangible fixed assets	1,356	*1,350*
Fees payable to the Company's auditor and its associates for the audit of the company's annual accounts	9	*9*

5. Directors' remuneration

No staff were directly employed by the company. Services provided by the contractors include the provision of staff and management to perform contractual responsibilities. Costs associated with the staff and management are included within the contractors service charge.

6. Interest receivable

	2015 £000	*2014* *£000*
Bank interest receivable	1	*2*
	1	*2*

7. Interest payable and similar charges

	2015 £000	*2014* *£000*
Bank interest payable	2,616	*2,660*
Other loan interest payable	11	*11*
Loans from group undertakings	1,297	*1,553*
	3,924	*4,224*

8. Taxation

	2015 £000	*2014 £000*
Total current tax	-	*-*
Deferred tax		
Total deferred tax	-	*-*
Taxation on profit on ordinary activities	-	*-*

Factors affecting tax charge for the year

The tax assessed for the year is lower than *(2014 - higher than)* the standard rate of corporation tax in the UK of 20.25% *(2014 - 21.5%)*. The differences are explained below:

	2015 £000	*2014 £000*
Profit on ordinary activities before tax	124	*(730)*
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 20.25% (2014 - 21.5%)	25	*(153)*
Effects of:		
Utilisation of tax losses	(25)	*(184)*
Non-taxable income	-	*337*
Total tax charge for the year	-	*-*

Factors that may affect future tax charges

There were no factors that may affect future tax charges.

A deferred tax asset of £150k has not been recognised due to the uncertainty in respect of future profits. The maximum tax losses potentially available to the Company are £833k.

9. Tangible fixed assets

	Land and buildings £000
Cost or valuation	
At 1 January 2015	**64,769**
At 31 December 2015	**64,769**
Depreciation	
At 1 January 2015	**1,797**
Charge for the period	**1,356**
At 31 December 2015	**3,153**
Net book value	
At 31 December 2015	**61,616**
At 31 December 2014	*62,972*

The land and buildings are carried at cost and are now completed. All construction costs were capitalised and are included in this value. Depreciation commenced September 2013 with a full month charge in that month. Interest and fees capitalised as at balance sheet date 31 December 2015 are £3,242k (2014: £3,449k). Accumulated depreciation of capitalised interest and fees as at the 31 December 2015 is £315k (2014: £180k).

10. Debtors

	2015 £000	*2014 £000*
Trade debtors	**18**	*1,879*
Other debtors	**70**	*-*
Prepayments and accrued income	**671**	*29*
	759	*1,908*

11. Cash and cash equivalents

	2015 £000	*2014 £000*
Cash at bank and in hand	**2,266**	*1,942*
	2,266	*1,942*

12. Creditors: Amounts falling due within one year

	2015 £000	*2014 £000*
Bank loans	**801**	*810*
Trade creditors	**218**	*408*
Amounts owed to group undertakings	**236**	*142*
Accruals and deferred income	**1,212**	*2,403*
	2,467	*3,763*

13. Creditors: Amounts falling due after more than one year

	2015 £000	2014 £000
Bank loans	49,419	50,220
Unamortised debt issue costs	(558)	(586)
Amounts owed to group undertakings	14,078	14,314
	62,939	63,948

Secured loans

Bank borrowings relate to a £52,000,000 loan facility. The term of the loan is 35 years.

As at 31 December 2015 borrowings totalling £50,220,000 (2014: £51,030,000) were outstanding under the facility. Borrowings under this facility are repayable in quarterly instalments commencing November 2013 and ending July 2047.

Interest on amounts drawn is charged at a rate of 5.11%.

The loan facility is secured by fixed and floating charges on the assets of the Company.

Shareholder loans

Subordinate loans constitute unsecured debt issued under the Investment Deed. The total sum available under the Investment Deed is £14,530,334 which matures in 2063. The amounts drawn are repayable in quarterly instalments commencing Feb 2014

Shareholder loan notes carried an interest rate of 10.5% to 31st August 2013, 7.01% from 1st September 2013 to 31st August 2022, 8.5% from 1st September 2022 to 31st August 2032and 9.5% thereafter plus a variable element of interest based on annual changes in RPI.

14. Loans

Analysis of the maturity of loans is given below:

	2015 £000	2014 £000
Amounts falling due within one year		
Bank loans	801	810
	801	810
Amounts falling due 1-2 years		
Bank loans	600	801
	600	801
Amounts falling due 2-5 years		
Bank loans	2,117	2,002
	2,117	2,002
Amounts falling due after more than 5 years		
Bank loans	46,702	47,417
Unamortised debt issue costs	(558)	(586)
	46,144	46,831

15. Financial instruments

	2015 £000	*2014 £000*
Financial assets		
Financial assets measured at amortised cost	**2,284**	*3,821*
	2,284	*3,821*
Financial liabilities		
Financial liabilities measured at amortised cost	**(65,895)**	*(67,047)*
	(65,895)	*(67,047)*

Financial assets measured at amortised cost comprise cash at bank and in hand and trade debtors.

Financial Liabilities measured at amortised cost comprise bank loans, group loans, trade creditors, accruals and other creditors.

16. Share capital

	2015 £000	*2014 £000*
Authorised, allotted, called up and fully paid		
15,000 Ordinary shares of £1 each	**15**	*15*

17. Related party transactions

Equitix Education 2 Limited and Centro Place Investments Limited are considered to be related parties due to their shareholding in the Company's immediate parent company Uliving@Essex Holdco Limited. Transactions with these related parties relate to interest expense on shareholder loans and accrued interest and outstanding loan balances held at the year end. The Directors consider the material transactions undertaken by the Company during the year with related parties to be as follows:

	2015 Interest £000	2015 Creditor £000	2014 Interest £000	2014 Creditor £000
Equitix Education 2 Limited	1,043	12,714	1,242	12,114
Centro Place Investments Limited	194	2,244	233	2,271

18. Controlling party

In the directors' opinion, there is no ultimate controlling party.

The immediate parent company is Uliving@Essex Holdco Limited. The smallest and largest group into which this company is consolidated is ULiving@Essex Holdco Limited. Copies of those accounts can be obtained from Welken House, 10 - 11 Charterhouse Square, London, EC1M 6EH.

19. First time adoption of FRS 102

The policies applied under the entity's previous accounting framework are not materially different to FRS 102 and have not impacted on equity or the statement of comprehensive income.

APPENDIX 7

ANNUAL REPORT AND FINANCIAL STATEMENTS OF HOLDCO

Registered number: 8037507

ULIVING@ESSEX HOLDCO LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2015

ULIVING@ESSEX HOLDCO LIMITED

COMPANY INFORMATION

Directors	M Davies (resigned 15 July 2015) M Fowkes N Guerin (resigned 17 December 2015) I Smith N Swiderski (resigned 17 December 2015) P Sheldrake S Veal (appointed 15 July 2015)
Company secretary	D Adams (appointed 1 February 2016)
Registered number	8037507
Registered office	Welken House 10-11 Charterhouse Square London EC1M 6EH
Independent auditors	Grant Thornton UK LLP Statutory Auditor & Chartered Accountants Grant Thornton House Melton Street Euston Square London NW1 2EP

ULIVING@ESSEX HOLDCO LIMITED

CONTENTS

GROUP STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

Introduction

The directors present their strategic report of ULiving@Essex HoldCo Limited (the "Company") for the year ended 31 December 2015.

Business review

The Group profit for the year before taxation was £124k (2014: loss £730k).

Having completed the construction phase of the Meadows building in 2013, the directors consider that the operating phase of the project is performing satisfactorily.

Principal activities

The principal activity of the Company is that of a holding company. It holds 100% of the share capital of ULiving@Essex Limited, whose principal activity is to design, build, finance and manage student accommodation for the period of 51 years from August 2012 to August 2063 pursuant to a project agreement dated 7 August 2012. The construction of the new accommodation achieved practical completion on 18 September 2013.

The directors do not recommend the payment of a dividend (2014: £nil).

Financial key performance indicators

The directors consider revenue, operating profit, profit before tax and profit after tax and achievement of milestones under the PFI/PPP concessions to be the key performance indicators of the Group.

Principal risks and uncertainties

Under the terms of the PFI/PPP concession contracts, the Group is required to meet certain key performance targets. The directors review actual performance against those targets on a regular basis to mitigate risks arising from contract activities.

The Group's main commercial risks during the period are attributable to the collection of rent and payment of senior loan facility.

The Group has committed term loan facilities which are secured on the assets and future revenues of the Group.

The Group's cash flow risk is managed by monitoring cash flow as part of the day-to-day control procedures. The Directors consider cash flow projections to ensure appropriate facilities are available to be drawn as necessary.

Credit risk is mitigated via monitoring the progress of the project against milestones under the concessions agreement.

The Company manages its liquidity risk based on business needs, tax, capital or regulatory consideration, if applicable, through numerous sources of finance in order to maintain flexibility.

This report was approved by the board and signed on its behalf.

P Sheldrake
Director

Date: 7 June 2016

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

The directors present their report and the financial statements for the year ended 31 December 2015.

Results and dividends

The profit for the year, after taxation, amounted to £124k *(2014 - loss £730k)*.

Directors

The directors who served during the year were:

M Davies (resigned 15 July 2015)
M Fowkes
N Guerin (resigned 17 December 2015)
I Smith
N Swiderski (resigned 17 December 2015)
P Sheldrake
S Veal (appointed 15 July 2015)

Going concern

The Group meets its day to day working capital requirements principally through a mixture of shareholder loans and project related bank term loans. The bank term loans are in place to 2047 and interest payments are fixed for the term of the loan.

The Group's forecasts and projections, taking into account of reasonably possible changes in trading performance show that the Group should be able to operate within the level of its current facilities,

The directors have a reasonable expectation that the Company and Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly the Directors continue to adopt the going concern basis on preparing the financial statements.

Principal risks and uncertainties

Under the terms of the PFI/PPP concession contracts, the Group is required to meet certain key performance targets. The directors review actual performance against those targets on a regular basis to mitigate risks arising from contract activities.

The Group's main commercial risks during the period are attributable to the collection of rent and payment of senior loan facility.

The Group has committed term loan facilities which are secured on the assets and future revenues of the Group.

The Group's cash flow risk is managed by monitoring cash flow as part of the day-to-day control procedures. The Directors consider cash flow projections to ensure appropriate facilities are available to be drawn as necessary.

Future developments

The Directors of the Company are not aware of any circumstances by which the principal activity of the Company would alter or cease.

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

Disclosure of information to auditors

Each of the persons who are directors at the time when this Directors' Report is approved has confirmed that:

- so far as that director is aware, there is no relevant audit information of which the Company and the Group's auditors are unaware, and
- that director has taken all the steps that ought to have been taken as a director in order to be aware of any relevant audit information and to establish that the Company and the Group's auditors are aware of that information.

Auditors

The auditors, Grant Thornton UK LLP, will be proposed for reappointment in accordance with section 485 of the Companies Act 2006.

This report was approved by the board and signed on its behalf.

P Sheldrake
Director

Date: 7 June 2016

DIRECTORS' RESPONSIBILITIES STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2015

The directors are responsible for preparing the Group Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland'. Under Company law the directors must not approve the financial statements unless they are satisfied that they give give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies for the Group financial statements and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ULIVING@ESSEX HOLDCO LIMITED

We have audited the financial statements of ULiving@Essex Holdco Limited for the year ended 31 December 2015, which comprise the Group Statement of Comprehensive Income, the Group and Company Statements of Financial Position, the Group Statement of Cash Flows, the Group and Company Statement of Changes in Equity and the related notes. The financial reporting framework that has been applied in their preparation is applicable law including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland'.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an Auditors' Report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Financial Reporting Council's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Group's and the parent Company's affairs as at 31 December 2015 and of the Group's profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Group Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements and the directors' report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent Company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF ULIVING@ESSEX HOLDCO LIMITED

Richard Hagley

Richard Hagley (Senior Statutory Auditor)

for and on behalf of
Grant Thornton UK LLP

Statutory Auditor
Chartered Accountants

Grant Thornton House
Melton Street
Euston Square
London
NW1 2EP

7 June 2016

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2015

	Note	2015 £000	*2014* *£000*
Turnover	3	**7,583**	*7,284*
Cost of sales		**(2,180)**	*(2,442)*
Gross profit		**5,403**	*4,842*
Administrative expenses		**(1,356)**	*(1,350)*
Operating profit	4	**4,047**	*3,492*
Interest receivable and similar income	6	**1**	*2*
Interest payable and expenses	7	**(3,924)**	*(4,224)*
Profit/(loss) on ordinary activities before tax		**124**	*(730)*
Profit/(loss) for the year		**124**	*(730)*
Other comprehensive income for the year			
Total comprehensive income for the year		**124**	*(730)*
Profit for the year attributable to:			
Owners of the parent company		**(124)**	*730*
		(124)	*730*

The notes on pages pages 16 to 27 form part of these financial statements.

There were no recognised gains and losses other than those included in the consolidated statement of comprehensive income.

The consolidated statement of comprehensive income has been prepared on the basis that all operations are continuing operations.

The company has taken advantage of Section 408 of the Companies Act 2006 not to publish its own statement of comprehensive income.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2015

	Note		2015 £000		2014 £000
Fixed assets					
Tangible assets	10		**61,616**		*62,972*
			61,616		*62,972*
Current assets					
Debtors: amounts falling due within one year	12	**759**		*1,908*	
Cash at bank and in hand	13	**2,266**		*1,942*	
		3,025		*3,850*	
Creditors: amounts falling due within one year	14	**(2,467)**		*(3,763)*	
Net current assets			**558**		*87*
Total assets less current liabilities			**62,174**		*63,059*
Creditors: amounts falling due after more than one year	15		**(62,939)**		*(63,948)*
Net liabilities			**(765)**		*(889)*
Capital and reserves					
Called up share capital	18		**15**		*15*
Profit and loss account			**(780)**		*(904)*
			(765)		*(889)*

The financial statements were approved and authorised for issue by the board and were signed on its behalf by:

P Sheldrake
Director

Date: 7 June 2016

The notes on pages 16 to 27 form part of these financial statements.

COMPANY STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2015

	Note	2015 £000	*2014 £000*
Fixed assets			
Investments	11	**15**	*15*
		15	*15*
Total assets less current liabilities		**15**	*15*
Net assets excluding pension asset		**15**	*15*
Net assets		**15**	*15*
Capital and reserves			
Called up share capital	18	**15**	*15*
		15	*15*

The financial statements were approved and authorised for issue by the board and were signed on its behalf on 7 June 2016.

P Sheldrake
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2015

	Share capital	Retained earnings	Total equity
	£000	£000	£000
At 1 January 2015	15	(904)	(889)
Comprehensive income for the year			
Profit for the year	-	124	124
At 31 December 2015	15	(780)	(765)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2014

	Share capital	Retained earnings	Total equity
	£000	£000	£000
At 1 January 2014	15	(174)	(159)
Comprehensive income for the year			
Loss for the year	-	(730)	(730)
At 31 December 2014	15	(904)	(889)

The notes on pages 16 to 27 form part of these financial statements.

COMPANY STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2015

	Share capital	Total equity
	£000	£000
At 1 January 2015	15	15
Other comprehensive income for the year	-	-
Total comprehensive income for the year	-	-
Total transactions with owners	-	-
At 31 December 2015	15	15

COMPANY STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2014

	Share capital	Total equity
	£000	£000
At 1 January 2014	15	15
Other comprehensive income for the year	-	-
Total comprehensive income for the year	-	-
Total transactions with owners	-	-
At 31 December 2014	15	15

The notes on pages 16 to 27 form part of these financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2015

	2015 £000	*2014 £000*
Cash flows from operating activities		
Profit/(loss) for the financial year	**124**	*(730)*
Adjustments for:		
Amortisation of debt issue costs	**28**	*29*
Depreciation of tangible assets	**1,356**	*1,350*
Interest paid	**3,924**	*4,224*
Interest received	**(1)**	*(2)*
Increase in debtors	**1,148**	*778*
(Decrease)/increase in creditors	**(1,379)**	*221*
Net cash generated from operating activities	**5,200**	*5,870*
Cash flows from investing activities		
Purchase of tangible fixed assets	**-**	*(338)*
Interest received	**1**	*2*
Net cash from investing activities	**1**	*(336)*
Cash flows from financing activities		
Repayment of loans	**(810)**	*(780)*
Loans from group companies repaid	**(143)**	*(73)*
Interest paid	**(3,924)**	*(4,224)*
Net cash used in financing activities	**(4,877)**	*(5,077)*
Net increase in cash and cash equivalents	**324**	*457*
Cash and cash equivalents at beginning of year	**1,942**	*1,485*
Cash and cash equivalents at the end of year	**2,266**	*1,942*
Cash and cash equivalents at the end of year comprise:		
Cash at bank and in hand	**2,266**	*1,942*
	2,266	*1,942*

1. Accounting policies

1.1 Basis of preparation of financial statements

The financial statements have been prepared under the historical cost convention and in accordance with Financial Reporting Standard 102, the Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland and the Companies Act 2006.

The preparation of financial statements in compliance with FRS 102 requires the use of certain critical accounting estimates. It also requires Group management to exercise judgment in applying the Company's accounting policies (see note 2).

The Company is registered in England and Wales under the Companies Act 2006.

The presentational currency is sterling (£).

The following principal accounting policies have been applied:

1.2 Basis of consolidation

The consolidated financial statements present the results of Group and its own subsidiaries ("the Group") as they formed a single entity. Intercompany transactions and balances between group companies are therefore eliminated in full.

The consolidated financial statements incorporate the results of business combinations using the purchase method. In the Statement of Financial Position, the acquiree's identifiable assets, liabilities and contingent liabilities are initially recognised at their fair values at the acquisition date. The results of acquired operations are included in the Consolidated Statement of Comprehensive Income from the date on which control is obtained. They are deconsolidated from the date control ceases.

In accordance with the transitional exemption available in FRS 102, the group has chosen not to retrospectively apply the standard to business combinations that occurred before the date of transition to FRS 102, being 01 January 2014. Therefore, the Group continues to recognise a merger reserve which arose on a past business combination that was accounted for as a merger in accordance with UK GAAP as applied at that time.

1.3 Going concern

The directors have, at the time of approving the financial statements, a reasonable expectation that the Group and Company have adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the financial statements. Further details are contained in the Directors' Report.

1.4 Revenue

Turnover represents income received in the ordinary course of business for services provided and excludes value added tax.

Revenue is recognised on a straight-line basis over the term of the relevant lease.

1. Accounting policies (continued)

1.5 Tangible fixed assets

The property achieved practical completion in September 2013 and is being carried at cost, which includes professional fees and borrowing costs capitalised in accordance with the Company's accounting policy. Depreciation commenced in September 2013 with a full month charge in that month.

Land and buildings are stated at cost, net of depreciation and any provision for impairment. Depreciation is provided on tangible fixed assets, except freehold land, at rates calculated to write off the cost, less estimated residual value, on a straight-line basis over their expected useful lives.

Depreciation is provided on the following basis:

Freehold property	- 50 years
Capitalised fees	- 10 years

Residual value is £nil as the head lease passes back to the University for a nominal value £1 at the end of the concession. No depreciation was provided during construction.

1.6 Valuation of investments

Investments in subsidiaries are measured at cost less accumulated impairment. Where merger relief is applicable, the cost of the investment in a subsidiary undertaking is measured at the nominal value of the shares issued together with the fair value of any additional consideration paid.

Investments in unlisted Group shares, whose market value can be reliably determined, are remeasured to market value at each balance sheet date. Gains and losses on remeasurement are recognised in the Consolidated Income Statement for the period. Where market value cannot be reliably determined, such investments are stated at historic cost less impairment.

Investments in listed company shares are remeasured to market value at each Statement of Financial Position date. Gains and losses on remeasurement are recognised in profit or loss for the period.

1.7 Debtors

Short term debtors are measured at transaction price, less any impairment. Loans receivable are measured initially at fair value, net of transaction costs, and are measured subsequently at amortised cost using the effective interest method, less any impairment.

1.8 Cash and cash equivalents

Cash is represented by cash in hand and deposits with financial institutions repayable without penalty on notice of not more than 24 hours. Cash equivalents are highly liquid investments that mature in no more than three months from the date of acquisition and that are readily convertible to known amounts of cash with insignificant risk of change in value.

1. Accounting policies (continued)

1.9 Financial instruments

Financial assets and financial liabilities are recognised in the Group's balance sheet when the Company becomes a party to the contractual provisions of the instrument. The Group has not classified any of its financial assets as held to maturity or available-for-sale.

Financial assets

All financial assets are recognised and derecognised on a trade date where the purchase or sale of a financial asset is under a contract whose terms require delivery of the financial asset within the time frame established by the market concerned, and are initially measured at fair value.

Loans and receivables

These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise principally through the provision of goods and services to customers (trade receivables) under PFI contracts but also incorporate other types of contractual monetary asset. They are carried at cost less any provision for impairment.

Impairment of financial asset

Impairment of financial assets relates to trade receivables. They are assessed for indicators of impairment at each balance sheet date. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire or when it transfers the financial asset and substantially all the risk and rewards of ownership of the asset to another entity.

Financial liabilities and equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

An Equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recognised at the proceeds received.

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

1. Accounting policies (continued)

1.10 Creditors

Short term creditors are measured at the transaction price. Other financial liabilities, including bank loans, are measured initially at fair value, net of transaction costs, and are measured subsequently at amortised cost using the effective interest method.

1.11 Finance costs

Upfront finance costs of procuring senior debt facilities are capitalised during construction and subsequently amortized over the life of the relevant loans and charged to the profit and loss account. Arrangement fees for these facilities have been capitalised against the cost of the loan.

Finance costs that are directly attributable to the cost of construction of the fixed assets are capitalised as part of the cost of those assets. The commencement of capitalisation begins when both finance costs and expenditure for the assets are being incurred and activities that are necessary to get the assets ready for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to get the assets ready for use are complete.

1.12 Taxation

Current and deferred tax, including UK corporation tax, is provided at amounts expected to be paid using the tax rates and laws that have been enacted or subsequently enacted by the balance sheet date.

Deferred tax assets and liabilities are recognised where the carrying amount of an asset or liability in the balance sheet differs from its tax base, except for differences arising on the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting, nor taxable profit.

Recognition of deferred tax assets is restricted to those instances where it is probable that taxable profit will be available against which the differences can be utilised.

The amount of the asset or liability is determined using tax rates that have been enacted or substantively enacted by the reporting date and are expected to apply when the deferred tax assets are recovered.

Deferred tax assets and liabilities are offset when the Company has a legally enforceable right to offset current tax assets and liabilities and the deferred tax assets and liabilities relate to taxes levied by the same tax authority on the same taxable company.

2. Judgments in applying accounting policies and key sources of estimation uncertainty

The estimates and judgements that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the financial year are as follows:

Classification of asset

The Group has entered into a Project Agreement with the University of Essex as well as a lease and leaseback arrangement for two sites upon which student accommodation has been built. The Project Agreement governs the relationship between the University and the Group including terms of use of the University brand in marketing material, the general actions of the Group and University as landlord and operator. Management consider that as the Group takes full occupancy and demand risk associated with the provision of the accommodation, that the building will be fully depreciated during the concession and therefore full value of these assets will be exhausted during the concession, and that the Group has the ability to exercise control over the user of the asset, then the Group should account for the asset of the concession on its balance sheet.

Capitalisation of costs

During the period of construction, all costs incurred as a direct result of financing, designing and constructing the student accommodation, including finance costs, have been capitalised. The directors consider this to be appropriate since the risks and rewards of ownership rest with the Group.

3. Analysis of turnover

An analysis of turnover by class of business is as follows:

	2015	*2014*
	£000	*£000*
Rental income	**7,555**	*7,255*
Third party revenue	**23**	*29*
Pass through revenue	**5**	-
	7,583	*7,284*

	2015	*2014*
	£000	*£000*
United Kingdom	**7,583**	*7,284*
	7,583	*7,284*

4. Operating profit

The operating profit is stated after charging:

	2015 £000	*2014 £000*
Depreciation of tangible fixed assets	1,356	*1,350*
Fees payable to the Group's auditor and its associates for the audit of the company's annual accounts	9	*9*

5. Directors' remuneration

No staff were directly employed by the company. Services provided by the contractors include the provision of staff and management to perform contractual responsibilities. Costs associated with the staff and management are included within the contractors service charge.

6. Interest receivable

	2015 £000	*2014 £000*
Bank interest receivable	1	*2*
	1	*2*

7. Interest payable and similar charges

	2015 £000	*2014 £000*
Bank interest payable	2,616	*2,660*
Other loan interest payable	11	*11*
Loans from group undertakings	1,297	*1,553*
	3,924	*4,224*

8. Taxation

	2015 **£000**	*2014* *£000*
Total current tax	-	-
Deferred tax		
Total deferred tax	-	-
Taxation on profit on ordinary activities	-	-

Factors affecting tax charge for the year

The tax assessed for the year is lower than *(2014 - higher than)* the standard rate of corporation tax in the UK of 20.25% *(2014 - 21.5%)*. The differences are explained below:

	2015 **£000**	*2014* *£000*
Profit on ordinary activities before tax	**124**	*(730)*
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 20.25% (2014 - 21.5%)	**25**	*(153)*
Effects of:		
Utilisation of tax losses	**(25)**	*(184)*
Non-taxable income	-	*337*
Total tax charge for the year	-	-

Factors that may affect future tax charges

There were no factors that may affect future tax charges.

A deferred tax asset of £150k has not been recognised due to the uncertainty in respect of future profits. The maximum tax losses potentially available to the Group are £833k.

9. Parent Company Profit for the year

The Company has taken advantage of the exemption allowed under section 408 of the Companies Act 2006 and has not presented its own Statement of Comprehensive Income in these financial statements. The profit after tax of the parent Company for the year was £Nil thousand *(2014 - £Nil)*.

10. Tangible fixed assets

Group

	Land and buildings £000
Cost or valuation	
At 1 January 2015	64,769
At 31 December 2015	64,769
Depreciation	
At 1 January 2015	1,797
Charge for the period	1,356
At 31 December 2015	3,153
Net book value	
At 31 December 2015	61,616
At 31 December 2014	*62,972*

The land and buildings are carried at cost and are now completed. All construction costs were capitalised and are included in this value. Depreciation commenced September 2013 with a full month charge in that month. Interest and fees capitalised as at balance sheet date 31 December 2015 are £3,242k (2014: £3,449k). Accumulated depreciation of capitalised interest and fees as at the 31 December 2015 is £315k (2014: £180k).

11. Fixed asset investments

Subsidiary undertakings

The following were subsidiary undertakings of the Company:

Name	Country of incorporation	Class of shares	Holding	Principal activity
Uliving@Essex Limited	England & Wales	Ordinary	100 %	Design, build and management of student accommodation

11. Fixed asset investments (continued)

Company

	Investments in subsidiary companies £000
Cost or valuation	
At 1 January 2015	**15**
At 31 December 2015	**15**
At 31 December 2015	-
Net book value	
At 31 December 2015	**15**
At 31 December 2014	*15*

12. Debtors

	Group 2015 £000	*Group 2014 £000*	Company 2015 £000	*Company 2014 £000*
Trade debtors	**18**	*1,879*	-	-
Other debtors	**70**	-	-	-
Prepayments and accrued income	**671**	*29*	-	-
	759	*1,908*	-	-

13. Cash and cash equivalents

	Group 2015 £000	*Group 2014 £000*	Company 2015 £000	*Company 2014 £000*
Cash at bank and in hand	**2,266**	*1,942*	-	-
	2,266	*1,942*	-	-

14. Creditors: Amounts falling due within one year

	Group 2015 £000	*Group 2014 £000*	Company 2015 £000	*Company 2014 £000*
Bank loans	**801**	*810*	-	-
Trade creditors	**218**	*408*	-	-
Amounts owed to group undertakings	**236**	*142*	-	-
Accruals and deferred income	**1,212**	*2,403*	-	-
	2,467	*3,763*	-	-

15. Creditors: Amounts falling due after more than one year

	Group 2015 £000	*Group 2014 £000*	Company 2015 £000	*Company 2014 £000*
Bank loans	**49,419**	*50,220*	-	-
Unamortised debt issue costs	**(558)**	*(586)*	-	-
Amounts owed to group undertakings	**14,078**	*14,314*	-	-
	62,939	*63,948*	-	-

Secured loans

Bank borrowings relate to a £52,000,000 loan facility. The term of the loan is 35 years.

As at 31 December 2015 borrowings totalling £50,220,000 (2014: £51,030,000) were outstanding under the facility. Borrowings under this facility are repayable in quarterly instalments commencing November 2013 and ending July 2047.

Interest on amounts drawn is charged at a rate of 5.11%.

The loan facility is secured by fixed and floating charges on the assets of the Group.

Shareholder loans

Subordinate loans constitute unsecured debt issued under the Investment Deed. The total sum available under the Investment Deed is £14,530,334 which matures in 2063. The amounts drawn are repayable in quarterly instalments commencing Feb 2014

Shareholder loan notes carried an interest rate of 10.5% to 31st August 2013, 7.01% from 1st September 2013 to 31st August 2022, 8.5% from 1st September 2022 to 31st August 2032 and 9.5% thereafter plus a variable element of interest based on annual changes in RPI.

16. Loans

	Group 2015 £000	*Group 2014 £000*	Company 2015 £000	*Company 2014 £000*
Amounts falling due within one year				
Bank loans	**801**	*810*	-	-
	801	*810*	-	-
Bank loans	**600**	*801*	-	-
	600	*801*	-	-
Bank loans	**2,117**	*2,002*	-	-
	2,117	*2,002*	-	-
Bank loans	**46,702**	*47,417*	-	-
Debenture loans	**(558)**	*(586)*	-	-
	46,144	*46,831*	-	-

17. Financial instruments

	Group 2015 £000	*Group 2014 £000*
Financial assets measured at amortised cost	**2,284**	*3,821*
	2,284	*3,821*
Financial liabilities measured at amortised cost	**(65,895)**	*(67,047)*
	(65,895)	*(67,047)*

Financial assets measured at amortised cost comprise cash at bank and in hand and trade debtors.

Financial Liabilities measured at amortised cost comprise bank loans, group loans, trade creditors, accruals and other creditors.

18. Share capital

	2015	*2014*
	£000	*£000*
Authorised, allotted, called up and fully paid		
15,000 Ordinary shares of £1 each	**15**	*15*

19. Related party transactions

Equitix Education 2 Limited and Centro Place Investments Limited are considered to be related parties due to their shareholding in Uliving@Essex Holdco Limited. Transactions with these related parties relate to interest expense on shareholder loans and accrued interest and outstanding loan balances held at the year end. The Directors consider the material transactions undertaken by the Group during the year with related parties to be as follows:

	2015 Interest £000	**2015 Creditor £000**	**2014 Interest £000**	**2014 Creditor £000**
Equitix Education 2 Limited	**1,043**	**12,714**	**1,242**	**12,114**
Centro Place Investments Limited	**194**	**2,244**	**233**	**2,271**

20. Controlling party

In the directors' opinion, there is no ultimate controlling party. The company is controlled by its shareholders under the shareholders agreement:

Equitix Education 2 Limited - 85%
Centro Place Investments Limited - 15%

On 30th November 2015 BY Development Limited sold its remaining 5% shareholding in the Company to Equitix Education 2 Limited.

21. First time adoption of FRS 102

The policies applied under the entity's previous accounting framework are not materially different to FRS 102 and have not impacted on equity or the statement of comprehensive income.

APPENDIX 8

DEMAND REPORT

Private & Confidential
www.cushmanwakefield.com

University of Essex, The Meadows and The Quays: Refinancing Demand Due Diligence

Prepared on behalf of Uliving

January 2017

Cushman & Wakefield

Job No/Ref: 150LBC00

Contents

Disclaimer and confidentiality clause

Whilst facts have been rigorously checked, Cushman & Wakefield (C&W) can take no responsibility for any damage or loss suffered as a result of any inadvertent inaccuracy within this report. Information contained herein should not, in whole or part, be published, reproduced or referred to without prior C&W approval. Any such reproduction should be credited to C&W. DTZ Debenham Tie Leung remains a trading entity of C&W.

C&W has provided an opinion on the market sustainability of rent levels within the current market climate and for the reasonableness of rent increases going forward. Whilst C&W has provided an opinion on rents and rent increases over the long term, based upon existing and current future demand and supply conditions and the current education policy environment, C&W cannot guarantee these conditions will continue to apply, as we cannot predict or anticipate the actual effects of external regulatory changes, the behaviour of RPI in the future, or the actions or behaviour of others in increasing competition and new supply or in their marketing efforts. Accordingly C&W's opinion regarding future rent increases will inevitably carry more weight in the earlier years of the concession than in later years. Any assessment of the applicability of rent increases in forthcoming years should accordingly be reviewed in light of the contemporary demand and supply conditions, policy environment and student behaviours existing at that time.

Executive Summary

Introduction

1. This report has been commissioned by Uliving to provide demand due diligence services to support the refinancing of the 1,429 en-suite and townhouse rooms at The Meadows and The Quays student accommodation at the University of Essex.

2. This report is addressed to the following Addressees to whom we offer a duty of care and Reliance:

Uliving@Essex Limited
10-11 Charterhouse Square
London EC1M 6EH

Assured Guaranty (Europe) Limited
11th Floor, 6 Bevis Marks,
London, EC3A 7BA

Assured Guaranty Municipal Corp.
1633 Broadway
New York
NY 10019

In its separate capacities as trustee for the holders of the Bonds and as trustee for the Secured Creditors:
BNY Mellon Corporate Trustee Services Limited
1 Canada Square, London, E14 5AL

TradeRisks Limited
21 Great Winchester Street,
London, EC2N 2JA

About the University

3. The University of Essex is a research-intensive university founded in 1963 which received its Royal Charter in 1965. The University has three campuses with the majority of both students and accommodation located at the main campus in Colchester. Its main campus is based close to Colchester in Essex; providing a self-contained true campus environment at the outskirts of the city.

4. The University is among the leading UK institutions in social sciences and describes itself as an academic community, which encourages its members to challenge the status quo and have a positive impact on society both, during and after their time at University. Moreover, the institution prides itself for its international outlook; reflected in its diverse student base as well as internationally focussed research and teaching.

5. The University scored highly in the 2013 Research Excellence Framework (REF) submitting world-leading research ratings in a range of humanities based subjects. The institution is ranked among the top 20 research universities overall, with a top 5 position in social science and a first place in politics research. The University also features within the top half of newspaper league table rankings and achieved, with a rank of 30th in The Times 2017 league table, its highest rank to date. Through its strategic focus on excellence in research and teaching, the University is likely to maintain a strong performance in future.

Background to University Accommodation

6. The University campus is based outside of Colchester (approximately 20 min. by bus and over 30 min. walking to the city centre) and was designed as a university “town” operating as a largely self-contained site. With all academic and social facilities in one place (such as teaching buildings, student accommodation, shops, banks, a gallery and a theatre, bars and cafés, and sports facilities) student life is predominantly centred on the campus and providing a full student experience on

campus is a central strategy of the University. This includes the provision of residences to house more than first year undergraduates, as the University recognises that living on campus is attractive to international students (currently guaranteed accommodation in all years of study) as well as non-guaranteed returners from UK and EU backgrounds.

7. Campus institutions are attractive to students at this time as they wish to become fully immersed in their studies and the student experience, as highlighted by the predominance of campus based institutions in the top 30 of the Times Higher Student Experience Survey. High levels of satisfaction are being achieved in the National Student Survey (NSS). Alongside this the University has significant investment plans for the Colchester campus. The new business school and development of the heart of the campus seek to reinvigorate and extend the estate, whilst growth in student numbers is also leading to significant levels of academic recruitment.

8. In 2016/17, the University offers 4,117 rooms (4,113 lettable) rooms. Several small 1 year arrangements have been utilised by the University to house students in recent years.

9. In 2013, due to the uncertainties created in the applications cycle from the core and margin changes and the increase in rooms from The Meadows I, the University took the decision to open accommodation applications to non-guaranteed returning students. The University experienced a significant increase in demand for accommodation from returners as a result. These occurrences have demonstrated that there is latent demand for accommodation on campus from UK and EU (i.e. non-guaranteed) returning undergraduates.

10. Options to live off campus are limited. There is only one larger private sector student hall to date, The Maltings, which is located at King Edward Quay to the east of the campus. The walking distance between the hall and the campus equals approximately 25 minutes. There are two smaller private schemes to the north west of the campus (about 15 minutes walking distance), however their offer cannot compete with the quality and location of existing and proposed The Meadows schemes, nor do they partner long-term with the University. There is currently only one planning application for a 230 bed scheme from Victoria Hall in the development pipeline for Colchester. Students therefore are reliant upon the HMO housing market for accommodation, where the University is relatively dislocated from the amenities of the town.

The Meadows and The Quays

11. The accommodation consists of 649 new (in 2013/14) en-suite and townhouse rooms at The Meadows and 780 rooms at the Quays of stock transferred accommodation, constructed in 2003 and refurbished for 2013/14.

12. The two schemes are located on the North West edge of the Colchester campus, approximately a 10 to 15 minute walk to the centre of the campus. Whilst close on a map the two properties are separated by a railway line. There is a foot bridge which provides students with pedestrian access over the tracks and directly to the university campus.

The Meadows Student Accommodation

13. Rents range from £123.69 per week at The Quays for an en-suite room to £151.89 for a double en-suite flat with the majority of rooms priced under £141 per week in 2016/17. Students are given the option of let lengths of either 39 or 50 weeks. 39 weeks is a favourable term given the majority of the newer en-suite accommodation in the UK would be offered at 42 weeks, making the annual pricing of a room at University of Essex more affordable than many new options around the UK.

Student to Bed Ratios

14. The University projects the full-time student body at Colchester to grow to just over 15,485 students by 2020/21 from 11,790 in 2016/17 (based on University forecast). This is a CAGR of 7%.

15. Using forecast student numbers provided by the University, combined with HESA data, C&W derived the demand for university accommodation over time. The demand pool has been calculated by removing all students domiciled in Essex and some students from surrounding counties, who may not wish to live on campus due to the proximity of their homes to the University, as well as excluding partner colleges and other campuses than Colchester. A Student:Bed ratio (SBR) for the Colchester campus is calculated using the demand pool and the number of beds offered by the University (owned and nominated) in any given year. The 2014/15 SBR as a baseline is measured as 1.8:1. With the first circa 643 beds delivered by 2018, and due to the University's actual and projected growth, the SBR moves to 2.5:1. The sensitivity test of a 10% shortfall in the demand pool in 2018 leads to an SBR of 2.3, which is strong overall and compared to other campus based institutions, and therefore acceptable to C&W.

16. There is a Restrictive Covenant (RC) in place on phase 1 of The Meadows accommodation (see section 5). The applicable test uses C&W's methodology for student demand based on HESA metrics (as per on campus SBR calculation outlined above). Supply of accommodation includes University owned beds and one off campus residence in the form of The Maltings, which is utilised by the Student Union and could be considered comparable accommodation. Normally C&W would not include such a residence as the University has influence over where its students reside to a large extent, and this favours accommodation on campus. However, due to the PA and the wishes of the Addressees of this Report, The Maltings has been included in the definition of Total Bed Supply.

17. Under these calculations and during all stages of the forecast, and based on the evidence provided under the PA methodology for supply, C&W has concluded that the Students:Bed ratio does not breach the restrictive covenant threshold of 1.5:1.

Conclusions

18. Anticipating intensified recruitment activity and rising student numbers in forthcoming years, the University foresees a shortage of accommodation on campus for its guaranteed and prioritised student groups (1^{st} year students offered a guarantee and returning non-EU internationals).

19. Due to the self-contained nature of the University's campus, relative lack of competition and pressure on the housing market, C&W believes that developing additional housing on-campus to meet first year accommodation guarantees and for a proportion of returning students is a well-founded strategy. Other campus based institutions such as Lancaster and Kent pursue similar strategies due to their locations/dislocation from the market and ability to maintain a self-contained residential campus. The accommodation is intended for those students who are offered a guarantee of accommodation, but we understand that there is also continuing demand from UK/EU returning students who also express a desire to lie on the campus beyond the first year.

Risk Matrix

20. The following risk matrix highlights the main issues that funder and investors should be aware of in investing in The Meadows and The Quays.

Risk Matrix

Risk Issue	Remarks	Factors that may address the risk	Risk to Funders
National risks			
Tuition fees and policy changes	Tuition fees at the University of Essex are £9,000, in line with the majority of institutions. Although student behaviour has been positively affected to date, with students aiming for higher quality institutions, the longer term effects of this policy upon affordability of higher education are not known. In 2015 HEFCE Student Number Controls were further extended, allowing successful universities to recruit more students within an overall expansion of places in the higher education system. However, strong universities stand to benefit more and there may be greater fluctuations in recruitment due to competitive factors each year. The Higher Education and Research Bill will seek to allow HEIs to increase fees in line with inflation. It is not yet clear how strong an impact tuition fee increases at undergraduate level will affect demand from UK student for postgraduate education.	The quality of students at the University is high and the University is reacting positively to changes across the sector in its strategies. Recruitment has been strong and the strategies in place – brand, curriculum and investment – stand the University in good stead. The national and international character of its students leads to strong demand for student accommodation.	Low
International student arrangements in the UK	Non-EU students have been subject to restrictions since 2012, when they were no longer able to work for 20 hours a week whilst studying (they have no rights to work) or to remain in the UK for 2 years on graduation as they used to under the previous rules. Students have to obtain a visa in order to remain in the UK to work now, which has to be sponsored by an employer. The change to work experience rules may deter some international students, such as many Indian students, from studying in the UK (who valued the opportunity to work following their degree).	Legislation is being considered to allow those students, who are talented in STEM subjects to remain. The University continues to attract a large number and proportion of students from non-EU domiciles. Moreover, EU student numbers have seen significant growth from 2008 onwards; providing the University with a diversified student base.	Low
Risk Issue	**Remarks**	**Factors that may address the risk**	**Risk to Funders**
Brexit impacts on higher education	The impacts of Brexit may be wide ranging affecting recruitment of non UK students from all domiciles. Long term it is too early to say how these impacts will affect demand for high quality universities. Short term the impacts can be seen in a number of main events, such as the perception that UK is unwelcoming to foreign nationals, mitigated by the weakening of the pound against major currencies. Some visa trials to allow students to remain to work after graduation are currently underway, which again may pilot opportunities to widen the appeal of UK HE in future if they are	Longer term we await further news Short term, UCAS undergraduate statistics (end of June 2016) reported the number of EU applicants rose by 6% (+2,920) to 51,850. The number of applicants from outside the EU decreased by 2% (-1,230) to 69,300. The University of Essex, along with many of the higher quality UK institutions remains comfortable with its competitive position and with its outlook with regard to non UK student recruitment.	A watching brief, but short term signs are that the sector is stable.

	widened out. Further impacts on access to European research grants is a potential risk to research competitiveness.		
Project specific risks			
Off campus competition for returning students.	In developing accommodation for returning students one of the key potential risks to the funder is how to protect the accommodation in the event of a material reduction in supply or increase in choice of rooms for (in particular) returning students. Currently there are few blocks in Colchester, however in order for sustained demand from returning students to be maintained it would be desirable to go beyond just an RC, and to develop relationships with the Council to discourage speculative development, and only those who are working with the University. This would extend the influence of the institution in managing the volume and quality of rooms available to its students in the town.	C&W to understand the relationships between the University and the Council, and whether the University's plans are reflected in the local plan. Having a choice of accommodation, price points and group bookings will mitigate some of the risk.	Low

1.0 Introduction

Objectives of the Report

1.1 This market due diligence report is created in relation to the envisaged first development phase by Uliving of The Meadows and the Quays at the University of Essex. The report focuses on:

- The University's overall strategy and attractiveness, particularly where it impacts on estates and student residential accommodation;
- The nature of the student population;
- The existing University accommodation, the competitive supply context, examining supply of student residential accommodation on and off campus (current and future known);
- Operations and marketing of accommodation by the University, as well as the restrictive covenant.

1.2 The report contains an assessment of the demand environment for bed spaces in phases on campus in light of market conditions, as well as University strategy and operations.

1.3 This report is addressed to the following Addressees to whom we offer a duty of care and Reliance:

Uliving@Essex Limited
10-11 Charterhouse Square
London EC1M 6EH

Assured Guaranty (Europe) Limited
11th Floor, 6 Bevis Marks,
London, EC3A 7BA

Assured Guaranty Municipal Corp.
1633 Broadway
New York
NY 10019

In its separate capacities as trustee for the holders of the Bonds and as trustee for the Secured Creditors:
BNY Mellon Corporate Trustee Services Limited
1 Canada Square, London, E14 5AL

TradeRisks Limited
21 Great Winchester Street, London,
EC2N 2JA

Overview of the Project

1.4 The accommodation consists of 649 new (in 2013/14) en-suite and townhouse rooms at The Meadows and 780 rooms at the Quays of stock transferred accommodation. The Meadows is made up of 19 town houses for 228 students, plus en-suite cluster flats for a further 420 students and one 1 bed flat. The Quays is a primarily en-suite scheme with a small number of premium en-suite and double rooms build originally in 2003, and refurbished for 2013/14. The project is designed to meet existing demand for on campus bed spaces from guaranteed and prioritised student groups. In addition, the University experienced increasing demand from returning students, which may further evolve given the availability of modern accommodation on campus.

1.5 Rents range from £123.69 per week at The Quays for an en-suite room to £151.89 for a double en-suite flat with the majority of rooms priced under £141 per week in 2016/16. Students are given the option of let lengths of either 39 or 50 weeks. 39 weeks is a favourable term given the majority of the newer en-suite accommodation in the UK would be offered at 42 weeks, making the annual pricing of a room at University of Essex more affordable than many new options around the UK.

1.6 Further details can be found in Section 6 of this report.

2.0 University Strategy

About the University of Essex

2.1 The University of Essex is a public research university situated in the East of England. It was founded in 1963 and received its Royal Charter in 1965. In 2014/15, 12,185 full-time students were based across three campuses:

- Colchester Campus is the main campus of the University. According to HESA data, the Colchester campus represents around 88% of the University's full-time student population. It lies two miles from Colchester and is home to 16 academic department and schools. Despite its rather rural location, the campus is well connected to London and Stansted Airport, both can be reached within 1.5 hours by public transport.

- Southend Campus was opened in 2007 and is located in the city of Southend-on-Sea, 1.5 hours from London by public transport. Courses are offered by four departments; i.e. Essex Business School, the School of Health and Human Sciences (incorporating the Centre for Social Work), East 15 Acting School and the Centre for Psychoanalytic Studies.

- The third site is Loughton Campus, which lies approximately 14.5 miles to the northeast of London. It is home to the East 15 Acting School and houses state-of-the-art studios, technical equipment and theatre space; such as Unit Four, a £1.5million facility for the Stage and Production Management course.

2.2 The University of Essex is a leading UK university in social sciences and humanities, achieving high scores in the Research Excellence Framework 2014. In 2013, the institution was awarded a Regius Professorship in Political Science by Her Majesty The Queen.

2.3 The University is regularly ranked among the top 30-60 universities across various league tables. Moreover, the institution has been awarded the 2013 Times Higher Education Award for Outstanding Support for Students for their placement scheme Frontrunners, which allows students to improve their skills and employability through paid placements.

2.4 In 2015 the institution also won the 'Best Advancing Staff Equality' initiative at the Guardian University Awards for the Essex lesbian, gay, bisexual and transgender (LGBT) alliance; the first network of its kind in the county.

Mission and Values

2.5 The University of Essex states “Our mission [is] to contribute to society through excellence in education and excellence in research.”

2.6 In pursuance of this mission, the following nine core values underpin the University’s actions and decision-making processes:

Excellence

- Excellence in education and research are seen as equally important priorities.

Academic freedom

- Academic freedom in testing traditional views and creating new ideas.

Integrity

- Integrity by means of openness, honesty and ethical behaviour.

Community

- Strengthening the community of students, staff and alumni to develop and disseminate knowledge creating cultural, economic and social value nationally and internationally; as well as to allow individuals to fulfil their potential.

Inclusivity

- Promoting inclusivity to sustain a diverse community, which ensures equal opportunities for its members, and promotes respect and dignity at all times.

Innovation

- Supporting innovation by means of harnessing creativity to deliver excellence in education and research and address the needs of a changing world.

Global outlook

- Pursuing a global outlook through international collaborations and co-operations both, on an institutional and individual level.

Partnerships

- Developing partnerships on a regional, national and international level with individuals, groups and institutions, which are based on trust and respect, and are of mutual benefit to both parties.

Accountability

- Enhancing accountability by means of anchoring decision-making responsibilities at the lowest appropriate organisational level; as well as ensuring transparency.

Strategic Plan 2013-2019

2.7 The University's Strategic Plan 2013-2019 sets out strategic actions and priorities in support of the institution's mission:

- **Student recruitment** based on potential and merit, irrespective of socio-economic background.
- Provision of **intellectually stimulating and challenging study programmes** to produce active citizens, who contribute to the development of society.
- Commitment to **research-led education** to allow students to develop intellectual independence, critical thinking and a thirst for knowledge.
- Provision of skills development to enhance **employability and entrepreneurship**.
- Provision of **internationalised educational opportunities** to foster global engagement and intercultural awareness among graduates.
- Promotion of **participation in arts, culture, sports and volunteering** as well as provision of placement and academic exchange opportunities.
- Support for and retention of **committed academic and professional staff**, recognizing and awarding achievement of excellence in education. This links to the establishment of a formal performance assessment mechanism to evaluate staff.

Excellence in Education

- **Maximising research quality and intensity** across a broad range of University specialisms with selective investment in academic areas of excellence to enhance the research profile nationally and internationally.
- Ensuring **impact-oriented knowledge exchange** with the non-academic world.
- Foster **research-business collaborations** of projects with potentially societal and/or commercial impact.
- Establishing a **clear vision for the Knowledge Gateway Research Campus** to enhance research impact and the development of research partnerships.
- **Increasing the volume and diversifying the sources of research funding**. This links to the creation of a Research Capital Infrastructure and Equipment Fund as well as a Research Seedcorn Fund.
- **Engaging with key national and international bodies** responsible for setting research agendas and allocating research funding.
- **Decreasing reliance on external funding** for University Research Centres and Doctoral Training Centres.
- Support for and retention of **committed academic staff**, recognizing and awarding achievement of excellence in research. This links to the establishment of a formal performance assessment mechanism.

Excellence in Research

2.8 In addition, support activities are aligned to the attainment of excellence in education and research through the development of estate, plant and equipment in accordance with strategic requirements and suitability of University spaces.

2.9 The University has taken care to differentiate itself in the marketplace, creating a distinctive "challenger" identity which appeals to enquiring minds who want to challenge the status quo. This is summed up by the back page of the Undergraduate prospectus which is included at Appendix A of this report, and also in the preface by Shami Chakrabati the University's Chancellor (since 2014) in the same document. At a time in higher education where having a distinct identity is a competitive advantage, these demonstrations of a clear brand set this university apart. Alongside ongoing curriculum review and significant investment in the development of the campus, the University is playing to its strengths and preparing for a more competitive landscape.

Competitive Position and Aspirations

2.10 There are a number of developments which the University is working on which are likely to put the University in a strong competitive position for the future.

- Aspiration to move up The Times Good University Guide league table to 25th within the period of the current Strategic Plan (3 years) from 30th. The University is confident that this can be achieved and that some of the steps to achieving this have already been taken.

Increasing the number of students with good degrees by 159 more than currently (within a graduating population of 4,000) will give a boost to the metric that contributes to the league table ranking. The University also believes it will be in the top 25 universities for graduate jobs and further study if just 87 more students find graduate level employment. These are particular measures which had been identified alongside the continuing spend on education and infrastructure which are also underway.

- Teaching Excellence Framework: the TEF is being developed as a metric against which universities will be measured in future, as well as research through the Research Excellence Framework. Essex is very well positioned on these new metrics, as shown in Appendix D, and this will stand the University in good stead as and when the TEF is incorporated into league tables and becomes part of student decision making. The University has received preliminary information on how the TEF will be measured (which is a gold, silver, bronze scale), and believe that they are within the gold banding, which is likely to contain circa 20 of 160 HEIs.
- Employability: linking to the above metrics, the University has invested significantly in ways that students are engaging with employability issues throughout their time at the University. Every department has a Director of Employability and Employability Officers within the faculties. The Employability and Careers centre co-ordinates the work, and a stepping stone programme is in place to help graduates find work. Every degree programme has an embedded module on employability, and a placement or study abroad year which does not attract a tuition fee (at most universities it does).
- Retention: initiatives are underway to improve retention, involving students in conversations with the Student Union through the Heirloom Project. At intake, students are encouraged to interact with the SU at an event where they are given information about how to engage with the University, what opportunities there are for social clubs and sporting activities. They are encouraged to be demanding in their interaction with the university, in their academic time and in making the most of their time at university. This first engagement is then followed up periodically through the year. Establishing this level of personal engagement with every student has been seen to increase retention at the University as students feel personally involved and included in a community.
- Curriculum development and growth potential: the University states that there is growth in each discipline, and ongoing “root and branch” review of courses for relevancy and attractiveness. There are growth opportunities identified in many programme areas such as the business school, law, economics, computational science, biological sciences, and the acting school.
- New entry channels for student recruitment: The primary focus for recruitment in future, in order to mitigate some of the risks around Brexit and immigration policy, will be within the UK. New pathways are being created for “Year 0” or foundation year study to take place at the University to encourage progression on to degree level courses. In the first year of operation it is expected that 300 such students will be recruited, and these are outside of the forecasts reported in this document.

Small groups of research intensive apprenticeship programmes are taking place. Also, 32 schools have joined the University's programme to raise attainment, achievement and aspirations.

VI6 is a group of six local schools where there is a very low level of participation in HE. Groups of students are taught at the University's campus one day per week and this is leading to a rise in both interest and participation in Higher Education over time.

Internationally the University will work with an independent pathway provider, and this relationship has been selected through competitive tender and is due for launch in December 2017. The provider will offer "Year 0" programmes preparing students in English language and selected subject areas. Partnerships are also being developed with individual partners in China and some developing countries, which will allow the University to transmit its brand clearly and short-circuit some of the potentially detrimental messages about the UK – allowing for more meaningful recruitment efforts to take place directly between institutions.

- The Knowledge Gateway (explained further below): the University's plan for a contiguous science park on its campus is innovative in that it will interact at every level with the university and its students, rather than be host to new businesses. It is envisaged that it will be a big draw for students who wish to start their own businesses as well as to those who wish to hire them.

Key Estates Developments

2.11 The University has invested in several estates developments across its Colchester and Southend campuses over recent years. The key developments at the Colchester campus are presented in the following.

2.12 The £21 million Silberrad Student Centre for student services opened in summer 2015. It provides all services regarding accommodation, payments, registration and student welfare under one roof. Further facilities include an integrated learning centre for creative and group working; new IT facilities; a state-of-the-art media centre; a 24-hour postgraduate study area; as well as further study and library spaces.

2.13 A £26 million extension to the Albert Sloman Library also opened in summer 2015 and offers 388 new study spaces, a new 24/7 postgraduate reading room as well as a collection of 1.4 million books.

2.14 Essex Business School will move to a new £21m eco-friendly building, which is located next to the Knowledge Gateway research park. The building features contemporary facilities including a lecture theatre, dedicated space for MBA students as well as flexible group learning and ICT spaces.

2.15 The Knowledge Gateway is a science and learning park which will be developed at the northern end of the campus. The development is expected to create circa 2,000 jobs and co-locate businesses and learning in an advanced science park intrinsically linked to the academic life of the University, building on the existing R&D work taking place at Parkside.

2.16 In 2013, The Meadows, a contemporary purpose-built student accommodation scheme, was opened, which is the newest accommodation at the campus.

Summary

2.17 The University follows a strategic approach that encompasses the entirety of its operations. Pursuing excellence in research and education lie at the core of all strategic initiatives, which are supported by streamlined processes and investment in academic and accommodation estates as well as facilities. Given the University's favourable positioning and profile in the social sciences and humanities coupled with its ambition to further extent its impact nationally and internationally, the institution is likely to continue to enhance its reputation and attract increasing numbers of students in future.

3.0 Student Demand

In this section, patterns of student demand and related trends at the University of Essex are analysed. Figures generally relate to the entire institution; i.e. cover all campuses, however, where appropriate, numbers for the Colchester campus are presented separately. The approach therefore allows benchmarking of the university against UK average recruitment levels, whilst illustrating particular circumstances in Colchester where they are different to the whole institution. Colchester makes up 87% of the full time student body at the University:

University full time students by campus, 2016/17

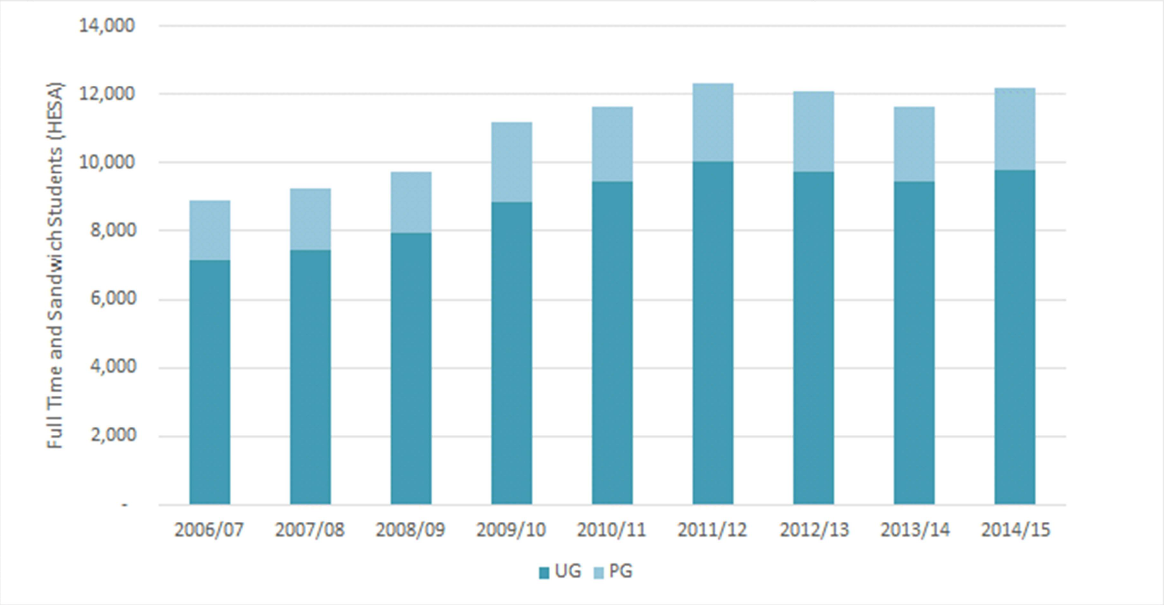
Colchester	Southend	Loughton	Total
11,791	1,244	384	13,419

Source: University of Essex (latest available data)

Mode of Study

3.1 The University attracted 12,185 full-time and sandwich students in 2014/15, which equals 82% of the total student body and is significantly above the UK average full-time proportion of 73%. According to the University's enrolment data, the number of full-time and sandwich students increased to 12,729 in 2015, reflecting year-on-year growth of 4.5%. Overseas student numbers grew particularly fast at a rate of 22%.

Figure 3.1: Full-time and sandwich students over time, University of Essex (all campuses)



Source: HESA Student Population 2006/07 – 2015/16

In 2014/15, there were 10,730 full-time and sandwich students at the Colchester campus, which constituted 88% of the University's total full-time student population and reflects year-on-year growth of 4%.

3.2 Full-time students grew faster than the national average over a 5-year time span (9% vs. 4%). On the contrary, part-time students are underrepresented at the University relative to the national average. Around 15% (2,250 students) study part-time in comparison to the average national proportion of 25%.

Table 3.1: Mode of study

Mode of Study	2014/15			2009/10			Essex	UK
	Student numbers	%	UK Comparator	Student numbers	%	UK Comparator	Growth 2009/10 to 2014/15	Growth 2009/10 to 2014/15
Full-time	12,155	82%	67%	11,130	75%	59%	9%	4%
Part-time	2,250	15%	25%	3,275	22%	34%	-31%	-34%
Sandwich	30	0%	7%	35	0%	5%	-12%	35%
Other	380	3%	2%	425	3%	2%	-10%	6%
Total	14,815	100%	100%	14,860	100%	100%	0%	-8%

Source: HESA 2009/10 to 2014/15

3.3 The Colchester campus mirrors the overall trend in student numbers at the University of Essex with regard to the study mode. The high proportion of full-time students is positive in terms of demand for student accommodation as this group is most likely to require a room and hence represents the main part of the demand pool. The remainder of this section will thus only deal with full-time and sandwich students.

Level of Study

3.4 The proportion of undergraduate and postgraduate students at the University of Essex is similar to the national average. UG level student numbers increased more than twice as fast as the UK average over the five year timespan from 2009 to 2014 (10% at UoEssex compared to 6% national average), while PG level student numbers grew in line with the UK average at 4%. The student population at the Colchester Campus has the same distribution of UG and PG students as the overall institution.

Table 3.2: Level of study

Level of Study	2014/15			2009/10			Essex	UK
FT &SW	Student numbers	%	UK Comparator (%)	Student numbers	%	UK Comparator (%)	Growth 2009/10 to 2014/15	Growth 2009/10 to 2014/15
UG	9,770	80%	82%	8,850	79%	82%	10%	6%
PG	2,415	20%	18%	2,315	21%	18%	4%	4%
Total	12,185	100%	100%	11,165	100%	100%	9%	6%

Source: HESA 2009/10 to 2014/15

Age Profile

3.5 The University of Essex has a similar age profile to the national average. Around 54% of students are aged 20 years or younger. The institution's above average growth relates to students in the age category of 24 years or below, reflecting the fast growth in UG level students. Patterns of student numbers are again similar for the Colchester Campus.

Table 3.3: Age Profile of students

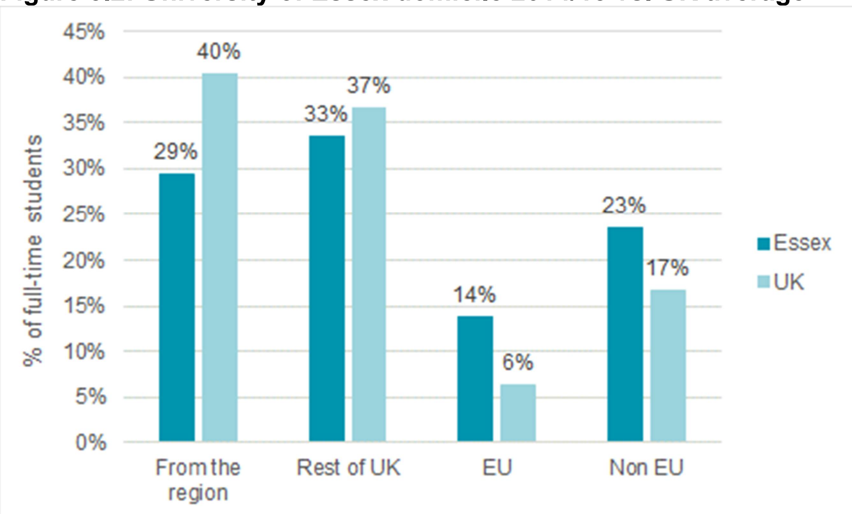
Age of Study	2014/15			2009/10			Essex	UK
FT & SW	Student numbers	%	UK Comparator (%)	Student numbers	%	UK Comparator (%)	Growth 2009/10 to 2014/15	Growth 2009/10 to 2014/15
18	1,895	16%	14%	1,655	15%	14%	15%	9%
19	2,365	19%	18%	2,015	18%	18%	17%	10%
20	2,320	19%	19%	2,025	18%	17%	15%	15%
21 – 24	3,475	29%	31%	3,065	27%	31%	13%	6%
25 – 29	985	8%	9%	1,080	10%	10%	-9%	-5%
30 & over	1,145	9%	8%	1,325	12%	10%	-13%	-11%
Unknown	-	0%	0%	-	0%	0%		-87%
Total	12,185	100%	100%	11,165	100%	100%	9%	6%

Source: HESA 2009/10 to 2014/15

Domicile

3.6 The University of Essex has a diverse student population with the proportion of international students being well above the national average, as shown in the following chart.

Figure 3.2: University of Essex domicile 2014/15 vs. UK average



Source: HESA 2014/15

3.7 While both, EU and non-EU students are highly represented; only EU students grew significantly faster than the UK average reaching 1,670 students in 2014 (+45%). On the contrary, a growth rate of 10% was achieved for non-EU students, which is below the UK average of 20%. A high proportion of international students is regarded as having a positive impact on student demand for term time accommodation, which is likely to further increase if the University pursues its international focus, as embedded in its identity, values and Strategic Plan 2013-2019. This is equally valid with regard to the Colchester Campus, which mirrors the institutional pattern of student domiciles.

Table 3.4: Domicile of students

Domicile	2014/15			2009/10			Essex	UK
FT & SW	Student numbers	%	UK Comparator (%)	Student numbers	%	UK Comparator (%)	Growth 2009/10 to 2014/15	Growth 2009/10 to 2014/15
UK	7,655	63%	77%	7,410	66%	79%	3%	3%
EU	1,670	14%	6%	1,155	10%	6%	45%	12%
Non EU	2,860	23%	17%	2,600	23%	15%	10%	20%
Total Non UK	4,530	37%	23%	3,750	34%	21%	21%	18%
Total	12,185	100%	100%	11,165	100%	100%	9%	6%

Source: HESA 2009/10 to 2014/15

3.8 Since 91% of all international students at the University of Essex are based at Colchester main campus, the main campus and the institution overall have the same profile of country domiciles. As shown in the table below, China, Nigeria, Hong Kong, Norway, Malaysia and the United States are the main sources of non-EU students at the University of Essex. Among these students, there are 90 Chinese students based at the Southend campus and 60 US students based at Loughton campus. EU students are mainly domiciled in Cyprus, Romania, France, Lithuania, Greece and Bulgaria.

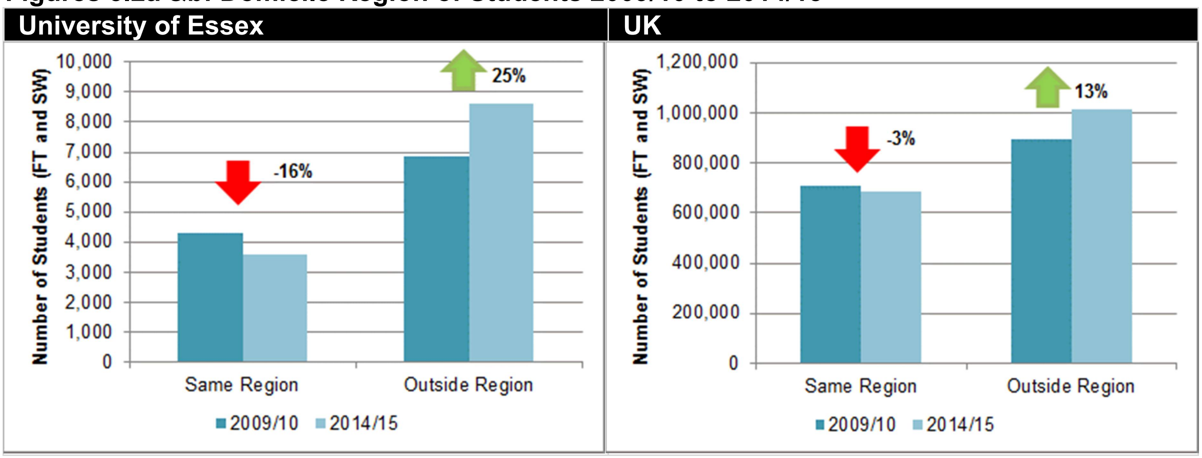
Table 3.5: Country Domiciles of Students at the University of Essex

Non-EU Students		EU Students	
China	800	Cyprus (EU)	375
Nigeria	325	Romania	275
Hong Kong	215	France	205
Norway	210	Lithuania	135
Malaysia	160	Greece	125
United States	140	Bulgaria	100

Source: HESA 2014/15

3.9 A greater proportion of students at the University of Essex are from outside the institution's region than the national benchmark (70.6% vs. 59.7%). The number of students from outside the region also experienced faster growth over a 5-year time span than the UK average (25% vs. 13%). This development is likely to contribute to sustaining and increasing demand for purpose-built student accommodation at the Colchester campus.

Figures 3.2a &b: Domicile Region of Students 2009/10 to 2014/15



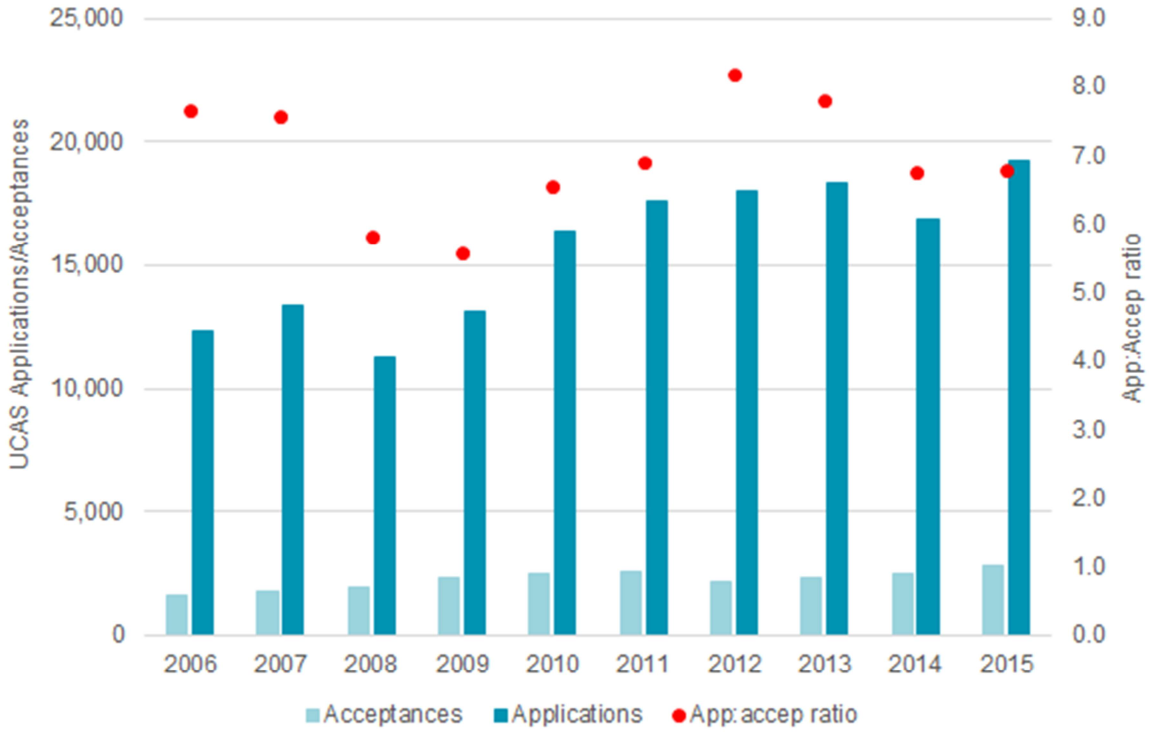
Source: HESA 2009/10 to 2014/15

Applications

3.10 Applications to the University of Essex have grown significantly from 2008 to 2015 (+71 vs. UK average of 32%)[1]. Contrary to the national trend, applications increased in 2012, the year of the latest tuition fee rise, and only declined in 2014. Nonetheless, the University was able to maintain or slightly grow its first year intake in 2014 due to successful Clearing. Applications increased significantly in 2015, up by 14% compared to 2% at a national level.

3.11 The University of Essex increased their acceptances by 46% from 2008 to 2015, which is significantly above the UK average of 16%. As a result, the ratio of applications to acceptances fell from its peak of 8.2 in 2012 to 6.8 in 2014. The ratio was maintained at 6.8 in 2015, above the UK average of 6.6, as the number acceptances and applications grew at a similar rate that year.

Figure 3.3: UCAS Applications and acceptances over time, University of Essex



Source: UCAS end of year cycle statistics 2015

Tuition Fees

3.12 As of 2006/07, tuition fees for undergraduate study in England were increased and capped at £3,000 a year (plus inflation) until 2009. In 2012/13 the new tuition fee cap of £9,000 was introduced. A system linking tuition fee increases for full-time UG courses to a university's performance in the new Teaching Excellence Framework (TEF) will be introduced in phases over the next three years. For the academic year 2016/17, the University of Essex decided to maintain its fee level at £9,000 per

[1] It should be noted that in 2008 the UCAS application system changed from six to five choices, which had an impact on the time series data. Thus, application data from 2008 onwards is not completely comparable to earlier years. Equally, the changes to core and margin in 2014 to allow more ABB students to "trade up" may have changed the way that student apply to university through the UCAS system.

year for all new full-time undergraduate students from the UK and EU (as advertised on their website in September 2016). Fees are set to increase to £9,250 in 2017/18.

3.13 The 2015 budget announced the abolition of the maintenance grant, and the provision of larger loans to students of lower income households instead. This change came into effect for the academic year 2016/17. In 2015 the maintenance grant was still available to students whose household income is less than £42,620 per year. Eligible students will be able to apply for loans through Student Finance England. In 2016/17 the maximum maintenance loan for students is £8,200 per year (up from £5,740 in 2015) for those who are living away from home (outside London). For those students living at home the maximum maintenance loan is £6,904 per year (up from £4,565 in 2015).

3.14 As with tuition fees systems since 2006, loans will not be repaid until after the student obtains work. Under the new system, students will not start repaying their maintenance loans until they enter employment and earn over £21,000 per year.

3.15 From 2016/17 onwards, UK and EU students on a taught or research master course can take out a loan through the government of up to £10,000 (part-time: £5,000) to help with their tuition fees or living costs.

3.16 Tuition fees at the University of Essex in 2016/17 for UK and EU undergraduate students are charged at £9,000 per year. International undergraduate students are charged £12,950 per year for full-time undergraduate degree courses and the International Year 1 in Business, which increases to £13,350 per year in 2017/18. The International Foundation Programme costs £11,350 per year in 2016/17 (£11,750 in 2017/18).

3.17 UK and EU postgraduate students studying an MPhil, PhD, MAD or MSD award will pay £4,120 per year, with international students paying £14,950 for Biological Sciences and Psychology degrees and £12,950 in all other subject areas. Taught programmes such as MA, MSc and MRes will cost UK/EU students between £5,950 and £9,950 per year with fees rising to £11,150 in computational finance and £12,700 in some areas of performing arts. Master fees for international students are between £14,500 and £15,500 depending on the subject of study.

Bursaries

3.18 Undergraduate students commencing their studies in 2016/17 with a household income of up to £25,000 will receive a total bursary of £2,500 over three years. The bursary is only available to UK full-time students.

3.19 The University also offers a number of scholarships to undergraduate and postgraduate students with different eligibility criteria. There are various financial support schemes, such as the German or Greek Partnership Bursaries, which are only accessible to students from the respective nationalities. The Masters Excellence Scholarship awards a 25% discount on tuition fees for self-funded home and EU students who achieved a first class honours bachelor’s degree at a UK university.

Research Profile and University Attractiveness

3.20 The University of Essex is ranked among the top 40 universities in the Times and Complete University league tables, and placed 62 in the Guardian ranking 2017. Across all rankings, student satisfaction scores highly, whereas a fall in places was mainly due to a higher student to staff ratio

and slightly lower entry tariff which coincided with successful recruitment.

Table 3.7: University league table performance

	2011	2012	2013	2014	2015	2016	2017
Times	41	41	40	39	32	35	30
Guardian	43	39	50	63	54	47	62
Complete University	37	38	39	39	39	34	40

Source: Newspaper university league tables

3.21 The University performs well in the National Student Survey 2016, with a ranking of joint 20th in the country with an average satisfaction rating of 90%. In The Times Higher National Student Experience Survey 2016, the University was ranked 65th out of 117 institutions. The highest scores were achieved in categories relating to campus facilities, such as 'Good environment on campus/around university', 'Centralised convenient facilities', 'Good community atmosphere' and 'Good library'. In general, the survey highlights high levels of satisfaction at campus based universities, with five of the top 10 institutions sharing this characteristic.

3.22 The University of Essex exhibits a strong research profile being ranked in the top 20 universities for research excellence overall, in the top 5 for Social Sciences and number one for politics research. The performances of different subject areas are shown in the table below. The highest percentage of world leading research was submitted in Politics and International Studies, Modern Languages and Linguistics as well as Psychology, Psychiatry and Neuroscience. When scores for world leading and internationally excellent research are combined, another three well performing research areas are identified; i.e. Economics and Econometrics, Art and Design and Philosophy.

Students to Bed Ratio Projections

3.23 The University projects the full-time student body at Colchester to grow to just over 15,485 students by 2020/21 from 11,790 in 2016/17 (based on University forecast). This is a CAGR of 7%.

3.24 Using forecast student numbers provided by the University, combined with HESA data, C&W derived the demand for university accommodation over time. By removing all students domiciled in Essex and some students from surrounding counties, who may not wish to live on campus due to the proximity of their homes to the University, as well as excluding partner colleges and other campuses than Colchester, a Student:Bed ratio (SBR) for the Colchester campus is calculated using the number of beds available in any given year. The following table shows the calculations with new supply being considered from 2017 onwards.

3.25 The 2014/15 SBR as a baseline is measured as 1.8:1. With the first circa 643 beds delivered by 2018, and due to the University's actual and projected growth, the SBR moves to 2.5:1. The sensitivity test of a 10% shortfall in the demand pool in 2018 leads to an SBR of 2.3, which is strong overall and compared to other campus based institutions, and therefore acceptable to C&W.

Table 3.9: Demand Pool Calculation and Student to Bed Ratio at the University of Essex

	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Colchester Students derived from HESA	8,840	8,645	9,455								
Colchester FT students (sourced from Uni)			9,301	10,055	11,791	12,682	13,689	14,597	15,485	15,485	15,485
Deductions (local students not in TTA) (HESA method)	1,545	1,553	1,666								
Future local deductions (pro rata using time trend)				1,754	1,922	2,067	2,231	2,379	2,524	2,524	2,524
Demand pool (all years)	**7,295**	**7,092**	**7,789**	**8,301**	**9,869**	**10,615**	**11,458**	**12,218**	**12,961**	**12,961**	**12,961**
1st year demand pool	**3,140**	**3,244**	**3,874**	**3,874**	**4,020**	**4,232**	**4,481**	**4,694**	**4,899**	**4,899**	**4,899**
Supply (existing + Phase 2a)	**3,674**	**4,085**	**4,421**	**4,314**	**4,114**	**4,114**	**4,557**	**4,557**	**4,557**	**4,557**	**4,557**
University owned	3,423	2,657	2,686	2,686	2,686	2,686	2,486	2,486	2,486	2,486	2,486
Uliving Existing (Meadows I incl. Quays)	-	1,428	1,428	1,428	1,428	1,428	1,428	1,428	1,428	1,428	1,428
1 year nominations	251	-	307	200	-	-	-	-	-	-	-
											-
Meadows ph2a	-	-	-	-	-	-	643	643	643	643	643
Meadows ph2 ALL	-	-	-	-	-	-	643	643	1,193	1,193	1,743
Students:Bed Ratio (All years of study)											
SBR assuming Ph2a 643 beds	2.0	1.7	1.8	1.9	2.4	2.6	2.5	2.7	2.8	2.8	2.8
SBR assuming Ph2 at 1743 beds	2.0	1.7	1.8	1.9	2.4	2.6	2.5	2.7	2.5	2.5	2.3
SBR Meadows ph2a and no growth from 2016	2.0	1.7	1.8	1.9	2.4	2.4	2.2	2.2	2.2	2.2	2.2
Students:Bed Ratio (First years only)											
SBR assuming Ph2a 643 beds	0.9	0.8	0.9	0.9	1.0	1.0	1.0	1.0	1.1	1.1	1.1
SBR assuming Ph2 at 1743 beds	0.9	0.8	0.9	0.9	1.0	1.0	1.0	1.0	1.0	1.0	0.9
SBR Meadows ph2a and no growth from 2016	0.9	0.8	0.9	0.9	1.0	1.0	0.9	0.9	0.9	0.9	0.9

Notes: these are based on C&W's treatment of University of Essex's forecasts at Colchester, with pro rata deductions of local students according to the rates of change apparent in the time series evidence to date. On the supply side the timing of the addition of new rooms is indicative.

Short term arrangements run for 1 year only and can therefore be removed from the University's supply if required (as was the case in 2013). The number of University rooms drops by 200 from 2018/19 due to a rolling programme of refurbishments. Those rooms will ultimately all come back into use.

This is driven by an analytic methodology applied and tested through a number of Universities. Deductions from the demand pool include those students who live within a commutable time from the University and who currently do not live in term time accommodation (in this instance Essex, Bedford, Cambridgeshire, Hertfordshire, Norfolk, Southend on Sea, Suffolk). The assumption is that these students either live at home with a parent/guardian and/or are commuting.

3.26 Looking at the forecast post-2018, if only 643 beds are built the SBR at Colchester becomes considerably higher than the market expectations, based on the University's projected growth. In order to show the implications of the full potential Meadows scheme of 1,743 beds on the proposed phasing we have assumed that there is no growth beyond the final year of projections provided by the University (2020). By 2022, with all of the additional beds in place the SBR moves to 2.3 under current assumptions. Running a sensitivity once again assuming a 10% shortfall in the demand pool, this numbers moves to 2.1. These numbers are strong in comparison with many campus based universities and are therefore acceptable to C&W.

3.27 Cushman & Wakefield has also calculated an additional demand scenario (based on the 2014/15 demand pool) whereby the University suffered a 50% reduction in EU students as a result of the UK's decision to leave the European Union. Essex currently attracts 14% of its full-time student base from the EU, above the UK average of 6%. A 50% reduction in these students would result in a 2014/15 SBR of 1.6:1. It should be noted that the 50% reduction has been included as an "extreme scenario" and the University of Essex is well placed to continue to attract EU students in the future.

3.28 C&W has calculated the SBRs for a range of campus based institutions to illustrate that many of them operate at ratios which are below the average of 2.1:1 students per bed (once local students are removed). These benchmarks (calculated on a like-for-like basis as far as possible) highlight that it is possible for campus based institutions to successfully operate at these levels, and indeed that we understand that at Lancaster and Keele further accommodation projects are also being

considered or encouraged off campus.

Table 3.10: Comparator SBRs 2014

		2014				
		FT Students (all campuses)	Beds	Beds expected to increase?	SBR	2016 Essex only*
The University of Birmingham		27,300	5,600	Y	4.0	
The University of Exeter		19,370	6,600	Y	2.9	
The University of Kent		17,240	4,700	Y	2.3	
The University of Reading		12,590	5,000	Y	2.1	
NATIONAL AVERAGE SBR (on and off campus supply)					2.1	
Loughborough University		14,025	7,800	N	2.0	
The University of Warwick		17,790	8,400	Y	2.0	
The University of Keele		7,420	3,300	Y	1.9	
The University of Essex		12,185	4,421		1.7	2.4
The University of Lancaster		11,450	6,600	Y	1.5	

Details of the demand pool relate to competitor projects and have not been shown, this table is only provided as an illustration

**note that the comparisons for other universities are not yet available – HESA 2014/15 is the latest published.*

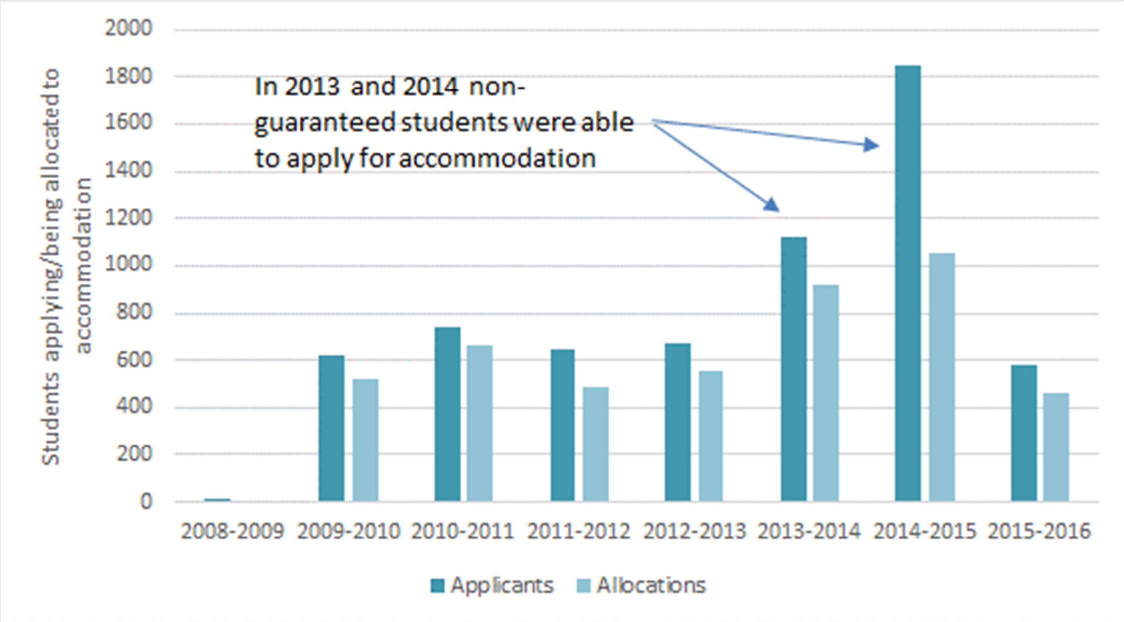
Latent Accommodation Demand and Demand from Returning Students

3.29 We understand that due to the increased number of first years at the University there is a recommendation being discussed to remove the guarantee to non-EU international students. This has been something of a competitive advantage in recent years and something that is offered by other campus based institutions such as Kent. However, from 2015 (until the new scheme is envisaged to be ready in 2018) the University foresees that there will be insufficient accommodation to meet this element of the guarantee. A further recommendation aims to remove the allocation of rooms from the Colchester Institute, where 36-54 of its students are accommodated by the University in recent years.

3.30 C&W has observed that following a large increase in bedrooms, there is often a short period of readjustment needed in the marketing/booking/allocation system. In response to the 648 room increase in accommodation due to The Meadows I in 2013/14, the University opened applications to non-guaranteed returning students for the first time in nine years. That year there were 616 applicants and 479 accepted a place on campus.

3.31 A year later in 2014/15, the institution experienced a significant increase in applications from non-guaranteed returners; receiving 642 applications. 535 rooms were finally allocated to this group. Due to strong undergraduate first year recruitment that year, however, it was necessary for the university to seek additional accommodation in order to house all the students who had been offered a room. Additional rooms were secured through the private sector accommodation – The Maltings (200 rooms), Forest Road (82 rooms) and Candan House (25 rooms). This resulted in 235 returning students being housed on campus, while the remaining 306 students were offered rooms in these private schemes.

Figure 3.4: Returning Undergraduate Student Applications and Allocations of accommodation



Source: The University of Essex

3.32 The change in the number of rooms therefore allowed the University to test demand for returning students to live on campus and the result is a demonstrable level of demand from this group. This was only tested for two years. C&W believes that given more time and a cultural change in the expectations of returning students, this proportion could be increased further. We also understand that there is significant and sustained demand for accommodation from returning students, and that this is likely to become more pronounced as the University grows.

Occupancy Levels

3.33 Overall, occupancy levels have been near to 100% in the year 2014/15 and were 100% at the start of the academic year 2015/16. The Quays achieved levels of 98% and 99%, while most buildings of The Meadows were fully occupied (99% and 100%), reflecting the popularity of the accommodation offer. Only the three Godwin town houses, which form part of The Meadows, saw a lower occupancy rate of 96%. Similarly, older halls such as The Towers and South Courts showed lower occupancy levels overall, with 96%. University accommodation was fully occupied at the start of the academic year 2015/16.

3.34 Occupancy across the whole of the University's portfolio is shown below. The University has achieved high occupancy across its rooms with 99% and 100% achieved for the last three years, and in 2011/12. In 2012 occupancy was 95%, coinciding with the increase in tuition fees. In that year occupancy was lower across all the stock at the start of the year, including The Quays.

Table 3.11: Occupancy

TOTAL UNIVERSITY OWNED AND MANAGED

	Number of Rooms	Occupancy	Voids	%
2010/11	3705	3518	187	95%
2011/12	3696	3613	83	98%
2012/13	3674	3491	183	95%
2013/14	4085	4039	46	99%
2014/15	4421	4421	0	100%
2015/16	4421	4421	0	100%

Source: University of Essex

3.36 Double en-suite rooms in cluster flats in South Courts, the North Houses and the Quays are popular among returning international students, however they also pose an increased void risk. Rooms, which could not be filled with returning international students in the past proved to be difficult to let to other students due to relatively high rents for single occupants and their location in cluster flats with predominantly international students. Some double en-suite rooms were offered as temporary twin rooms in 2014/15, a room type, which is not permanently prevalent on campus. In order to address letting difficulties of the double rooms, the University suggests to change the use of 32 double rooms in South Courts and North Houses to twin rooms, which could be used to assess future demand for this room type.

3.37 There were also some difficulties in letting couple flats, which were often offered to students on the waiting list. From the 32 flats, 13 were let as single or twin rooms in 2014/15. A main reason may be the dated décor of the flats in The Towers in combination with the relatively high rent level. Thus, it is proposed that the interior of the flats should be updated and their use should be changed to penthouse apartments targeted towards premium single, couples and twin occupants. This would position the offering at the higher end of the accommodation portfolio, both in terms of quality and rents.

3.38 The third accommodation type, which is envisaged to be changed are the family flats in The Towers. Letting problems have arisen due to their unsuitability for families. Apart from having dated décor, noise levels are relatively high and they are too small for families with more than one child or a child of 5 years or older. In addition, the off campus houses in St. Andrews Avenue are priced higher than comparable accommodation in the private sector. As result, the University envisages the removal of St. Andrew's from the accommodation portfolio by either selling it or letting it to visiting academics. The Tower family flats could be changed to premium apartments as mentioned above, while Brightlingsea Court could potentially provide family accommodation.

Summary

3.39 The University of Essex is a successful and well regarded institution. The evidence set out in this section demonstrates its academic strengths and its solid basis of demand for student accommodation against the background of a high proportion of full-time and international students. The University is currently on a strong growth trajectory and has been able to materially change its student population in recent years. There is therefore positive evidence that the University will continue to grow in future, both from the increase in the size of the 1st year intake, and the compound effect of more returning students.

4.0 Accommodation Supply

University of Essex Accommodation Stock

4.1 The University has three campuses with the majority of accommodation being located at the main campus in Colchester. In 2016/17, the University offers 4,117 rooms (4,113 lettable). The number of private rooms is limited, counting 1,256 rooms.

Table 4.1: Summary Table of Accommodation in Colchester

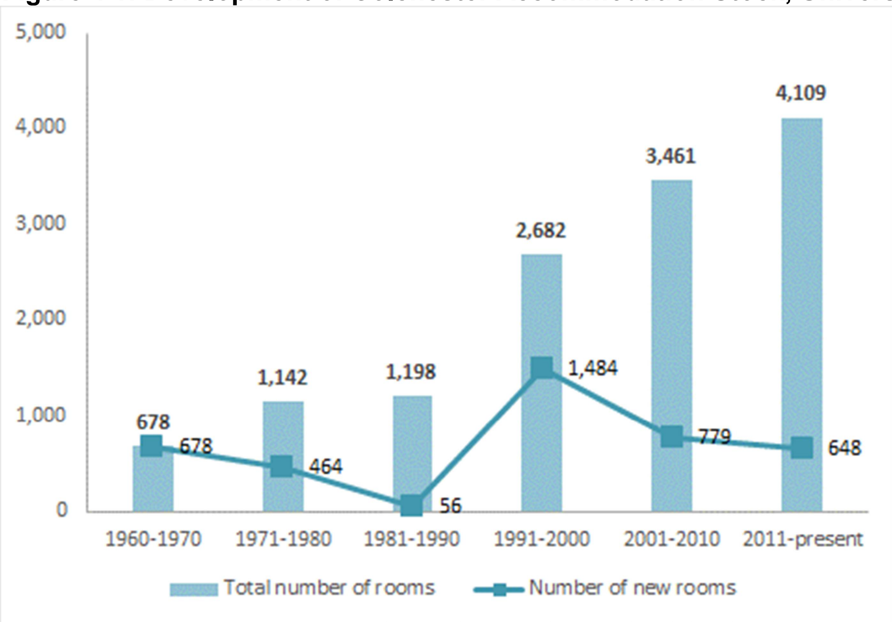
Provider	2014/15	2015/16	2016/17	2018/19 (known)
University	4,117	4,117	4,117	4,753**
Private in Colchester *	1,256	1,256	1,256	1,256
Total in Colchester	5,373	5,373	5,373	6,009**

*Note: the University nominated 200 rooms in a 1 year arrangement at the Maltings in 2015 but not in 2016
** The addition of 643 rooms at Meadows 2a minus 7 rooms at Wolfson

University Accommodation in Colchester

4.2 The University of Essex has an accommodation stock of over 4,000 bed spaces on its Colchester campus. A significant number of 1,198 rooms were developed over 25 to 50 years ago, with another 1,484 being over 15 years old. The Quays and The Meadows are the newest additions to the portfolio, being built in 2003 and 2013 respectively.

Figure 4.1: Development of Colchester Accommodation Stock, University of Essex



Source: University of Essex Accommodation Data

4.3 The University offers various room types and price points across its estate; all being on a self-catered basis. Let lengths are 39 weeks for undergraduate students and 50 weeks for postgraduate students. The newest halls; i.e. The Quays and The Meadows were developed in partnership with Uliving and are operated by Derwent FM. The following table highlight the stock by room type at the Colchester campus.

Table 4.2: University Accommodation in Colchester, 2016/17

Halls of Residence	Room Type	No of Rooms	Lease Length (weeks)	Weekly Rent 2016/17	Annual Rent 2016/17		Age	Walking Distance to Campus
					39 week contract	50 week contract		
The North Towers A	Shared	292	39/50	£88.20	£3,439.80	£4,410.00	1965/'66	3 min.
	Couple Flat	8	39/50	£155.47	£6,063.33	£7,773.50		
The North Towers B	Shared	360	39/50	£88.20	£3,439.80	£4,410.00	1968	
	Couple Flat	9	39/50	£167.16	£6,519.24	£8,358.00		
North Towers Total		**669**						
The South Towers	Shared	458	39/50	£76.93	£3,000.27	£3,846.50	1971	
	Couple Flat	2	39/50	£199.08	£7,764.12	£9,954.00		
	Family Flat	6	39/48	£182.21	£7,106.19	£9,110.50		
		2	39/49	£202.23	£7,886.97	£10,111.50		
		5	39/50	£179.06	£6,983.34	£8,953.00		
South Towers Total		**473**						
Wolfson Court	Shared	56, will be reduced to 49	39/50	£92.89	£3,622.71	£4,644.50	1982	3 min.
The Houses	En-suite	252	39/50	£122.64	£4,782.96	£6,132.00	1991	5 min.
	Double En-suite	6	39/50	£146.02	£5,694.78	£7,301.00		
	Accessible	8	39/50	£76.93	£3,000.27	£3,846.50		
	Couple flat	1	39/50	£179.06	£6,983.34	£8,953.00		
The Houses Total		**323**						
South Courts	En-suite	1188	39/50	£135.38	£5,279.82	£6,769.00	1993/'96/ 2000	3 min.
	Double En-suite	26	39/50	£146.02	£5,694.78	£7,301.00		
	Accessible	4	39/50	£76.93	£3,000.27	£3,846.50		
	Family Flat	1	39/50	£167.16	£6,519.24	£8,358.00		
South Courts Total		**1,219**						
The Quays	En-suite	736	39/50	£123.69	£4,823.91	£6,184.50	2003	15 min.
	Premium En-suite	18	39/50	£137.83	£5,375.37	£6,891.50		
	Double En-suite	25	39/50	£151.90	£5,924.10	£7,595.00		
	Family Flat	1	39/50	£182.21	£7,106.19	£9,110.50		
The Quays Total		**780**						
The Meadows	En-suite	420	39/50	£140.98	£5,498.22	£7,049.00	2013	10 min.
	Shared	228	39/50	£131.39	£5,124.21	£6,569.50		
	Flat	1	39/50	£167.16	£6,519.24	£8,358.00		
The Meadows Total		**649**						
Total		**4,113**						

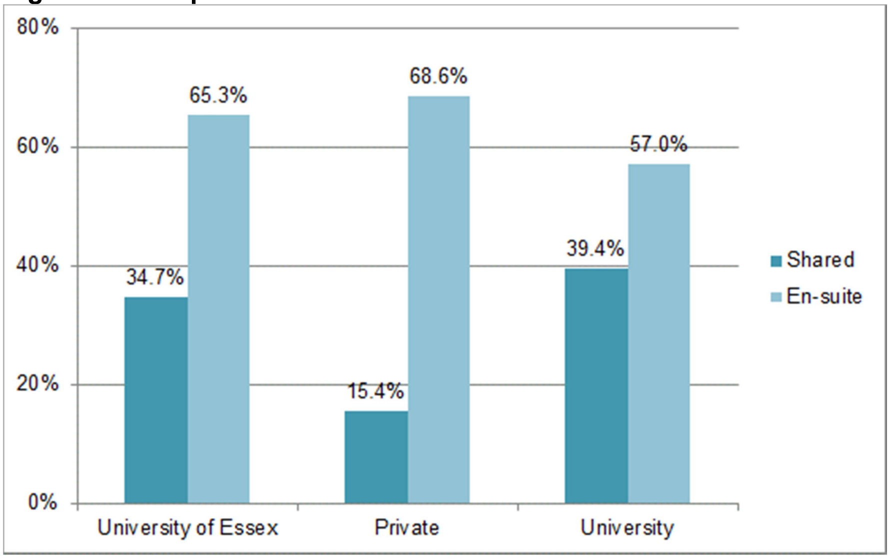
Source: University of Essex accommodation website and information

4.4 The lowest priced single occupancy room is a standard room at The Towers for £76.93 per week, while the highest priced option is an en-suite room at The Meadows for £140.98 per week. Couple flats/studios and family flats are mainly located in The Towers and are priced between £155.47-£199.08 per week for couple flats and between £179.06 to £202.23 for family flats. Additionally, there are two family houses off campus on St. Andrews Avenue.

4.5 Rent increases across all rooms (excluding family flats and couple studios) were 2% between 2015 and 2016. Rents for family flats and studios increased by 3%-5% year-on-year. Annual RPI in 2015 was 1% by comparison.

4.6 The University stock has a high proportion of en-suite rooms in comparison to the overall market for university accommodation in the UK (65.3% vs. 57%), which is positive in terms of meeting student demand for this popular product type.

Figure 4.2: Proportionate Distribution of Standard and En-suite Accommodation



Source: University of Essex and C&W Student Accommodation Tracker 2016

Note that in the University's terminology a shared room is a standard room with shared bathroom

4.7 A requirement for up to 2,000 additional rooms has been identified by the University in order to house students arising from academic growth as well as potentially recapturing latent demand from returning students who have already demonstrated a preference to be housed on campus. These new beds would be built in phases of the Meadows phase 2

Table 4.4: Meadows Phase 2a Rents and Room Types

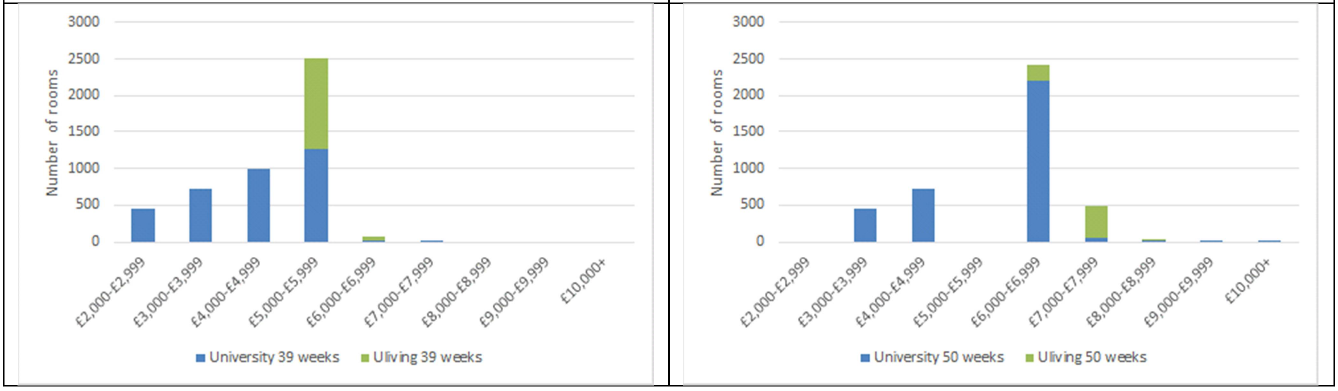
Type of Room	Quantity	Model 2015/2016 Base Date	Rent 2016/17 (1st Contract Year)	Rent 2017/18 (2nd Contract Year)	Rent 2018/19 (3rd Contract Year	Letting Period (Weeks)
Standard ES	601	£141.00	£144.53	£148.86	£153.33	39
Enhanced ES	6	£155.00	£158.88	£163.64	£168.55	39
Premium ES	16	£164.00	£168.10	£173.14	£178.34	39
Studio	20	£168.00	£172.20	£177.37	£182.69	39
Total	**643**					

4.8 Note that the let length for the scheme has been set at 39 weeks in the base case model. The standard let length will be useful competitively as it will compare favourably with accommodation on campus and also is cheaper than the Maltings off campus.The small number of studios in the scheme mitigates the risk of low demand for this type of room. The accommodation will be in close proximity to the campus and its design will offer a high quality and social choice to the existing mix at the University of Essex.

4.9 On campus the University offers a very wide range of rents. It also offers rooms on both a 30 or a 50 week let option. The charts below illustrate the relationships between the University and the Uliving accommodation on each of the tenancy options. Note that the Meadows Phase 2a is only currently modelled on 39 week lets, and hence only appears in the Uliving accommodation in that chart.

Figures 4.3a&b: Rent Charts

39 Week Let Chart	50 Week Let Chart



4.10 The take up of 50 week lets at the Meadows and at the University of Essex overall is as follows:

Table 4.5: Record of 50 week lets within the Meadows Phase 1 and the UoEssex portfolio

	Meadows & Quays		All University accommodation	
	% on 50 week lets	Lettable rooms	% on 50 week lets	Lettable rooms
2014/15	33%	1,429	15%	4,113
2015/16	29%	1,429	14%	4,113
2016/17	27%	1,429	14%	4,113

Source: University of Essex

Private Rented Accommodation in Colchester

4.11 The University stock mainly targets new undergraduates and postgraduates as well as returning overseas students. While returning UK and EU students have mainly taken up rooms in the private sector (both PBSA and HMO), the University has noticed an increasing demand from these students for on campus term time accommodation. In 2014/15, 541 non-guaranteed students were housed in university accommodation.

4.12 The private PBSA market comprises 1,256 rooms across five schemes in 2016. The three smallest schemes; Forest Road House, Candan House and Greenstead House, constitute a low price option with relatively basic amenities. Avon Way House is operated by Mansion Student and offers mid-range accommodation both in terms of quality and price. The newest scheme is The Maltings, which opened in 2014, adding 780 rooms to the market. The University of Essex nominated 200 of these rooms in 2015, and the student union has an arrangement to house returning students here.

Table 4.3: Private Purpose-built Student Accommodation in Colchester

Halls of Residence	Room Type	No of Rooms	Lease Length (weeks)	Weekly Rent 2016/17 in £	Annual Rent 2016/17	Walking Distance to Campus	
Avon Way House	Standard	254	48	91/93	£4,368 / £4,464	20 min.	
	2 Bedroom Flat			96	£4,608		
Forest Road House	Standard	116	48	78.46/92.3	£3,766.08 / £4,430.4	20 min.	
	En-suite	8		106.15/120	£5,095.2 / £5,760		
Candan House	Standard	45	48	83.07	£3,987.36	20 min.	
	En-suite	8		106.15	£5,095.20		
Greenstead House	Standard	46	44	87.69	£3,858.36	15 min.	
	En-suite			106.15-120	£4,670.6 / £5,280		
The Maltings	En-suite	779	44	135/139	£5,940 / £6,116	20 min.	
			51	129.5/133.5	£6,604.5 / £6,808.5		
	Studio		44	£159	£6,996		
			51	152.5/159	£7,777.5 / £8,109		
	1 Bed Flat		51	£165	£8,415		
	Double Studio		51	£185	£9,435		
Total		**1,256**					

Source: Provider websites and C&W Student Accommodation Tracker

Houses of Multiple Occupation in Colchester

4.13 According to Colchester City Council there were approximately 600 licensed or due to be licensed HMOs. However, the actual number of this housing type is expected to be significantly higher, as around 2,000 unconfirmed HMOs are thought to exist. Student HMOs are predominantly concentrated in areas close to the University, such as Greenstead, Wivenhoe and the Hythe. Moreover, 200 HMOs were registered under the Student Accommodation Accreditation Scheme as of 2010/11 (Colchester City Council, HMO Strategy 2012/13).

The Development Pipeline

4.14 A 230 bed scheme proposed by Victoria Hall is the only application for PBSA currently in the planning pipeline for Colchester. The proposed plans comprise a mix of cluster flats and studios.

Table 4.3: Development pipeline Colchester

Address	Postcode	Planning Ref	Status	App date	No of beds	Applicant	Additional information
Former Bus Depot, Magdalen Street, Colchester, Essex	CO1 2LD	160103	Application	20/01/2016	230	Victoria Hall	59 cluster flats, 17 studios

Source: Colchester City Council Planning Portal

Summary of Key Implications, Risks and Uncertainties

4.15 The nature of the University's campus naturally encourages students to want to live on campus, and there are limited options to live in purpose built accommodation elsewhere in the town. Other than The Maltings, there are no substantial PBSA blocks to date (although there is a planning application for 230 beds from Victoria Hall) and this has resulted in a predominance of students in the housing market.

4.16 The University's strategy to encourage greater participation in residences is in line with strategies of other campus based institutions. The new accommodation is expected to add to the existing portfolio by increasing the number and mix of en-suite rooms as well as creating a small number of studios. The proposed range fits well in terms of offering a choice of price points and in creating accommodation which adds to the student experience.

5.0 Operations and Marketing

University Accommodation Marketing Process and Strategic Direction

5.1 The University markets their main stock of accommodation through their website. Accommodation for couples and family flats are not marketed on the website but are dealt with by the accommodation office directly.

5.2 Accommodation is offered to students in line with the accommodation guarantee, however the campus nature of the University creates an opportunity to house a much wider group of students who also desire accommodation from the University on campus.

5.3 Some accommodation is marketed to returning home and EU undergraduate students as well as to all returning postgraduate students.

The Application Process

5.4 Once the UCAS status of prospective undergraduate students is unconditional firm or conditional firm, they can apply online via the myEssex applicant portal from early March onwards. First of all, a registration needs to be made after which it takes 24-48 hours for the relevant data to be imported into the application system. Postgraduate students (in years when they are able to apply) can also apply online. The data import takes about 72 hours. In order to meet the application deadline for guaranteed accommodation, applicants need to be aware of registering on time.

5.5 The application deadlines for guaranteed accommodation are the 26th August 2016 for undergraduates. No accommodation guarantee was offered to postgraduates in 2016. International Foundation Programme and Year One in Business students through the International Academy were able to apply for accommodation in 2016, but returning students were unable to access the system in 2016.

5.6 Accommodation offers are sent by email and include information on the allocated room and charges. There is only a limited time frame for an offer to be accepted online.

Accommodation Guarantees and the Allocation Process

The University guarantees rooms to the following categories of students provided they apply until the published deadlines:

Undergraduate Student applications

- Home, EU and international first year undergraduate students, who hold an offer of the University of Essex as their firm choice and who applied by 26 August 2016. Applicants with conditional firm offer need to achieve unconditional status by the UCAS deadline, in order to be guaranteed a room.
- Foundation Year students as well as Pre-Sessional English students are eligible for accommodation
- Returning international undergraduates were guaranteed if applications made before 15 january
- International Foundation, Incoming Study Abroad and Erasmus students, who undertake a full year of study
- Students under the age of 18 at the start of the academic year on a full time course

5.7 Postgraduate students are not guaranteed accommodation in 2016 but can apply, whereas in the previous year they were guaranteed, as were a number of other types of students such as Hotel students for the duration of their course.

5.8 Quotas are set for part year incoming study abroad and ERASMUS students as well as International Academy EELP students. If the number of these students exceeds the quota, they will be allocated according to their date of application. Remaining study abroad and ERASMUS students will be offered void rooms (if they exist) or be placed on a waiting list. International Academy students, who are not offered a room through the quota system, will also be added to the waiting list.

5.9 A contingent of rooms is also provided for late applicants comprising September Pre-Sessional English students, International Foundation and International Diploma students as well as clearing students from Hong Kong. Rooms are held until a week before Arrivals Day. Afterwards, any unfilled rooms are subsequently transferred to the general room pool to minimise the risk of voids. If student numbers exceed reserved rooms, they will be allocated according to the date of their application with the remaining students being placed on a waiting list.

5.10 A specific number of rooms are nominated internally to Student Support for RSN, Nightline and students with medical/welfare needs, and to the Student Union for Sabbatical Officers.

5.11 External organisations such as Colchester Institute, South Essex College and Barts and London School of Medicine and Dentistry are also provided with a number of rooms according to contractual agreements.

5.12 Finally, students on the waiting list will be offered rooms depending on the following priorities:

1. Students with welfare/medical needs
2. New international undergraduate and postgraduate students
3. New Home/EU undergraduate and postgraduate students
4. Part year Incoming Study Abroad, Erasmus and EELP students who fall outside the guaranteed quota of available rooms
5. Returning Study Abroad students
6. All other full-time students

Restrictive Covenant

5.13 There is a Restrictive Covenant (RC) in place on phase 1 of The Meadows accommodation. The RC states that the University will not enter into an arrangement without the service providers consent, support, market or advertise any other accommodation unless all the Applicable Tests have been satisfied in full and/or all the SPV rooms are nominated in the year that the University enters into an Excluded Relevant Arrangement.

5.14 The applicable tests state that:

- The students:bed ratio floor level of 1.5:1 must not be breached – for each of the 3 previous years
- The floor level would not be breached in the following 3 years utilising the University's projected student numbers provided to HEFCE; nor would it be breached if the proposed scheme were to be counted as part of bed supply in the 3 year period preceding the current contract year
- 98% of the rooms would have to be occupied for the 3 previous years.

5.15 According to the tests that C&W has done on the student numbers and demand metrics, we believe that test has been passed. This is using C&W's methodology for student demand based on HESA metrics and applying a commutable distance according to the Demand Pool calculations set out in Section 3 of this report. The definitions of the excluded local persons are included in the PA for completeness.

5.16 Supply of accommodation includes one off campus residence in the form of The Maltings, which is utilised by the Student Union and could be considered comparable accommodation. Normally C&W would not include such a residence as the University has influence over where its students reside to a large extent, and this favours accommodation on campus. However, due to the PA and the wishes of the Addressees of this Report, The Maltings has been included in the definition of Total Bed Supply.

5.17 Under these calculations and during all stages of the forecast, and based on the evidence provided under the PA methodology for supply, C&W has concluded that the Students:Bed ratio does not breach the restrictive covenant threshold of 1.5:1.

5.18 The calculations and the method followed in the PA are as follows:

Table 5.1: RC Test Calculations according to the PA

Bed to student ratio calculation		Three year backwards					Three year looking forward				
Source:		HESA					University provided				
	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Full time students	8,840	8,643	9,456	10,055	11,791	12,682	13,689	14,597	15,485	15,485	15,485
Deduction local students	1,545	1,553	1,666	1,754	1,922	2,067	2,231	2,379	2,524	2,524	2,524
Demand pool	**7,295**	**7,090**	**7,790**	**8,301**	**9,869**	**10,615**	**11,458**	**12,218**	**12,961**	**12,961**	**12,961**
1st year demand pool	**3,140**	**3,244**	**3,874**	**3,884**	**4,020**	**4,232**	**4,481**	**4,694**	**4,899**	**4,899**	**4,899**
Supply											
University owned	3,423	2,657	2,686	2,686	2,686	2,686	2,686	2,686	2,686	2,686	2,686
Meadows I and Quays	-	1,429	1,429	1429	1,429	1429	1,429	1,429	1429	1,429	1,429
Meadows II	-	643	643	643	643	643	643	643	643	643	643
Owned and Marketed	**3,423**	**4,729**	**4,758**	**4,758**	**4,758**	**4,758**	**4,758**	**4,758**	**4,758**	**4,758**	**4,758**
PBSA											
The Maltings	-	-	400	780	780	780	780	780	780	780	780
Total PBSA	-	-	**400**	**780**	**780**	**780**	**780**	**780**	**780**	**780**	**780**
Total supply	**3,423**	**4,729**	**5,158**	**5,538**	**5,538**	**5,538**	**5,538**	**5,538**	**5,538**	**5,538**	**5,538**
Bed/Student ratio											
Including PBSA	2.13x	**1.50x**	**1.51x**	**1.50x**	1.78x	1.92x	**2.07x**	**2.21x**	**2.34x**	2.34x	2.34x

6.0 The Meadows and The Quays

6.1 Uliving@Essex comprises of two purpose built student schemes:

- The Quays, Wivenhoe, Colchester, CO7 9BX and;
- The Meadows, Annan Road, Colchester CO4 3ZE.

6.2 Uliving@Essex was originally a partnership between the University and Bouygues. Bouygues have subsequently sold their stake in the partnership to Equitix.

6.3 As part of the partnership agreement with Uliving@Essex, the University have the right to nominate students each year at a set rent. The rent is subject to a fixed rent review each year, however, every five years this is rebased to market rental levels.

6.4 The two schemes are located on the North West edge of the Colchester campus, approximately a 10 to 15 minute walk to the centre of the campus. Whilst close on a map the two properties are separated by a railway line. There is a foot bridge which provides students with pedestrian access over the tracks and directly to the university campus.

The Meadows

6.5 The 648 beds at the Meadows are the newest accommodation on the campus. It has the most modern specification and decoration being only four years old. It provides:

- Townhouse rooms - 12 bedroom houses, with a shared kitchen, lounge. Each floor has four bedrooms and two bathrooms. The ground floor also has a disabled bathroom for guests. The typical room size is 10m2
- En-suite cluster flats – Between 6 and 8 bed spaces share a kitchen/dining room. The typical room size is 12.7m2.

The Meadows

Source: Uliving

6.6 All rooms have good quality fitted furniture with double beds. Buildings are set within an attractive landscaped environment approximately a 15 minute walk from the centre of the university campus.

The Quays

6.7 The Quays was built 14 years ago but was refurbished approximately 4 years ago. It provides:

- En-suite cluster flats – 4 to 9 bed spaces sharing a kitchen/dining room. The typical bedroom room size is 13m2. Rooms include some fitted furniture and single beds.
- Large en-suites cluster flats - these rooms are converted from former office/retail space and are slightly larger. Rooms include a double bed.
- Double en-suite rooms – large en-suite room with a double bed, two desks and chairs, two bedside cabinets and two wardrobes.

The Quays

Source; Uliving

Rents

6.8 The various rent levels at each property are in the table below. Under the Project Agreement rents are typically indexed at RPI + the z-factor (0.50% in each academic year until 2020/21.

Table 6.1: Rents over time

	No. of Rooms	Letting Period (weeks)	Actual Base Rents	Forecast Base Rents
			2016-17	**2017-18**
Meadows				
Shared	228	39	£131.39	£135.77
En-suite	420	50	£140.98	£143.38
Arber House Flat	1	39	£167.16	£170.00
Quays				
En-suite	219	50	£123.69	£128.14
En-suite	530	39	£123.69	£128.14
Large	2	39	£137.83	£140.17
Large	3	50	£137.83	£140.17
Doubles	13	50	£151.89	£154.47
Doubles	12	39	£151.89	£154.47
Flat D	1	52	£182.21	£185.31

Source: Equitix

Appendix A: Brand Identity

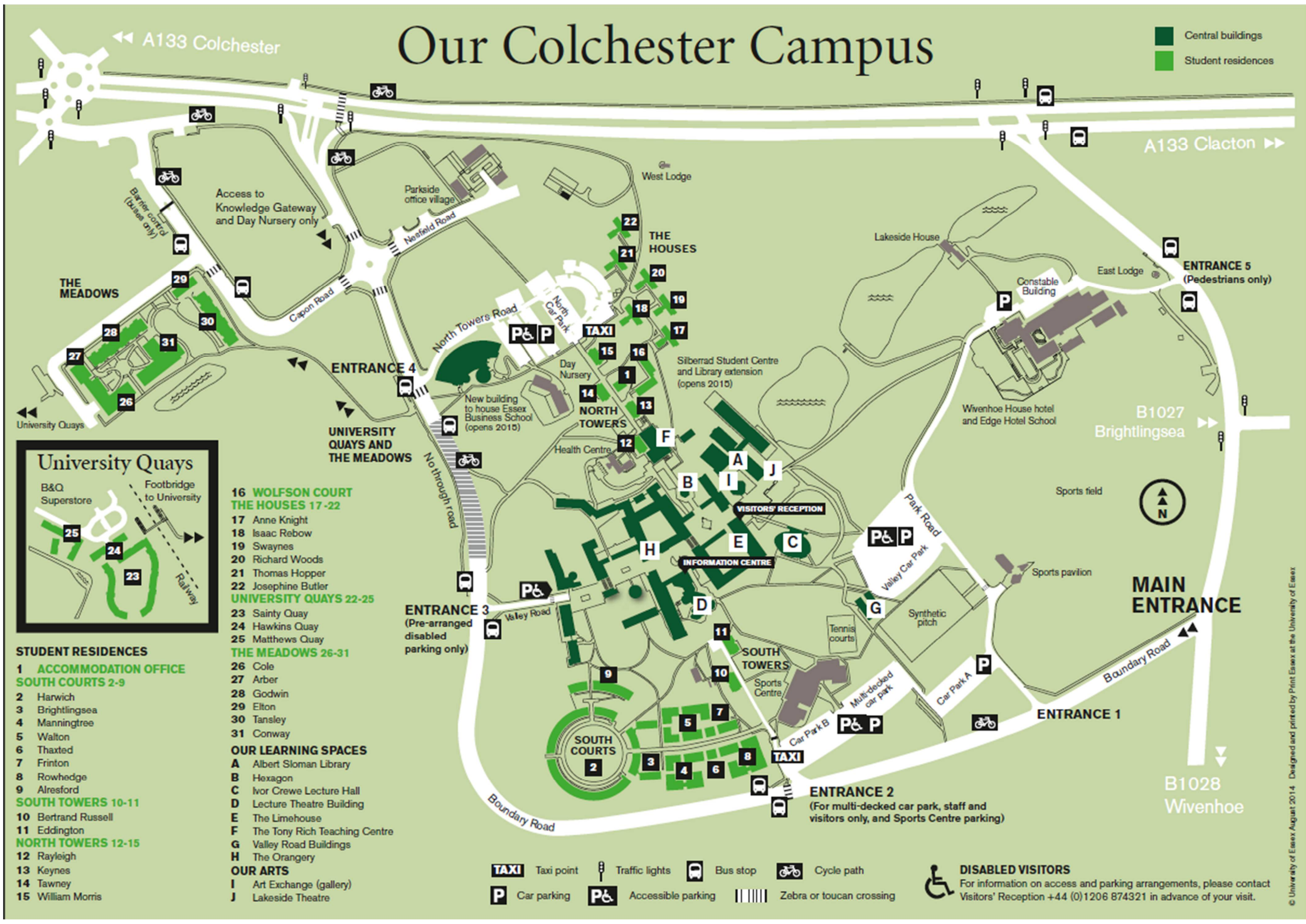
WE ARE ESSEX.

WE'RE ON THE SIDE OF **PEOPLE WITH GUTS** – REBELS WITH A CAUSE. WE'RE ABOUT PEOPLE WHO **LOVE TO LEARN HOW**, BUT **WANT TO CHALLENGE WHY**. BUT WHY DO WE HAVE TO STOP HERE? WHY CAN'T WE TAKE IT FURTHER, TO THE BIT WHERE IT REALLY GETS INTERESTING? WE'RE ABOUT THE PEOPLE WHO HUDDLE OUTSIDE A CLASS LONG AFTER IT'S FINISHED BECAUSE THERE'S MUCH **MORE TO BE SAID**, MORE ARGUMENTS TO BE HAD. WE'RE ABOUT PEOPLE WHO ARE BOLD ENOUGH TO **CHALLENGE INEQUALITY** AND THE STATUS QUO. PEOPLE WHO DON'T EXPECT THE WORLD TO CHANGE SIMPLY BECAUSE THEY LIKED A FACEBOOK STATUS OR NODDED WHEN SOMEONE ELSE SPOKE. AT ESSEX YOU'RE NOT JUST A STUDENT, **YOU'RE A MEMBER**, SOMEONE WITH GENUINE LICENCE TO SHAPE WHAT GOES ON AROUND YOU. TO US IT DOESN'T MATTER WHERE YOU'VE COME FROM. WE'RE INTERESTED IN HOW YOU WANT TO GROW AND **WHAT YOU WANT TO CHANGE**. WE'RE AFTER PEOPLE WHO WILL HELP US PUSH THE FRONTIERS OF KNOWLEDGE. **CHALLENGING CONVENTION** IS IN OUR DNA. ALL OF WHICH LEAVES YOU WITH A DECISION: ARE YOU GOING TO SIT AND WATCH THE WORLD GO BY? OR DO YOU HAVE THE **COURAGE AND ENERGY** TO SHAPE IT? WE'LL HELP YOU EXPLORE, QUESTION AND CREATE **POWERFUL IDEAS**. WE'LL INTRODUCE YOU TO PEOPLE FROM EVERY CORNER OF THE PLANET, A **GENUINELY GLOBAL COMMUNITY** THAT LIVES, WORKS AND PLAYS TOGETHER. IF YOU GIVE UP AT THE FIRST HURDLE, ESSEX ISN'T FOR YOU. IF YOU WANT TO BE SPOON-FED A DEGREE, ESSEX ISN'T FOR YOU. IF YOU ARE BRAVE ENOUGH TO HAVE IDEAS AND GENEROUS ENOUGH TO SHARE THEM,

WELCOME HOME.

Back page of Undergraduate Prospectus 2016, University of Essex

Appendix B: Campus and Accommodation Location



Source: www.essex.ac.uk

Appendix C: Demand for Higher Education over time

Demand for Higher Education over time

National Student Market Commentary

The Student Accommodation Sector is maturing and should no longer be regarded as an easy win. There are still many opportunities and the UK Higher Education sector remains strong, but land owners, operators and investors need to give careful consideration to individual markets and locations to ensure success.

Underlying Student Demand

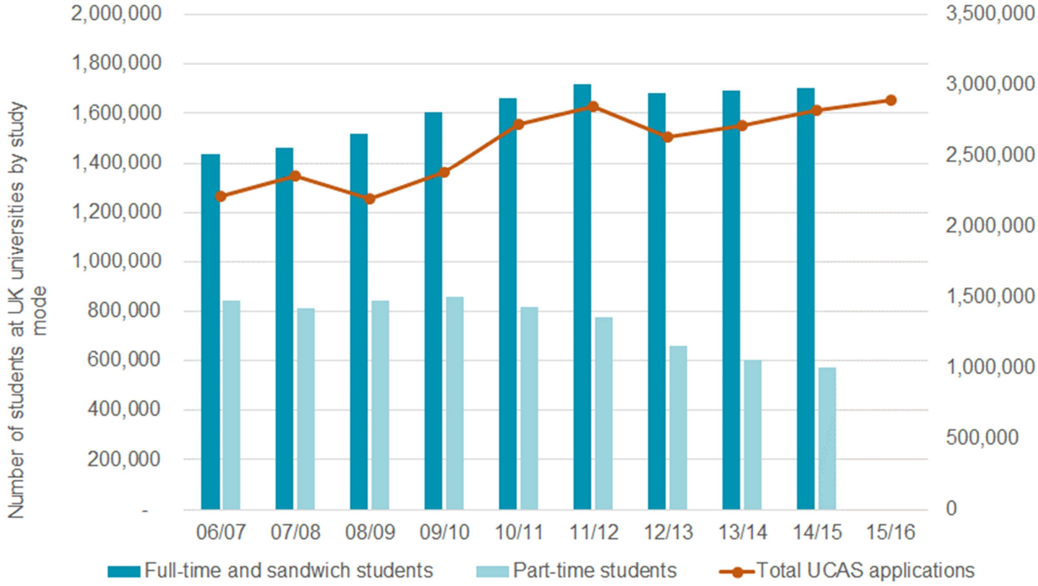
Based on the most recent 2014/15 HESA data, there is very positive evidence at undergraduate level that demand for HE has recovered after a dip in student numbers in 2012/13, when tuition fees of £9,000 were introduced at most universities. However, growth in student numbers has slowed down slightly in comparison to the previous year and is weaker than the levels experienced prior to the 2012/13 fee increase.

Full-time student numbers reached 1.697 million in 2014/15, up by 1% from 2012/13 and exceeding 2010/11 numbers. Full-time students constitute the core of the market and are the cohort that continues to grow. Cushman & Wakefield's understanding is that this has been driven by students taking the decision to go to university more seriously than ever before. Expectations are rising, and the questions about what "value for money" really looks like in the world of HE are coming to the fore.

Trends in Student Numbers and Applications at UK Universities

Looking at UCAS applications, demand for HE shows a positive trajectory over recent years, although growth in application numbers was lower in 2015 (2% year on year) compared to each of the previous two years (3% in 2013 and 4% in 2014). Based on applications, Cushman & Wakefield expect HESA student numbers for 2015 to have grown at a rate of between 0% and 1%. UCAS applications increased on average by 3% per year from 2012 to 2015. Early indications for 2016 are that application numbers are holding at the same level as 2015, which was the largest intake of undergraduates ever and, if true, will see universities naturally expanding in size.

Trends in Student Numbers and Applications 2006-2015



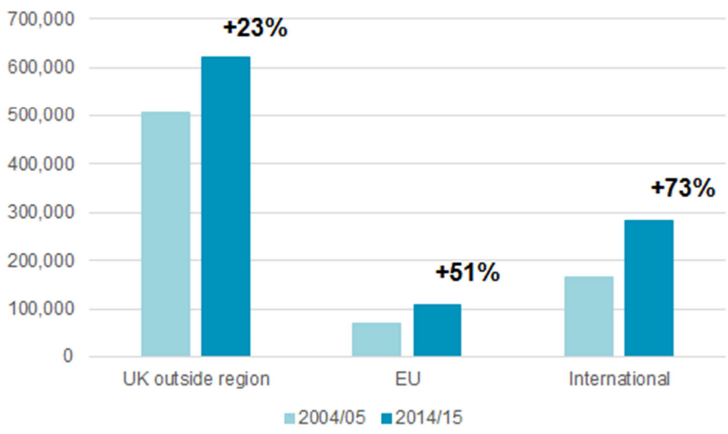
Source: HESA data 2006-2014, UCAS application data 2006-2015

Despite two tuition fee increases within a time span of just six years, full-time student numbers have not been profoundly affected to date. Interestingly and contrary to some expectations, increases in the cost of HE have resulted in more UK students studying away from their home region than ever before. In 2014/15, over 621,000 UK students studied at a university outside their domicile region, accounting for 48% of all UK students and reflecting an increase in numbers of 23% on 2004 figures.

This appears to be a result of a more direct decision to make a return on investment in education than ever before. Students are choosing to go to universities with better employability records and credibility in order to maximise their attractiveness in the labour market. Equally, students are choosing institutions more carefully in terms of the student experience, so that their time studying is enriching and enjoyable. Crucially, part of the investment in HE, alongside choosing the best possible university, now seems to extend to choosing a quality residential experience that will support their academic and social experience.

Overall, students on full-time courses studying outside their home region counted 1,013,000 in 2014/15 including EU and international students. Many UK universities have been successful in attracting increasing numbers of EU and international students, growing by 51% and 73% respectively from 2004/05 to 2014/15. This is very positive in terms of demand for PBSA as these student groups generally constitute the core demand pool for student accommodation. However, growth has slowed down over recent years for both EU and international student domiciles which is reflected in a 1% increase from 2013 to 2014 (down from 8% and 12% respectively in 2009).

Trends in Student Domiciles 2004-2014



Source: HESA data 2004-2014

University Competitiveness

Universities are operating in an increasingly competitive market. With the shift in financial sources towards tuition fee income and away from public funding, student recruitment has become an even more important strategic focus of university activity. With the cessation of student number controls in 2015, there are predicted to be around 100,000 additional university places by 2035. The UCAS undergraduate entry system has also been amended, with students now able to “trade up” and move within the entry system with greater ease. This means that university recruitment – a world that used to be stable and quota driven – is now becoming far less predictable.

With students looking to get to the best possible institution, and with more choice than ever, successful and fleet-of-foot universities are able to fulfil their strategic ambitions. However, this inevitably means that some institutions will be left behind. This has implications for the universities themselves, but also for those who invest in and around them.

In this new world, the universities who are likely to do best can bring together a whole host of positive attributes that can be demonstrated to students – and to their partners and stakeholders.

The demands on universities are greater than they have ever been. The quality and modernity of their academic and residential facilities, and a definable distinctive vision and ability to convert and please their students are all key in recruitment and securing outcomes. This has led to huge capital investment into academic and residential facilities on campus.

In general, long term demand for a highly qualified and skilled workforce as well as demonstrably better long term career outcomes and earnings potential for university graduates, will continue to be main drivers of demand for HE.

INDEX OF DEFINED TERMS

THE ISSUER

Uliving@Essex Issuerco PLC
Welken House
10-11 Charterhouse Square
London, EC1M 6EH

FINANCIAL GUARANTEE PROVIDERS

Assured Guaranty Municipal Corp.
1633 Broadway
New York, New York 10019
USA

Assured Guaranty (Europe) Ltd.
11th Floor, 6 Bevis Marks
London EC3A 7BA

BOND TRUSTEE

BNY Mellon Corporate Trustee Services Limited
One Canada Square
London
E14 5AL

SECURITY TRUSTEE

BNY Mellon Corporate Trustee Services Limited
One Canada Square
London
E14 5AL

PRINCIPAL PAYING AGENT AND PAYING AGENT

The Bank of New York Mellon, London Branch
One Canada Square
London
E14 5AL

IRISH LISTING AGENT

McCann FitzGerald Listing Services Limited
Riverside One
Sir John Rogerson's Quay
Dublin 2, Ireland

LEGAL ADVISORS

To the Manager, the Financial Guarantors, the Bond Trustee and the Security Trustee as to English law

Norton Rose Fulbright LLP
3 More London Riverside
London SE1 2AQ
United Kingdom

To the Issuer, ProjectCo, HoldCo as to English law

CMS Cameron McKenna LLP
Cannon Place, 78 Cannon Street
London EC4N 6AF
United Kingdom

AUDITORS

To AGE

PricewaterhouseCoopers LLP
7 More London Riverside
London
SE1 2RT

To AGM

PricewaterhouseCoopers LLP
300 Madison Avenue
New York, New York 10027
USA

To the Issuer, ProjectCo, and HoldCo

Grant Thornton UK LLP
Statutory Auditor & Chartered Accountants
Grant Thornton House
Melton Street
Euston Square
London
NW1 2EP