

STATUTORY-BASIS FINANCIAL STATEMENTS

Financial Guaranty Insurance Company  
September 30, 2019

# Financial Guaranty Insurance Company

## Statutory-Basis Financial Statements

September 30, 2019

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# Financial Guaranty Insurance Company

## Statutory-Basis Balance Sheets

(Dollars in Thousands, Except per Share Amounts)

	September 30, 2019	December 31, 2018
	(Unaudited)	
<b>Admitted assets</b>		
Bonds	\$ 2,071,897	\$ 1,955,077
Common stock	—	121,148
Common stock – investment in subsidiaries	33,200	33,200
Surplus notes	8,860	8,865
Short-term investments	—	750
Other invested assets	45,822	43,244
Receivable for securities sold	79	—
Cash and cash equivalents	79,420	41,173
Total cash and invested assets	2,239,278	2,203,457
Accrued investment income	19,244	19,446
Other assets	26	34
Federal income tax receivable	7,973	5,816
Reinsurance receivable	33	19
Receivable from parent and subsidiaries	464	718
Total admitted assets	\$ 2,267,018	\$ 2,229,490
<b>Liabilities and capital and surplus</b>		
Liabilities:		
Losses	\$ 1,736,166	\$ 1,717,795
Loss adjustment expenses	11,129	16,646
Ceded reinsurance premiums payable	1	1
Unearned premiums	36,829	39,343
Contingency reserves	386,063	365,355
Other liabilities	21,812	23,940
Payable for securities purchased	8,618	—
Federal and foreign income tax payable	—	10
Total liabilities	2,200,618	2,163,090
Capital and surplus:		
Common stock, par value \$1,500 per share; 10,000 shares authorized, issued, and outstanding	15,000	15,000
Redeemable preferred stock, par value \$1,000 per share; 3,000 shares authorized, issued and outstanding	300,000	300,000
Unassigned deficit	(248,600)	(248,600)
Total capital and surplus	66,400	66,400
Total liabilities and capital and surplus	\$ 2,267,018	\$ 2,229,490

See accompanying notes.

# Financial Guaranty Insurance Company

## Statutory-Basis Statements of Operations and Changes in Surplus (Unaudited) (Dollars in Thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Premiums earned	\$ 3,068	\$ 2,774	\$ 6,113	\$ 3,935
Losses incurred	(34,557)	(33,804)	(69,648)	(63,635)
Loss adjustment expenses released (incurred)	14	584	148	(2,143)
Other underwriting expenses	(6,299)	(5,691)	(19,653)	(18,488)
Ceding commission income	1	1	66	66
Underwriting loss	(37,773)	(36,136)	(82,974)	(80,265)
Net investment income	20,146	20,320	60,927	60,568
Net realized capital gains, net of tax expense of \$2,518 and \$7,594, and \$3,245 and \$5,793, for the three and nine months ended September 30, 2019 and 2018, respectively	17,784	12,208	36,880	21,791
Net investment gain	37,930	32,528	97,807	82,359
Other income (loss)	3,187	2,726	(2,343)	8,368
Income (loss) before all other federal income taxes	3,344	(882)	12,490	10,462
Federal income tax benefit	(3,236)	(4,415)	(9,751)	(9,839)
Net income	\$ 6,580	\$ 3,533	\$ 22,241	\$ 20,301
<b>Changes in surplus</b>				
Surplus as regards policyholders, beginning of period	\$ 66,400	\$ 66,400	\$ 66,400	\$ 66,400
Net income	6,580	3,533	22,241	20,301
Change in net unrealized capital gains, net of tax (benefit) expense of \$(92) and \$(354), and \$1,001 and \$1,045, for the three and nine months ended September 30, 2019 and 2018, respectively	(346)	3,766	(1,334)	3,931
Change in foreign exchange adjustment	(2)	—	—	1
Change in net deferred income tax	(810)	(526)	(2,511)	(3,357)
Change in non-admitted assets	769	1,566	2,312	4,577
Change in contingency reserves	(6,191)	(8,339)	(20,708)	(25,453)
Surplus as regards policyholders, end of period	\$ 66,400	\$ 66,400	\$ 66,400	\$ 66,400

See accompanying notes.

Financial Guaranty Insurance Company

Statutory-Basis Statements of Cash Flows

(Unaudited)

(Dollars in Thousands)

	Nine Months Ended September 30,	
	2019	2018
<b>Operations</b>		
Premiums collected, net of reinsurance	\$ 3,638	\$ 4,221
Losses paid, net	(51,277)	(168,996)
Loss adjustment expenses paid, net	(5,369)	(8,959)
Underwriting expenses paid	(21,937)	(21,661)
Ceding commission received	65	67
Net investment income received	67,033	68,806
Other income received	9,794	9,290
Federal and foreign income tax payments	(9)	—
Net cash provided by (used in) operations	1,938	(117,232)
<b>Investment activities</b>		
Proceeds from sales, maturities, or repayments of investments:		
Bonds	471,876	659,886
Common stock	135,559	25,000
Net gains (losses) on short-term investments	1	(9)
Surplus notes	—	544
Other invested assets	9,977	9,579
Miscellaneous proceeds	2,774	4,182
Total investment proceeds	620,187	699,182
Cost of investments acquired:		
Bonds	(566,122)	(591,344)
Common stock	—	(2,053)
Surplus notes	—	(601)
Other invested assets	(18,928)	(6,849)
Total investments acquired	(585,050)	(600,847)
Net cash provided by investment activities	35,137	98,335
<b>Financing and miscellaneous activities</b>		
Other cash provided	422	880
Net increase (decrease) in cash, cash equivalents and short-term investments	37,497	(18,017)
Cash, cash equivalents and short-term investments:		
Beginning of period	41,923	109,672
End of period	\$ 79,420	\$ 91,655

See accompanying notes.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements

September 30, 2019

### **1. Organization and Background**

Financial Guaranty Insurance Company (the “Company” or “FGIC”), a New York stock insurance corporation, is a wholly owned subsidiary of FGIC Corporation (“FGIC Corp.”), a Delaware corporation which emerged from a proceeding under Chapter 11 of the United States Bankruptcy Code on April 19, 2013.

FGIC previously issued financial guaranty insurance policies insuring public finance, structured finance and other obligations, but it is no longer engaged in the business of writing new insurance policies. FGIC operates in accordance with the terms and conditions set forth in the Rehabilitation Plan (defined below). FGIC’s primary regulator is the New York State Department of Financial Services (the “NYSDFS”). FGIC UK Limited (“FGIC UK”), a wholly owned United Kingdom insurance subsidiary of FGIC, previously issued financial guaranties covering public finance, structured finance and other obligations, but it is no longer engaged in the business of writing new financial guaranties. FGIC UK’s primary regulator is the UK Prudential Regulation Authority.

On June 28, 2012, the Supreme Court of the State of New York (the “Rehabilitation Court”) issued an order pursuant to Article 74 of the New York Insurance Law (the “NYIL”) placing FGIC in rehabilitation and appointing the Superintendent of Financial Services of the State of New York as FGIC’s rehabilitator.

On June 11, 2013, the Rehabilitation Court approved the First Amended Plan of Rehabilitation for FGIC, dated June 4, 2013, together with all exhibits and the plan supplement thereto (as the same may be amended from time to time, collectively, the “Rehabilitation Plan”) in an order issued pursuant to Article 74 of the NYIL. The Rehabilitation Plan became effective on August 19, 2013 (the “Effective Date”), whereupon FGIC’s rehabilitation proceeding terminated. By notice dated on the Effective Date, FGIC’s rehabilitator set the initial cash payment percentage (“CPP”) at 17%.

On the Effective Date, FGIC emerged from its rehabilitation proceeding as a solvent insurance company under the NYIL, with its policies restructured in a manner intended to ensure it remains solvent and the Rehabilitation Plan became the exclusive means for resolving and paying (i) all policy claims, whenever arising, (ii) all other claims arising during, or relating to, the period prior to the Effective Date and (iii) all equity interests in FGIC in existence as of the commencement date of FGIC’s rehabilitation proceeding (June 28, 2012), in each case other than claims (including policy claims) paid in full by FGIC prior to such date. Claims arising during or relating to the period on and after the Effective Date (other than policy claims) are not covered by the Rehabilitation Plan and will be resolved and paid by FGIC in the ordinary course of business.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 1. Organization and Background (continued)

As of the Effective Date, any and all policies in force as of the Effective Date (except for certain policies that were novated on that date) were automatically modified by the Rehabilitation Plan.

The Rehabilitation Plan, including the restructured policy terms attached to the Rehabilitation Plan as Exhibit B (the “Restructured Policy Terms”), supersedes any and all provisions of each policy that are inconsistent with the Rehabilitation Plan. FGIC is responsible for administering, reviewing, verifying, reconciling, objecting to, compromising or otherwise resolving all claims (including policy claims) not resolved prior to the Effective Date, in each case in compliance with the Rehabilitation Plan and any applicable guidelines the NYSDFS has issued or may issue to carry out the purposes and effects of the Rehabilitation Plan (“NYSDFS Guidelines”).

With respect to any policy claim permitted by FGIC, pursuant to the Rehabilitation Plan and the applicable policy (as modified by the Rehabilitation Plan), FGIC is obligated to pay in cash to the applicable policy payee only an upfront amount equal to the product of the then-existing CPP and the amount of such permitted policy claim (subject to any setoff rights FGIC may have). The portion of such permitted policy claim not paid or deemed to be paid by FGIC generally comprises a deferred payment obligation (“DPO”) with respect to the applicable policy. The DPO with respect to any policy generally represents the aggregate amount of all permitted policy claims under such policy minus the aggregate amount paid, or deemed to be paid, in cash by FGIC with respect to such policy (other than DPO Accretion, defined below) from and after the Effective Date, subject to further adjustments as provided in the Rehabilitation Plan. From and after the Effective Date, each policy with an outstanding DPO accrues an amount (“DPO Accretion”) as described in Note 2, Significant Accounting Policies, under the sub-heading “Loss Reserves – DPO Accretion.” The DPO for any policy and any related DPO Accretion shall only be payable by FGIC when, if and to the extent provided in the Restructured Policy Terms and the Rehabilitation Plan. In the absence of an upward adjustment of the CPP, FGIC shall have no obligation to pay any portion of any DPO or DPO Accretion.

FGIC is required to re-evaluate the CPP (at least annually) pursuant to the procedures set forth in the Restructured Policy Terms to determine whether the CPP should remain the same or be adjusted upward or downward (each, a “CPP Revaluation”). All CPP Revaluations require review and approval by the board of directors of FGIC, and any change in the CPP (among other things) requires the approval of the NYSDFS. In October 2019, in connection with FGIC’s annual CPP Revaluation for 2019, the NYSDFS approved an upward adjustment to the CPP from 38.5% to 43.5% (the “2019 CPP Upward Adjustment”). In August 2018, in connection with FGIC’s annual CPP Revaluation for 2018, the NYSDFS approved an upward adjustment to the CPP from 33% to 38.5%.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### **1. Organization and Background (continued)**

The percentage of permitted policy claims that FGIC ultimately pays in cash in accordance with the Rehabilitation Plan, and the timing of any such payments, are subject to various factors and the outcome of future events, including the performance of FGIC's insured and investment portfolios and the results of FGIC's litigation and other loss mitigation efforts, and no assurance can be given with respect to the amount of any such percentage or the timing of any such payments. Based on the magnitude of FGIC's accrued and projected policy claims, while the CPP may further increase over time, FGIC expects to make payments in cash pursuant to the Rehabilitation Plan of only a fractional portion of its permitted policy claims and it does not expect to make any payments pursuant to the Rehabilitation Plan with respect to non-policy claims or equity interests.

References to and descriptions of provisions of the Restructured Policy Terms, the Rehabilitation Plan (and related agreements) and orders of the Rehabilitation Court included in these financial statements are merely summaries thereof, and do not contain all information necessary to fully understand such provisions and orders. Please refer to the specific terms, requirements and conditions of the Restructured Policy Terms, the Rehabilitation Plan (and related agreements) and orders of the Rehabilitation Court for a full understanding thereof, which in all cases shall govern, rather than any summary description contained in these financial statements.

### **2. Significant Accounting Policies**

The accompanying financial statements of the Company have been prepared in conformity with statutory accounting practices prescribed or permitted by the NYSDFS as well as those accounting practices detailed in NYSDFS Guidelines, as described below ("SAP"). The preparation of financial statements in conformity with SAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates, and those differences could be material. Operating results for the three and nine months ended September 30, 2019 are not necessarily indicative of results that may be expected for the year ending December 31, 2019. These unaudited interim financial statements should be read in conjunction with the audited Statutory Basis Financial Statements for the year ended December 31, 2018, including the accompanying notes. The December 31, 2018 balance sheet was derived from audited financial statements but does not include all disclosures required by SAP for annual periods.

SAP differs in some respects from accounting principles generally accepted in the United States ("GAAP"). The effects of the variances from GAAP on the accompanying statutory-basis financial statements have not been determined as of and for the three and nine months ended



# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### **.2. Significant Accounting Policies (continued)**

September 30, 2019 and 2018, but are presumed to be material. Significant accounting policies and variances from GAAP, where applicable, are as follows:

#### **NYSDFS Guidelines**

Pursuant to the provisions of the Rehabilitation Plan, the NYSDFS has issued NYSDFS Guidelines that define certain accounting practices for FGIC for reporting periods ending on or after the Effective Date. In accordance with such NYSDFS Guidelines, for reporting periods ending on or after the Effective Date, FGIC records loss reserves at the applicable reporting date in an amount equal to the excess of (i) the amount of FGIC's admitted assets minus FGIC's minimum required statutory surplus to policyholders at the reporting date (the "Minimum Surplus Amount," currently \$66.4 million) over (ii) the sum of FGIC's statutory reserves excluding loss reserves (e.g., unearned premiums, contingency reserves, loss adjustment expense reserves) and other liabilities. In accordance with such NYSDFS Guidelines, the loss reserve amount comprises the total amount of (i) the sum, net of reinsurance, of (x) the total amount of all policy claims submitted to FGIC in accordance with the Rehabilitation Plan that are unpaid (excluding any portions of such policy claims that are being disputed by FGIC) and (y) the net present value of the total amount of all policy claims that the Company expects to receive in the future in accordance with the Rehabilitation Plan (using the prescribed statutory discount rate which is based on the average rate of return on FGIC's admitted assets) (such sum is referred to as the "Claims Reserve"), (ii) the DPO for all policies at such reporting date and (iii) the DPO Accretion for all policies at such reporting date, minus an adjustment (the "Policy Revision Adjustment") in an amount that will permit FGIC to report a surplus to policyholders at such reporting date equal to the Minimum Surplus Amount (See also Note 6, Loss Reserves).

#### **Cash and Cash Equivalents**

The Company considers all bank deposits and all certificates of deposit with maturities of one year or less at the date of purchase to be cash. The Company considers highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less to be cash equivalents. Cash and cash equivalents other than money market mutual funds are carried at cost, which approximates fair value. Money market mutual funds are recorded at fair value. Changes in carrying values of money market mutual funds are recorded as changes in unrealized capital gains/losses, a component of surplus.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 2. Significant Accounting Policies (continued)

Under GAAP, these securities are adjusted to net asset value and included in cash and cash equivalents.

#### Investments

Investments are valued in accordance with the requirements of the National Association of Insurance Commissioners (“NAIC”).

Bonds with an NAIC designation of 1 or 2 determined by the Securities Valuation Office (“SVO”) are stated at amortized cost, with premiums and discounts amortized to net income using the effective interest method over the remaining term of the securities. Bonds with an NAIC designation of 3 through 6 determined by the SVO are stated at the lower of amortized cost or fair value. Under GAAP, bonds are designated at purchase as either held-to-maturity, available-for-sale or trading. Bonds designated as held-to-maturity are reported at amortized cost. Bonds designated as available-for-sale are reported at fair value with unrealized gains and losses reported in stockholders’ equity, net of tax. Bonds designated as trading are reported at fair value with unrealized gains and losses reported in net investment income.

Common stocks include shares of mutual funds that invest principally in common stocks. Common stocks (excluding investments in common stock of subsidiary, controlled and affiliated (“SCA”) entities (which are included in the balance sheet as common stock – investment in subsidiaries)) are recorded at fair value. Changes in carrying values are recorded as changes in unrealized capital gains/losses, a component of surplus, net of tax. Dividends are reported in net investment income. Under GAAP, investments in such common stocks are designated at purchase as either available-for-sale or trading. Common stocks designated as available-for-sale are reported at fair value with unrealized gains or losses reported as a component of stockholders’ equity, net of tax. Common stocks designated as trading are reported at fair value with unrealized gains and losses reported in net investment income.

Under SAP, investments in common stock of SCA entities are recorded based on the audited underlying equity adjusted to a statutory basis to the extent admissible under Statement of Statutory Accounting Principles (“SSAP”) 97, *Investments in Subsidiary, Controlled, and Affiliated Entities, A Replacement of SSAP No. 88* and subject to applicable limitations under the NYIL. One such limit restricts the amount reported as investments in common stock of SCA entities to 50% of the Company’s statutory surplus to policyholders. Under SAP, the reporting entity cannot admit as an asset the investment in an SCA entity for which audited financial statements are not prepared. Changes in the values of SCA entities are recorded as unrealized gains

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### **2. Significant Accounting Policies (continued)**

or losses and reported as a component of unassigned deficit. Under GAAP, SCA entities meeting certain criteria are consolidated with the Company.

Surplus notes with an NAIC designation equivalent of 1 or 2 as designated by an NAIC credit rating provider are stated at amortized cost, with premiums and discounts amortized to net income using the effective interest method over the remaining term of the notes. All other surplus notes are stated at the lower of amortized cost or fair value. If the issuer is subject to any order of liquidation, conservation, rehabilitation or any company action level event based on its risk-based capital, the surplus notes are non-admitted until such regulatory action ends. Under GAAP, these notes are stated at fair value.

Short-term investments are stated at amortized cost. Realized gains and losses on the sale of short-term investments are determined based on the specific identification method and are reflected in the determination of net income.

Included within bonds are loan-backed and structured securities (e.g., asset-backed and mortgage-backed securities), which are valued at amortized cost using the interest method, including anticipated prepayments. Prepayment assumptions are obtained from dealer surveys or internal estimates and are based on the current interest rate and economic environment. All such securities are adjusted for the effects of changes in prepayment assumptions on the related accretion of discount or amortization of premium of such securities using the retrospective method.

### **Other-Than-Temporary Impairments**

For all investments in bonds (including loan-backed and structured securities) acquired prior to October 1, 2015, a decline in the fair value of any such security below its cost basis as of a reporting date is automatically treated as an other-than-temporary impairment (“OTTI”).

FGIC conducts an impairment review no less than quarterly for all investments in bonds (including loan-backed and structured securities) acquired on or after October 1, 2015, and for all investments in surplus notes and common stocks, in each case which have fair values lower than their respective cost bases as of the review date. The analysis of a security’s decline in value is performed at the lot level. FGIC first determines whether it intends to sell the security. For loan-backed and structured securities, FGIC also determines whether it is more likely than not that it will be unable to hold the security for a period of time to recover its amortized cost basis. The impairment for any security that FGIC determines it intends to sell or, in the case of loan-backed and structured

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

securities, it is more likely than not that it will be unable to hold for a period of time to recover its amortized cost basis, is considered to be an OTTI.

For bonds (other than loan-backed and structured securities), surplus notes and common stocks that FGIC does not intend to sell, FGIC conducts a quantitative and qualitative impairment review that requires management to make numerous judgments, estimates and assumptions concerning relevant factors, such as (i) the magnitude and duration of the impairment, and (ii) possible explanations for the impairment (e.g., general interest rate, credit spread, market index movements; issuer-specific developments such as material negative credit events (e.g., actual or threatened bankruptcy or similar proceedings or debt restructurings); and security-specific developments such as existing or projected monetary and material non-monetary defaults and credit rating downgrades). Based on this review, FGIC determines whether the decline in fair value for any such security is temporary or an OTTI, with the decline in fair value for any such security that does not satisfy the specified quantitative or qualitative criteria treated as temporary.

If the decline in fair value for any such bond or surplus note is determined to be temporary, an unrealized loss is not recorded. If the decline in fair value for any common stock is determined to be temporary, FGIC records it as an unrealized loss, as common stocks are recorded at fair value. If the decline in fair value for any such bond, surplus note or common stock is treated as or determined to be an OTTI, the carrying value of such security is reduced to fair value as of the reporting date, establishing a new cost basis, with a charge to realized loss at the reporting date. Such realized losses are recorded through income and the new cost basis is not adjusted for subsequent recoveries in fair value. Amortization of any premium or discount from the date bonds or surplus notes are written down is based on the new cost basis.

For loan-backed and structured securities that the Company does not intend to sell and has not determined that it is unable to hold until recovery of their amortized cost bases, the Company estimates the cash flows expected to be collected over the term of each security as of the review date and calculates the present value of those expected cash flows using a discount rate equal to the original effective yield of the security, or in the case of floating rate securities, the then-current coupon. If the present value of future expected cash flows is less than the amortized cost basis of the security, the carrying value of such security is reduced to such present value as of the reporting date, establishing a new cost basis, with a charge to realized loss at such date for the entire reduction. Such realized losses are recorded through income and the new cost basis is not adjusted for subsequent recoveries in fair value. Amortization of premium or discount, as applicable, from the date the security is written down is based on the new cost basis.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

##### **Other Invested Assets**

Other invested assets include FGIC-insured securities purchased by FGIC and securities or other non-cash assets purchased, received or recovered by FGIC, in connection with its loss mitigation efforts.

For FGIC-insured securities purchased in connection with loss mitigation efforts, the value of the security comprises two components: (i) the portion representing the value of FGIC's insurance (the "Insurance Portion") and (ii) the remaining portion representing the value of the security without giving credit for FGIC's insurance (the "Non-Insurance Portion"). For each security, the Company estimates the value of the Insurance Portion using internally developed formulas, with the remainder of the value being the Non-Insurance Portion. The Insurance Portion is included in losses incurred and is deducted from the amortized cost and fair value of these FGIC-insured securities at the time of purchase and at each reporting date, respectively. For each FGIC-insured security purchased in connection with loss mitigation efforts, FGIC reduces the related Claims Reserve at each reporting date on a pro rata basis for the ratable portion of the securities purchased by FGIC. The reduction in Claims Reserves is also included in losses incurred.

The remaining Non-Insurance Portion of each purchased security is classified as other invested assets in the balance sheet and is subject to impairment analysis at each subsequent balance sheet date. Realized gains or losses and OTTI on the Non-Insurance Portion of these securities are recorded in other income. The amortized cost and fair value of these securities are shown excluding the Insurance Portion. Under SAP, these securities are carried at the lower of amortized cost or fair value as these securities have an NAIC designation of 3 through 6. Under GAAP, these securities are carried at fair value.

For securities or other non-cash assets purchased, received or recovered by FGIC in connection with its loss mitigation efforts, FGIC records the asset at the lower of cost or fair value at acquisition. FGIC generally does not consider the payment of claims to be included in the determination of the cost basis of assets purchased, received or recovered in connection with such claims. Realized gains or losses and OTTI on these assets are recorded in other income. Under SAP, these assets are carried at the lower of amortized cost or fair value. Under GAAP, these securities are carried at fair value.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

##### **Fair Value Measurements**

The Company discloses the fair value of its financial instruments in accordance with SSAP 100R, *Fair Value – Revised* (“SSAP 100R”), which requires the use of a fair value hierarchy with the highest priority given to quoted prices in active markets. The general disclosure requirements are for those items measured and reported at fair value in the balance sheet. Securities that are reported at amortized cost, but for which amortized cost equals fair value (such as a bond with a recognized OTTI on the reporting date) would not be included in the disclosures. SSAP 100R also requires certain disclosures of fair value measurements and valuation techniques, where practicable to determine, for financial instruments not carried at fair value in the balance sheet. SSAP 100R does not require companies to distinguish between recurring and non-recurring fair value measurements, which is required under GAAP.

##### **Premium Revenue Recognition**

For SAP, premiums collected in a single payment at policy inception are generally earned in proportion to the scheduled principal and interest payments over the legal lives of the insured bonds. Premiums collected periodically are reflected in income pro rata over the period covered by the premium payment. Under GAAP, premiums are earned in proportion to the amount of insurance protection provided over the expected life for homogeneous pools and over the legal life for non-homogeneous pools of policies. Ceded premiums are earned in a manner consistent with the underlying policies. Under SAP, the liability for unearned premiums is reflected net of reinsurance. Under GAAP, ceded unearned premiums are reported as an asset. When an obligation insured by the Company is refunded prior to the end of the expected policy coverage period, any remaining unearned premium is recognized at that time. A refunding occurs when an insured obligation is repaid or retired in full or legally defeased.

##### **Non-Admitted Assets**

Certain assets are charged directly against surplus but are reflected as assets under GAAP. Such assets principally include adjusted gross deferred tax assets and property and equipment.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

##### **Loss Reserves**

Loss reserves comprise the total amount of (i) the Claims Reserve, (ii) the DPO for all policies, and (iii) the DPO Accretion for all policies, minus the Policy Revision Adjustment. The Policy Revision Adjustment is prescribed by NYSDFS Guidelines and reflects the reduction in the loss reserve components necessary to reflect a Minimum Surplus Amount of \$66.4 million (see “NYSDFS Guidelines” above). Under GAAP, unpaid losses are reported on a gross basis (i.e., before reinsurance), and are discounted based on the risk-free rate for the anticipated shortfall in excess of the related unearned premium revenue, and the Policy Revision Adjustment is not recognized. The Company’s loss reserves are disclosed in Note 6, Loss Reserves. The Company’s losses incurred (released) for any reporting period equal the sum of the total Claims Reserve incurred (released), DPO Accretion for the period, and decreases (increases) in the Policy Reserve Adjustment.

##### *Claims Reserve*

The Claims Reserve is calculated on a policy-by-policy basis, net of reinsurance, as of the reporting date for each policy for which a payment default on an underlying insured obligation has occurred or is probable and the loss can be reasonably estimated. The Claims Reserve is determined for each policy using internally developed cash flow projection models or other methods for estimating losses and recoveries, calculated on a net present value basis using FGIC’s prescribed statutory discount rate. The Claims Reserve represents the total undisputed amount of all policy claims submitted to the Company that have not yet been permitted and paid (or deemed paid) by the Company in accordance with the Rehabilitation Plan, plus an estimate of the total amount of policy claims that the Company expects to receive in the future, less an estimate of the total amount that the Company expects to recover in the future in respect of policy claims paid (or deemed paid) by the Company prior to such recovery. The Company reduces the Claims Reserve to give effect to FGIC-insured securities purchased by FGIC (or for which FGIC has effectively stripped its insurance) in connection with loss mitigation efforts. The Company may increase the Claims Reserve to reflect potential obligations it may have under the Rehabilitation Plan in respect of certain cash reimbursements it has received.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

##### *DPO*

When FGIC pays (or is deemed to have paid) in cash the CPP of a permitted policy claim, the remaining unpaid balance of such permitted policy claim is added to the DPO under the related policy.

If, as a result of any CPP Revaluation, the CPP is adjusted upward, FGIC is obligated to pay the applicable policy payee in respect of the DPO under each policy an amount, determined in accordance with the Rehabilitation Plan, to true up the amounts of cash previously paid (or deemed to have been paid) by FGIC in respect of permitted policy claims paid at the prior CPP, which payment will generally reduce the DPO by an equal amount.

FGIC does not reduce the DPO or DPO Accretion balance recorded under any policy to give effect to FGIC-insured securities purchased by FGIC (or for which FGIC has effectively stripped its insurance) in connection with loss mitigation efforts. In the event of any subsequent CPP increase, FGIC, as the holder of such securities or stripped portions, would be entitled to receive a ratable portion of the related DPO and DPO Accretion payments payable under such policy.

##### *DPO Accretion*

Under the Restructured Policy Terms, each policy with an outstanding DPO accrues DPO Accretion in accordance with the Rehabilitation Plan based on such DPO at a rate of 3% per annum (on a daily basis on the basis of a 365-day year). DPO Accretion is calculated using the DPO with respect to the applicable policy as of the preceding June 30 or, with respect to the first year in which there is a DPO under such policy and until the next June 30, the first day on or after the Effective Date on which the DPO exists (the “First Payment Date”). DPO Accretion for any policy with a DPO commences on the First Payment Date for such policy and continues until such time (if ever) as the DPO for such policy is permanently reduced to zero. All DPO Accretion is calculated on a simple basis rather than a compound basis (i.e., no DPO Accretion accrues based on accumulated DPO Accretion). No DPO Accretion is added to a DPO, but is recorded separately. If, as a result of any CPP Revaluation, the CPP is adjusted upward, FGIC will pay in cash to the applicable policy payee a portion of the DPO Accretion under each policy having a DPO in an amount determined in accordance with the Rehabilitation Plan, which will reduce the DPO Accretion balance.



## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

##### **Loss Adjustment Expense Reserve**

A reserve for loss adjustment expense is recorded as a liability on the balance sheet. The loss adjustment expense reserve represents management's best estimate of the ultimate future net cost, determined using internally developed estimates, of the efforts involved in managing and mitigating existing and future policy claims. Such loss adjustment expense reserve is not subject to a Policy Revision Adjustment. The Company's loss adjustment expense reserve is disclosed in Note 7, Loss Adjustment Expense Reserve.

##### **Contingency Reserves**

Contingency reserves are computed on the basis of statutory requirements for the security of all policyholders, regardless of whether loss contingencies actually exist. The Company establishes contingency reserves in accordance with the NYIL, which is consistent with the requirements of SSAP 60, *Financial Guaranty Insurance*. Changes in the contingency reserve are charged directly to surplus. Under GAAP, contingency reserves are not required.

During 2018, the Company was granted permission by the NYSDFS to decrease contingency reserves by \$2.8 million.

##### **Federal Income Taxes**

Deferred tax assets and liabilities are recognized to reflect the tax impact attributable to temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases.

Deferred tax assets and liabilities are measured using statutory tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled and are recorded as a component of surplus. Under SAP and GAAP, a valuation allowance is established for deferred tax assets that are not expected to be realized. Under SAP, a net deferred tax asset is subject to limitations and may be non-admitted.

##### **Reinsurance**

A liability is recorded for uncollateralized amounts due from unauthorized reinsurers. Changes in this liability are charged or credited directly to unassigned surplus. Amounts due from unauthorized reinsurers that are secured by letters of credit or trust agreements are not included in

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### **2. Significant Accounting Policies (continued)**

this liability. Under GAAP, an allowance for amounts deemed uncollectible would be established through a charge to earnings.

Ceded loss reserves are calculated as reductions of the related gross Claims Reserves rather than assets, as would be required under GAAP. Prospective ceded losses are accounted for on a basis consistent with that used in accounting for the original policies issued, the terms of the reinsurance contracts, and the terms of the Rehabilitation Plan, which provides that payments are due in full from reinsurers with respect to any permitted policy claims covered by the reinsurance without regard to (i) the timing or amount of any cash payment made by FGIC on the underlying claims, (ii) the modification pursuant to the Rehabilitation Plan of FGIC's obligations to pay such permitted policy claims in cash or (iii) any language in the applicable reinsurance agreements that would contradict this result. The net Claims Reserve amount is reduced to give effect to such reinsurance. Ceded loss adjustment expense reserves and unearned premiums ceded to reinsurers have been reported as reductions of the related reserves rather than as assets, as would be required under GAAP. Prospective reinsurance premiums and loss adjustment expenses are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

### **Consolidation**

The accounts and operations of the Company's subsidiaries are not consolidated with the accounts and operations of the Company, as would be required under GAAP.

As part of its structured finance business, the Company may have insured debt obligations or certificates issued by special purpose entities that could be considered variable interest entities ("VIE"). The Company does not consolidate the assets and liabilities of a VIE. Under GAAP, the Company would be required to consolidate the assets and liabilities of a VIE if the Company were to determine that it was the primary beneficiary because it directs significant activities of and holds an economic interest in the entity.

### **Statements of Cash Flow**

The statutory-basis statements of cash flow are presented in a specified format, which differs from the format prescribed under GAAP. Cash, cash equivalents, and short-term investments in the statements of cash flow represent cash balances and investments with initial maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents includes cash balances and investments with initial maturities of three months or less.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

##### **Comprehensive Income**

Comprehensive income is not determined under SAP.

##### **Property and Equipment**

Property and equipment consists of office furniture, fixtures, computer equipment and software that are non-admitted assets under SAP. Under GAAP, these assets are reported at cost less accumulated depreciation.

##### **Reclassifications**

Certain 2018 amounts in the Company's statutory-basis financial statements have been reclassified to conform to the 2019 statutory-basis financial statement presentation.

#### **3. Fair Value Measurements**

SSAP 100R specifies a fair value hierarchy 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 the Company's assumptions about market participants' assumptions based on the best information available in the circumstances. The fair value hierarchy prioritizes model inputs into three broad levels: quoted prices for identical instruments in active markets are Level 1 inputs; quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets are Level 2 inputs; and model-driven valuations in which one or more significant inputs or significant value drivers are unobservable are Level 3 inputs.

Transfers among Levels 1, 2 and 3 are recognized at the end of the period in which the transfer occurs. The Company reviews the classification of financial instruments in Levels 1, 2 and 3 quarterly to determine whether a transfer is necessary. There have been no transfers into or out of Levels 1, 2 or 3 during the period.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 3. Fair Value Measurements (continued)

The fair values of the Company's admitted investments in bonds, surplus notes, common stocks, other invested assets, short-term investments and cash equivalents by level, and their related admitted values, are as follows:

	Level 1	Level 2	Level 3	Admitted Value
	<i>(In Thousands)</i>			
<b>September 30, 2019</b>				
Bonds:				
Obligations of states and political subdivisions	\$ —	\$ 191,064	\$ —	\$ 163,574
Loan-backed and structured securities	—	587,116	—	576,035
Obligations of the U.S. government and its agencies and instrumentalities	—	108,496	—	97,265
Corporate obligations	—	1,323,399	—	1,235,023
Total bonds	—	2,210,075	—	2,071,897
Surplus notes	—	10,598	—	8,860
Common stocks	—	—	—	—
Other invested assets	—	—	80,548	45,822
Short-term investments	—	—	—	—
Cash equivalents	—	70,458	—	70,458
Total	\$ —	\$ 2,291,131	\$ 80,548	\$ 2,197,037

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 3. Fair Value Measurements (continued)

	Level 1	Level 2	Level 3	Admitted Value
	<i>(In Thousands)</i>			
<b>December 31, 2018</b>				
Bonds:				
Obligations of states and political subdivisions	\$ —	\$ 233,391	\$ —	\$ 220,124
Loan-backed and structured securities	—	390,759	—	398,855
Obligations of the U.S. government and its agencies and instrumentalities	—	204,342	—	205,577
Corporate obligations	—	1,114,795	—	1,130,521
Total bonds	—	1,943,287	—	1,955,077
Surplus notes	—	8,840	—	8,865
Common stocks	121,148	—	—	121,148
Other invested assets	—	—	72,324	43,244
Short-term investments	—	750	—	750
Cash equivalents	—	30,717	—	30,717
Total	\$ 121,148	\$ 1,983,594	\$ 72,324	\$ 2,159,801

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 4. Investments

The amortized cost and fair value of the Company's admitted investments in bonds, surplus notes, common stocks, other invested assets, short-term investments and cash equivalents are as follows:

	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
	<i>(In Thousands)</i>			
<b>September 30, 2019</b>				
Bonds:				
Obligations of states and political subdivisions	\$ 163,574	\$ 27,490	\$ —	\$ 191,064
Loan-backed and structured securities	576,035	11,935	(854)	587,116
Obligations of the U.S. government and its agencies and instrumentalities	97,265	11,231	—	108,496
Corporate obligations	1,235,023	88,580	(204)	1,323,399
Total bonds	2,071,897	139,236	(1,058)	2,210,075
Surplus notes	8,860	1,738	—	10,598
Common stocks	—	—	—	—
Other invested assets	45,822	34,726	—	80,548
Short-term investments	—	—	—	—
Cash equivalents	70,458	—	—	70,458
Total	\$ 2,197,037	\$ 175,700	\$ (1,058)	\$ 2,371,679

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 4. Investments (continued)

	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Fair Value
<i>(In Thousands)</i>				
<b>December 31, 2018</b>				
Bonds:				
Obligations of states and political subdivisions	\$ 220,124	\$ 14,728	\$ (1,461)	\$ 233,391
Loan-backed and structured securities	398,855	1,379	(9,475)	390,759
Obligations of the U.S. government and its agencies and instrumentalities	205,577	3,400	(4,635)	204,342
Corporate obligations	1,130,521	9,821	(25,547)	1,114,795
Total bonds	1,955,077	29,328	(41,118)	1,943,287
Surplus notes	8,865	—	(25)	8,840
Common stocks	114,739	6,740	(331)	121,148
Other invested assets	43,244	29,080	—	72,324
Short-term investments	750	—	—	750
Cash equivalents	30,717	—	—	30,717
Total	<u>\$ 2,153,392</u>	<u>\$ 65,148</u>	<u>\$ (41,474)</u>	<u>\$ 2,177,066</u>

The Company has recorded OTTI of \$0.0 million and \$1.0 million, and \$2.4 million and \$5.5 million, on certain bonds for the three and nine months ended September 30, 2019 and 2018, respectively. OTTI on bonds is included in “Net realized capital gains or losses net of tax” in the statutory-basis statements of operations and represents the difference between the cost bases of these securities and their fair values (or, in the case of loan-backed and structured securities, the present value of expected cash flows) at the reporting date. The Company has recorded OTTI of \$0.2 million and \$12.1 million, and \$0.6 million and \$1.0 million, on other invested assets for the three and nine months ended September 30, 2019 and 2018, respectively. OTTI on other invested assets is included in “Other income” in the statutory-basis statements of operations and represents the difference between the cost bases of these securities and their fair values at the reporting date.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 4. Investments (continued)

In accordance with SSAP 43R, the Company is required to categorize its OTTI on loan-backed and structured securities based upon the reason for which the Company recognized an OTTI. The following summarizes those securities held at September 30, 2019 and 2018 for which an OTTI was recorded during the nine months ended September 30, 2019 and 2018:

	<b>Nine Months Ended September 30,</b>	
	<b>2019</b>	<b>2018</b>
	<i>(In Thousands)</i>	
Intent to sell	\$ 120	\$ 619
Inability to retain the investment in the security for a period of time sufficient to recover the amortized cost basis	—	—
Present value of the cash flows expected to be collected is less than the amortized cost basis of the security	—	1,207
Total OTTI on loan-backed and structured securities	<u>\$ 120</u>	<u>\$ 1,826</u>

The amortized cost and fair value of investments in bonds (including loan-backed and structured securities) at September 30, 2019, by contractual maturity date, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	<b>Amortized Cost</b>	<b>Fair Value</b>
	<i>(In Thousands)</i>	
Due in one year	\$ 17,448	\$ 17,564
Due after one through five years	548,903	568,882
Due after five years through ten years	408,995	433,919
Due after ten years	520,516	602,594
Loan-backed and structured securities	576,035	587,116
Total	<u>\$ 2,071,897</u>	<u>\$ 2,210,075</u>



# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 4. Investments (continued)

The amortized cost, fair value and unrealized holding loss for bonds, surplus notes, common stocks and short-term investments for which fair value declined and remained below amortized cost at September 30, 2019 and 2018 were as follows:

	Less Than 12 Months			Greater Than 12 Months		
	Amortized Cost	Fair Value	Unrealized Holding Loss	Amortized Cost	Fair Value	Unrealized Holding Loss
	<i>(In Thousands)</i>					
<b>September 30, 2019</b>						
Bonds:						
Obligations of states and political subdivisions	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Loan-backed and structured securities	<b>52,067</b>	<b>51,719</b>	<b>(348)</b>	<b>67,406</b>	<b>66,900</b>	<b>(506)</b>
Obligations of the U.S. government and its agencies and instrumentalities	—	—	—	—	—	—
Corporate obligations	<b>16,690</b>	<b>16,486</b>	<b>(204)</b>	—	—	—
Total bonds	<b>\$ 68,757</b>	<b>\$ 68,205</b>	<b>\$ (552)</b>	<b>\$ 67,406</b>	<b>\$ 66,900</b>	<b>\$ (506)</b>
Surplus notes	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Common stocks	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Short-term investments	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 4. Investments (continued)

	Less Than 12 Months			Greater Than 12 Months		
	Amortized Cost	Fair Value	Unrealized Holding Loss	Amortized Cost	Fair Value	Unrealized Holding Loss
<i>(In Thousands)</i>						
<b>September 30, 2018</b>						
Bonds:						
Obligations of states and political subdivisions	\$ 55,279	\$ 54,151	\$ (1,128)	\$ 9,609	\$ 8,402	\$ (1,207)
Loan-backed and structured securities	163,293	160,712	(2,581)	152,592	143,735	(8,857)
Obligations of the U.S. government and its agencies and instrumentalities	124,816	123,381	(1,435)	39,022	33,246	(5,776)
Corporate obligations	539,020	523,002	(16,018)	23,958	22,020	(1,938)
Total bonds	<u>\$ 882,408</u>	<u>\$ 861,246</u>	<u>\$ (21,162)</u>	<u>\$ 225,181</u>	<u>\$ 207,403</u>	<u>\$ (17,778)</u>
Surplus notes	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Common stocks	\$ 724	\$ 720	\$ (4)	\$ —	\$ —	\$ —
Short-term investments	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —

Net investment income was derived from the following sources:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
<i>(In Thousands)</i>				
Income from bonds	\$ 20,179	\$ 19,348	\$ 61,037	\$ 57,961
Income from common stocks	-	724	-	2,053
Income from surplus notes	103	102	308	118
Income from cash, cash equivalents and short-term investments	404	627	1,183	1,888
Total investment income	<u>20,686</u>	<u>20,801</u>	<u>62,528</u>	<u>62,020</u>
Investment expenses	<u>(540)</u>	<u>(481)</u>	<u>(1,601)</u>	<u>(1,452)</u>
Net investment income	<u>\$ 20,146</u>	<u>\$ 20,320</u>	<u>\$ 60,927</u>	<u>\$ 60,568</u>

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **4. Investments (continued)**

For the nine months ended September 30, 2019, prepayment penalties and acceleration fees reported as investment income were reported for four CUSIPs. The aggregate amount of investment income related to such penalties and fees was \$0.1 million.

For the three and nine months ended September 30, 2019 and 2018, proceeds from dispositions of investments in bonds carried at amortized cost were \$234.2 million and \$471.9 million, and \$213.4 million and \$659.9 million, respectively. For the three and nine months ended September 30, 2019 and 2018, gross realized gains on such dispositions were \$20.9 million and \$26.7 million, and \$3.0 million and \$22.7 million, respectively. For the three and nine months ended September 30, 2019 and 2018, gross realized losses on such dispositions were \$0.6 million and \$2.0, and \$5.2 million and \$9.7 million, respectively.

For the three and nine months ended September 30, 2019 and 2018, proceeds from dispositions of investments in common stock were \$0.0 million and \$135.6 million, and \$25.0 million and \$25.0 million, respectively. Gross realized gains on such dispositions were \$0.0 million and \$20.9 million, and \$6.7 million and \$6.7 million, for the three and nine months ended September 30, 2019 and 2018, respectively. There were no gross realized losses on such dispositions for the three and nine months ended September 30, 2019 and 2018, respectively. The Company sold all its investments in common stocks in February 2019.

Investments in cash, cash equivalents and bonds carried at amortized cost of \$4.5 million and \$4.3 million as of September 30, 2019 and December 31, 2018, respectively, were on deposit with various regulatory authorities. Investments in cash, cash equivalents and bonds carried at amortized cost totaling \$33.3 million and \$35.0 million as of September 30, 2019 and December 31, 2018, respectively, were on deposit with an institutional trustee to provide a secure funding source for certain non-policy obligations that may become due in the future.

The carrying values of the Company's investment in the common stock of SCA entities were \$33.2 million as of both September 30, 2019 and December 31, 2018. In July 2018, the Company dissolved an SCA entity that was not conducting any active business. The Company recorded a realized gain of \$13.3 million from such dissolution.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 5. Income Taxes

FGIC Corp. files a consolidated U.S. federal income tax return which includes FGIC. The method of allocation between FGIC Corp. and FGIC is determined under an amended and restated income tax allocation agreement approved by the NYSDFS and is based upon separate return calculations.

The following is a reconciliation of current federal income taxes computed at the statutory rate on income before provision for federal income taxes and the provision for current federal income taxes.

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
	<i>(In Thousands)</i>			
Income taxes computed at the statutory rate on income before provision for federal income taxes	\$ 1,231	\$ 13	\$ 4,218	\$ 3,358
Tax effect of:				
Tax-exempt interest	—	—	—	(91)
Change in valuation allowance	(1,150)	2,324	(3,898)	(936)
Realized gain on dissolution of subsidiary	—	(2,783)	—	(2,783)
Other, net	11	(198)	34	(237)
Expense (benefit) for federal income taxes	<u>\$ 92</u>	<u>\$ (644)</u>	<u>\$ 354</u>	<u>\$ (689)</u>
Federal income tax benefit	\$ (718)	\$ (1,170)	\$ (2,157)	\$ (4,046)
Expense related to change in net deferred income taxes	810	526	2,511	3,357
Total statutory income taxes	<u>\$ 92</u>	<u>\$ (644)</u>	<u>\$ 354</u>	<u>\$ (689)</u>

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 5. Income Taxes (continued)

The composition of current federal income tax benefit for the three and nine months ended September 30, 2019 and 2018 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
	<i>(In Thousands)</i>			
Current income tax:				
Federal	\$ (3,236)	\$ (4,415)	\$ (9,751)	\$ (9,839)
Federal income tax expense on net capital gains	2,518	3,245	7,594	5,793
Federal income tax benefit	<u>\$ (718)</u>	<u>\$ (1,170)</u>	<u>\$ (2,157)</u>	<u>\$ (4,046)</u>

The change in net deferred income taxes is composed of the following:

	September 30, December 31,		
	2019	2018	Change
	<i>(In Thousands)</i>		
Total adjusted gross deferred tax assets	\$ 248,811	\$ 271,632	\$ (22,821)
Less: Total gross deferred tax liabilities	245,217	265,881	(20,664)
Net deferred tax asset	<u>\$ 3,594</u>	<u>\$ 5,751</u>	(2,157)
Less: tax effect of net unrealized gains (losses)			354
Change in net deferred income taxes			<u>\$ (2,511)</u>

As of September 30, 2019, the Company had a domestic net operating loss (“NOL”) carryforward of \$3,214.5 million for federal income tax purposes, which will be available (subject to certain limitations) to offset future taxable income. If not used, the NOL carryforward will start expiring in 2029 through 2037 depending on the originating year.

As of September 30, 2019, the Company had an AMT credit carryforward of \$3.6 million for federal income tax purposes. In the absence of offsetting taxable income, the Company may claim a refund of 50% of the then remaining AMT credit carryforward in each tax year through 2020 and 100% of the then remaining AMT credit carryforward in 2021. The Company has recognized the AMT credit as a current period recoverable to the extent it relates to refundable AMT credits

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 5. Income Taxes (continued)

for the 2019 tax year. The remaining AMT credit carryforward has been recognized as a deferred tax asset.

	<b>September 30, 2019</b>
	<i>(In Thousands)</i>
Gross AMT credit recognized as:	
Current period recoverable	\$ 2,157
Deferred tax asset	3,594
Beginning balance of AMT credit carryforward	5,751
Amounts recovered	(2,157)
Adjustments	—
Ending balance of AMT credit carryforward	<u>3,594</u>
Non-admitted	—
Ending balance of AMT credit carryforward	<u>\$ 3,594</u>

As of September 30, 2019, the Company had a foreign tax credit carryforward of \$0.8 million, which will be available to offset future foreign tax. If not used, the foreign tax credit carryforward will start expiring in 2034 through 2036 depending on the originating year.

The amount of federal income taxes incurred and available for recoupment in the event of future losses is \$0.

In accordance with SSAP 101, *Income Taxes, A Replacement of SSAP No. 10R and SSAP No. 10* (“SSAP 101”), the Company evaluates its deferred income tax asset to determine whether a valuation allowance is required. SSAP 101 requires that companies assess whether a valuation allowance should be established based on the consideration of all available evidence using a “more likely than not” standard. In making such judgments, significant weight is given to evidence that can be objectively verified. Management believes it is more likely than not that the amortization of the net unearned premium reserve, collection of future installment premiums on contracts already written, and income from the investment portfolio will not generate sufficient taxable income to realize the entire deferred tax asset that currently exists. Accordingly, a valuation allowance of \$476.5 million was established against the Company’s domestic net deferred tax asset as of September 30, 2019. This resulted in a net deferred tax asset of \$3.6 million, which

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 5. Income Taxes (continued)

relates to the Company's AMT credit carryforward discussed above. Such net deferred tax asset is not admitted under SAP. The Company will continue to analyze the need for a valuation allowance on a quarterly basis. The Company's tax returns are subject to routine audits by the Internal Revenue Service and other taxing authorities.

The following table presents the total of deferred tax assets and liabilities by tax character:

	<b>September 30, 2019</b>	<b>December 31, 2018</b>
	<i>(In Thousands)</i>	
Gross deferred tax assets:		
Ordinary income	\$ 715,086	\$ 742,608
Capital losses	10,190	9,387
Gross deferred tax assets	<u>725,276</u>	<u>751,995</u>
Statutory valuation allowance adjustment	(476,465)	(480,363)
Adjusted gross deferred tax assets	<u>248,811</u>	<u>271,632</u>
Deferred tax assets non-admitted adjustment	(3,594)	(5,751)
Subtotal net admitted deferred tax asset	<u>245,217</u>	<u>265,881</u>
Deferred tax liabilities:		
Ordinary income	(245,148)	(265,766)
Capital gains	(69)	(115)
Deferred tax liabilities	<u>(245,217)</u>	<u>(265,881)</u>
Net admitted deferred tax asset	<u>\$ —</u>	<u>\$ —</u>

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 5. Income Taxes (continued)

The tax effects of temporary differences that give rise to significant portions of the net deferred tax asset at September 30, 2019 and December 31, 2018 are presented below by tax component:

	<b>September 30, December 31,</b>	
	<b>2019</b>	<b>2018</b>
	<i>(In Thousands)</i>	
Deferred tax assets:		
Premium revenue recognition	\$ 796	\$ 891
Net operating loss carryforward	675,036	700,074
Impairment losses on investments	3,093	4,839
AMT credit	3,594	5,751
Losses-salvage and subrogation recoverable	6,611	6,448
Unrealized loss from FGIC UK	19,629	19,629
Deemed repatriation of FGIC UK E&P	2,808	2,808
Other	13,709	11,555
Gross deferred tax assets	725,276	751,995
Statutory valuation allowance adjustment	(476,465)	(480,363)
Adjusted gross deferred tax assets	248,811	271,632
Deferred tax assets non-admitted adjustment	(3,594)	(5,751)
Net admitted gross deferred tax assets	245,217	265,881
Deferred tax liabilities:		
Tax basis losses incurred adjustment	(244,188)	(264,804)
Discount on bonds and other	(1,029)	(1,077)
Deferred tax liabilities	(245,217)	(265,881)
Net admitted deferred tax asset	\$ —	\$ —



## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 6. Loss Reserves

Loss reserves comprise the total amount of (i) the Claims Reserve, (ii) the DPO for all policies and (iii) the DPO Accretion for all policies, minus the Policy Revision Adjustment. The Policy Revision Adjustment shown in the table below is prescribed by NYSDFS Guidelines and reflects the reduction in the loss reserve components necessary to reflect a Minimum Surplus Amount of \$66.4 million.

The loss reserve components as of September 30, 2019 and December 31, 2018 are summarized as follows:

	<b>September 30, 2019</b>	<b>December 31, 2018</b>
	<i>(In Thousands)</i>	
Claims Reserve	<b>\$ 1,142,552</b>	\$ 1,334,365
DPO	<b>1,528,843</b>	1,453,824
DPO Accretion	<b>238,939</b>	206,171
Total	<b>2,910,334</b>	2,994,360
Policy Revision Adjustment	<b>(1,174,168)</b>	(1,276,565)
Loss reserves, net balance at end of period	<b><u>\$ 1,736,166</u></b>	<u>\$ 1,717,795</u>

#### Claims Reserve

The Claims Reserve is calculated on a policy-by-policy basis for insured obligations, net of reinsurance, as of the reporting date (using the prescribed statutory discount rate which is based on the average rate of return on the Company's admitted assets, which was 4.60% at both September 30, 2019 and December 31, 2018). The amount of the discount applied to the Claims Reserve as of September 30, 2019 and December 31, 2018 was \$834.6 million and \$934.5 million, respectively. The amount of the discount decreased by \$99.9 and \$34.5 for the nine months ended September 30, 2019 and the year ended December 31, 2018, respectively. Any decrease (increase) in the amount of the discount is recorded as an increase (decrease) to losses incurred.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 6. Loss Reserves (continued)

Activity related to the Claims Reserve for the nine months ended September 30, 2019 and the year ended December 31, 2018 is summarized as follows:

	<b>September 31, December 31,</b>	
	<b>2019</b>	<b>2018</b>
	<i>(In Thousands)</i>	
Claims Reserve, beginning of period	<b>\$ 1,334,365</b>	<b>\$ 1,518,188</b>
Total Claims Reserve released related to:		
Current year	—	—
Prior years	<b>(65,517)</b>	<b>(56,595)</b>
Total released	<b>(65,517)</b>	<b>(56,595)</b>
Paid related to:		
Current year	—	—
Prior years	<b>(51,277)</b>	<b>(42,797)</b>
Total paid	<b>(51,277)</b>	<b>(42,797)</b>
DPO related to policy claims paid at the applicable CPP, less DPO reductions:		
Current year	—	—
Prior years	<b>(75,019)</b>	<b>(84,431)</b>
Total related to DPO	<b>(75,019)</b>	<b>(84,431)</b>
Claims Reserve, end of period	<b><u>\$ 1,142,552</u></b>	<b><u>\$ 1,334,365</u></b>

As of September 30, 2019, FGIC's Claims Reserve was attributable nearly entirely to its Puerto Rico-related insured exposures and certain residential mortgage-backed securities ("RMBS") insured by FGIC. The Claims Reserve decreased \$191.8 million to \$1,142.6 million at September 30, 2019 from \$1,334.4 million at December 31, 2018. The Claims Reserve released of \$65.5 million for the nine months ended September 30, 2019 was primarily driven by decreases in estimated losses for certain FGIC-insured floating rate RMBS due to forward interest rate movements, which were partially offset by a decrease in the amount of the discount applied to the Claims Reserve.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 6. Loss Reserves (continued)

The following table shows the gross and net par in force for FGIC's Puerto Rico-related insured exposures as of September 30, 2019:

	<b>Gross Par In Force*</b>	<b>Net Par In Force*</b>
	<i>(In Thousands)</i>	
Puerto Rico General Obligation	\$ 189,655	\$ 188,078
Puerto Rico Convention Center District Authority	97,075	97,075
Puerto Rico Highways and Transportation Authority (Trans Revs – Senior)	367,200	339,529
Puerto Rico Highways and Transportation Authority (Trans Revs – Subordinate)	27,320	27,320
Puerto Rico Infrastructure Financing Authority**	293,030	293,030
Total	<u>\$ 974,280</u>	<u>\$ 945,032</u>

\* With respect to any FGIC-insured exposure, (i) gross par in force is based on the outstanding principal amount of such exposure, as of the date of determination, but, if such exposure has been the subject of any permitted policy claim paid by FGIC at the CPP in accordance with the Rehabilitation Plan, the gross par in force is reduced by the total amount of all such permitted policy claims relating to principal (without duplication of any other actual reductions), not merely by the CPP portion thereof paid in cash, since the Rehabilitation Plan prohibits future policy claims for that principal amount or interest thereon, and (ii) net par in force means the gross par in force for such exposure net of any related reinsurance.

\*\* Includes capital appreciation bonds (CABs) using their total original principal amount of \$111.2 million. As of September 30, 2019, the total accreted value of these CABs was \$214.9 million.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 6. Loss Reserves (continued)

The following table shows the scheduled net debt service due on FGIC's Puerto Rico-related insured exposures as of September 30, 2019, for each of the years presented:

	<b>Puerto Rico General Obligation</b>	<b>Puerto Rico Convention Center District Authority</b>	<b>Puerto Rico Highways and Transportation Authority (Trans Revs – Senior)</b>	<b>Puerto Rico Highways and Transportation Authority (Trans Revs - Subordinate)</b>	<b>Puerto Rico Infrastructure Financing Authority</b>	<b>Total</b>
	<i>(In Thousands)</i>					
2020	\$ 26,232	\$ 4,755	\$ 24,820	\$ 12,571	\$ 54,716	\$ 123,094
2021	95,096	19,075	38,486	17,258	54,712	224,627
2022	60,170	19,073	47,226	–	54,713	181,182
2023	1,579	19,076	28,866	–	8,045	57,566
2024	1,579	19,075	28,865	–	8,045	57,564
Thereafter	36,458	38,147	411,232	–	482,756	968,593
Total	\$ 221,114	\$ 119,201	\$ 579,495	\$ 29,829	\$ 662,987	\$ 1,612,626

There is no scheduled net debt service due for the remainder of 2019.

FGIC's Puerto Rico-related insured exposures are subject to significant stress and credit deterioration arising from Puerto Rico's fiscal, financial, liquidity and other challenges. There is substantial uncertainty as to Puerto Rico's ability and willingness to pay its various debt service obligations, as discussed below.

Puerto Rico has defaulted on all semi-annual debt service payments on FGIC-insured Puerto Rico Infrastructure Financing Authority ("PRIFA") bonds due from and after January 1, 2016, FGIC-insured General Obligation ("GO") and GO Guaranteed bonds due from and after July 1, 2016, and FGIC-insured Puerto Rico Highways and Transportation Authority ("PRHTA") and Puerto Rico Convention Center District Authority ("PRCCDA") bonds due from and after July 1, 2017. Due to Puerto Rico's defaults, FGIC has made payments in accordance with the terms of its related policies (as modified by the Rehabilitation Plan) in respect of aggregate policy claims of approximately \$358.4 million through September 30, 2019. To the extent Puerto Rico continues to fail to pay scheduled debt service on FGIC-insured exposures as and when due, FGIC would be obligated to pay the related claims under its policies (as modified by the Rehabilitation Plan), and such claims could be material. While FGIC will seek to recover any claim payments it makes, there can be no assurance that FGIC will be able to recover any such payments.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **6. Loss Reserves (continued)**

On June 30, 2016, the President of the United States signed into law the Puerto Rico Oversight Management and Economic Stability Act (“PROMESA”). PROMESA, among other things, established the Financial Oversight and Management Board (the “Oversight Board”) with broad responsibilities and authority for (i) overseeing the development of budgets and fiscal plans for the Commonwealth and its instrumentalities and (ii) initiating judicial processes under Title III of PROMESA to restructure the debts of the Commonwealth and its instrumentalities, by accessing multiple sections of the U.S. Bankruptcy Code (including cramdown provisions) that were not previously available to Puerto Rico. PROMESA also set forth collective action provisions intended to facilitate consensual debt restructurings pursuant to Title VI of PROMESA. PROMESA provided for an automatic stay of debt-related litigation and other enforcement actions upon its enactment (the “PROMESA Stay”), which expired on May 1, 2017.

On May 3, 2017, the Oversight Board filed a petition in the U.S. District Court for the District of Puerto Rico and thereby commenced a debt adjustment proceeding for the Commonwealth of Puerto Rico under Title III of PROMESA. On May 21, 2017, the Oversight Board filed a petition in the U.S. District Court for the District of Puerto Rico and thereby commenced a debt adjustment proceeding for PRHTA under Title III of PROMESA. The terms and timing for any final outcome of these Title III proceedings are uncertain but could materially impact FGIC.

On June 14, 2017, Judge Laura Taylor Swain (the federal judge hearing the Title III cases) entered an order designating a mediation team comprising five sitting federal judges to facilitate confidential settlement negotiations of any and all issues and proceedings arising in the Title III cases. On October 28, 2019, Judge Swain entered an order extending (i) the stay of the litigation of various issues in the Commonwealth and PRHTA Title III cases, including adversary proceedings and other disputes involving FGIC, from November 30, 2019 to December 31, 2019, and (ii) the mandatory mediation of various matters before the designated mediators, which were imposed by her prior order entered on July 24, 2019 (collectively, the “Stay and Mediation Order”). Since 2017, FGIC has participated in many mediation and negotiation sessions with no resolution to its claims.

The Oversight Board has certified several fiscal plans for the Commonwealth and PRHTA. On May 9, 2019, the Oversight Board certified a revised fiscal plan for the Commonwealth, which projects annual budgetary surpluses through 2037, followed by annual budgetary deficits (the “May 2019 Certified Fiscal Plan”). As was the case with prior certified fiscal plans for the Commonwealth, this revised fiscal plan does not provide a high degree of detail regarding the underlying data, assumptions and rationales supporting those assumptions, which hinders the reconciliation and verification of the financial projections. In addition, the Oversight Board and

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **6. Loss Reserves (continued)**

the Commonwealth appear to be at odds over basic assumptions used in the revised fiscal plan. Consequently, it is difficult to predict with any certainty the ability and willingness of the Oversight Board and Commonwealth to pay, or allocate or appropriate funds for payment of, the existing contractual debt service obligations of the Commonwealth and its authorities and public corporations, including PRIFA and PRCCDA, shown in the revised fiscal plan.

On June 5, 2019, the Oversight Board certified a revised fiscal plan for PRHTA, which continues to exclude large sources of PRHTA revenues from the forecasted cash flows for PRHTA and consequently continues to show limited capacity to pay PRHTA's existing contractual debt service obligations over the six-year period covered by such revised fiscal plan.

The Oversight Board may revise these certified fiscal plans if it determines that revisions are warranted. It is unclear, however, whether, or to what extent, the Oversight Board may revise these certified fiscal plans in the future. The nature and extent of any such revisions could be material to FGIC, since the final certified fiscal plans for the Commonwealth and PRHTA are intended to serve as the bases for the plans of adjustment in their respective Title III proceedings.

On September 27, 2019, the Oversight Board filed a joint plan of adjustment for the Commonwealth, the Employees Retirement System and the Puerto Rico Public Buildings Authority, in the Commonwealth's Title III proceeding. The proposed plan of adjustment is based on the May 2019 Certified Fiscal Plan and provides for, among other things, discounted recoveries for holders of GO and GO Guaranteed bonds and minimal recoveries for holders of PRIFA, PRCCDA and PRHTA bonds, which vary by bond type. The Oversight Board may amend this proposed plan of adjustment if it amends the May 2019 Certified Fiscal Plan or otherwise determines that revisions are warranted. It is unclear, however, whether, or to what extent, the Oversight Board may revise this proposed plan of adjustment in the future. The proposed plan of adjustment and the nature and extent of any such revisions could be material to FGIC.

The Oversight Board has not yet filed a proposed plan of adjustment for PRHTA in PRHTA's Title III proceeding, and it is unclear when it will file such plan of adjustment. Any such proposed plan of adjustment, however, may provide for additional recoveries for holders of PRHTA bonds, including bonds insured by FGIC.

On February 15, 2019, the United States Court of Appeals for the First Circuit held that members of the Oversight Board were not appointed in compliance with the Appointments Clause of the U.S. Constitution, but it declined to invalidate any prior actions of the Oversight Board, including the PROMESA Title III proceedings commenced by the Oversight Board. On June 20, 2019, the

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **6. Loss Reserves (continued)**

Supreme Court of the United States granted the separate petitions of the Oversight Board and other parties to review the First Circuit's ruling. On July 2, 2019, the First Circuit extended the stay of its ruling, which had been in effect, pending disposition of the case by the Supreme Court. On October 18, 2019, the Supreme Court heard oral argument from the parties in interest. The Supreme Court's opinion, when rendered, may be material to FGIC.

FGIC has commenced various legal proceedings and taken various legal actions against the Commonwealth, the Oversight Board and others with respect to actions taken (or not taken) that affect the Puerto Rico-related exposures it insures, including those discussed in Note 10, Legal Proceedings.

The ultimate impact of Hurricanes Irma and Maria, which caused widespread devastation in the Commonwealth in September 2017 (the "Hurricanes") (and the amount and timing of any federal aid or other assistance for the Commonwealth), PROMESA (including the Title III proceedings that have been or may be filed and legal challenges that have been or may be brought), laws enacted by the Commonwealth, executive orders issued by the Governor of Puerto Rico, and actions taken (or not taken) by the Oversight Board or the Commonwealth, on Puerto Rico and its fiscal, financial, liquidity and other challenges, including the payment or restructuring of its debt obligations (including those insured by FGIC), is uncertain, but could be material to FGIC.

As of September 30, 2019, FGIC's Claims Reserve for its Puerto Rico-related insured exposures was based on various factors and assumptions, including the possible timing and outcome of the Title III proceedings that have been or may be filed and legal challenges that have been or may be brought, the nature, timing and impact of recovery and relief efforts relating to the Hurricanes (including the amount and timing of any federal aid or other assistance for the Commonwealth), and the impact of actions taken (or not taken) by the Oversight Board or the Commonwealth, and other matters, including those highlighted above. The establishment of such Claims Reserve is an inherently uncertain process involving numerous assumptions, estimates and subjective judgments by management about the outcome of future events. Rulings, outcomes or other developments relating to, or otherwise affecting, Puerto Rico, including in the Title III proceedings, may lead to changes in the Claims Reserve for FGIC's Puerto Rico-related insured exposures and the policy claims that FGIC may be required to pay under its related policies, and such changes could be material. It is impossible to predict with any certainty how or when Puerto Rico will be able to resolve its debt and other challenges, and any such resolution could have a material effect on FGIC's Claims Reserve and the related policy claims that FGIC would be required to pay.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **6. Loss Reserves (continued)**

The cash flow projection models for estimating future losses and recoveries on insured RMBS utilize various important assumptions, including assumptions as to future mortgage loan performance (e.g., default rates, loss severity rates, and prepayment rates) that are typically based on recent historical performance and assumptions as to future interest rates that are typically derived from forward interest rate curves. The Company has insured certain floating rate RMBS transactions. Accordingly, the Company is exposed to interest rate risk. For Claims Reserve purposes, each quarter the Company projects its insured exposure on these transactions using forward interest rate curves as of the end of the second month of such quarter. For such RMBS transactions, increases or decreases in the interest rates comprising such curves as compared to the prior quarter could significantly impact the related Claims Reserve, and such changes could be material. The Claims Reserve should be most significantly impacted on such RMBS transactions where FGIC is not required to pay policy claims relating to principal losses until legal maturity of the transactions (2035-2037) because they will continue to have relatively high principal balances on which interest generally will accrue except as otherwise provided in the transaction documents.

The Company believes that the Claims Reserve as of September 30, 2019 is adequate. However, the establishment of the Claims Reserve is an inherently uncertain process involving numerous assumptions, estimates and subjective judgments by management about the outcome of future events. Rulings, outcomes or other developments relating to, or otherwise affecting, Puerto Rico may lead to changes in the Claims Reserve for FGIC's Puerto Rico-related insured exposures and the policy claims that FGIC may be required to pay under its related policies, and such changes could be material. It is impossible to predict with any certainty how or when Puerto Rico will be able to resolve its debt and other challenges, and any such resolution could have a material effect on FGIC's Claims Reserve and the related policy claims that FGIC would be required to pay. Actual loan performance and other RMBS-related developments may lead to changes in the Claims Reserve for insured RMBS, including as to default frequency and liquidation values for loans supporting the insured RMBS, future interest rate movements, the amount and timing of collateral cash flows, and the priority of application of those cash flows under the transactions documents.

Small changes in the assumptions, estimates or judgments used by management, which may arise from, among other things, further deterioration in FGIC-insured Puerto Rico-related exposures or the performance of FGIC-insured RMBS, interest rate movements, or changes in the ability or willingness of insured obligors (including Puerto Rico-related entities) to pay their debt service obligations, could result in significant changes in the Company's loss expectations and the related Claims Reserve. These changes will not affect the Company's loss reserve or operating results as long as a Policy Revision Adjustment is required to be made. There can be no assurance that the Company's estimate of the Claims Reserve is accurate. Accordingly, there can be no assurance



## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **6. Loss Reserves (continued)**

that the total amount of policy claims permitted by the Company after September 30, 2019 will not exceed or be less than its Claims Reserve at September 30, 2019, and it is possible that they could significantly exceed such reserve.

The Company evaluates the portfolio of insured obligations on a regular basis to determine if there has been credit deterioration. The Company evaluates such factors as rating agency downgrades, significant changes in a specific industry and specific events impacting a particular insured obligation, such as a negative credit event, performance below expectations, breaches of representations, warranties, covenants or deal triggers, management changes, regulatory changes, material litigation and other legal issues. Based on the Company's evaluation of these and other factors, the Company assigns insured obligations to risk categories, which assignment determines the level of on-going monitoring and surveillance efforts required and whether a Claims Reserve is recorded. The Company uses the following risk categories to define and monitor its insured obligations:

#### **Risk Category 1 – Performing**

Issuers/transactions are performing with no expectation of loss. Financial strength of the issuer/transaction would enable it to withstand volatility in performance without jeopardizing timely payment of debt service. Issuers/transactions are considered to be investment grade. Although rating changes may occur, it is not expected that a downgrade would be to below investment grade.

#### **Risk Category 2 – Under Heightened Surveillance**

Issuers/transactions typically would be considered low investment grade or higher-rated non-investment grade. Issuers/transactions have been determined to require heightened surveillance, taking into account the totality of their circumstances, but have not deteriorated to the level that they would be considered impaired and require a Claims Reserve.

#### **Risk Category 3 – Experiencing Credit Impairment**

Credit deterioration has occurred and there is substantial uncertainty as to the issuers/transaction's ability or willingness to pay its debt service obligations in a timely manner. Issuers/transactions typically would have suffered sustained negative trends or would have been the subject of a significant adverse event, but are currently not in payment default. Issuers/transactions have been determined to be impaired, and there is an increased probability of default, but FGIC has not

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 6. Loss Reserves (continued)

determined, or been able to determine, that policy claims are probable and estimable.

#### Risk Category 4 – Currently or Likely to Be in Payment Default

Issuers/transactions that have deteriorated to the point where payment default on their debt service obligations has occurred or is probable and the ultimate loss can be reasonably estimated. Claims Reserves are established on a case basis and are inclusive of any anticipated recoveries from the particular issuers/transactions or the related collateral. Issuers/transactions would be consistent with the lowest or in-default credit ratings. Issuers/transactions are reviewed and updated on at least a quarterly basis for any change in status.

The following table is a breakdown, as of September 30, 2019, of the Company's portfolio of insured obligations assigned to risk categories 2, 3 and 4:

	<b>Risk Category 2</b>	<b>Risk Category 3</b>	<b>Risk Category 4</b>	<b>Total</b>
	<i>(Dollars in Thousands)</i>			
Number of policies	12	–	84	96
Remaining weighted-average contract period (in years)	3	–	9	XXX
Insured contractual payments outstanding:				
Principal	\$ 79,911	\$ –	\$ 3,077,084	\$ 3,156,995
Interest	5,694	–	1,342,746	1,348,440
Total	\$ 85,605	\$ –	\$ 4,419,830	\$ 4,505,435
Gross Claims Reserve	\$ –	\$ –	\$ 2,249,017	\$ 2,249,017
Less:				
Gross projected recoveries	–	–	218,863	218,863
Discount	–	–	856,377	856,377
Gross Claims Reserve, net of discount and projected recoveries	\$ –	\$ –	\$ 1,173,777	\$ 1,173,777
Unearned premiums	\$ 8	\$ –	\$ 25,453	\$ 25,461
Reinsurance recoverable reported in the balance sheet	\$ –	\$ –	\$ 33	\$ 33

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **6. Loss Reserves (continued)**

In RMBS, asset-backed securities and other securitization transactions insured by FGIC, the structure of the waterfall of cash flows in the transaction documents and applicable terms and conditions of the Rehabilitation Plan may permit FGIC to recover claims paid from subsequent cash flows. The projected recoveries in the above table reflect FGIC's current estimate of these recoveries, but there can be no assurance that such recoveries will be received by FGIC. The Company's insured obligations are structured to provide for rights and remedies in order to mitigate claim loss exposure. Loss mitigation activities may include making repurchase claims or pursuing other claims for breaches of representations and warranties by the originator or others, obtaining appraisals of collateral or reviews of loan files, enforcing collateral provisions and covenants of the servicer or others, more frequent meetings with the issuer or servicer, evaluating the financial position of the originator or servicer, renegotiating financial covenants, triggers, or terms of servicing, enforcing rights to remove and replace the servicer, evaluating restructuring plans or bankruptcy proceedings, and commencing litigation or arbitration proceedings as and where appropriate.

There can be no assurance that any loss mitigation efforts will be successful, or as to the magnitude of any benefit that might be derived from any such efforts that are successful.

In accordance with the Rehabilitation Plan, each reinsurer is obligated to pay FGIC in full in cash for such reinsurer's reinsured portion of the entire amount of each permitted policy claim covered by the reinsurance, in each case without giving effect to the modification of FGIC's policy obligations and regardless of the amount paid in cash by FGIC on account of such policy claim. Any reinsurance recoverable on losses is calculated in a manner consistent with the calculation of the gross Claims Reserve and reflected in the Claims Reserve as a reduction of the liability.

# Financial Guaranty Insurance Company

## Notes to Statutory-Basis Financial Statements (continued)

### 6. Loss Reserves (continued)

#### DPO

Activity in the DPO for the nine months ended September 30, 2019 and the year ended December 31, 2018 is summarized as follows:

	<b>September 30, 2019</b>	<b>December 31, 2018</b>
	<i>(In Thousands)</i>	
DPO, beginning of period	\$ 1,453,824	\$ 1,484,761
Payments of DPO	–	(138,789)
DPO related to policy claims paid at the applicable CPP, less DPO reductions	75,019	84,431
DPO increases related to amounts recovered by FGIC	–	23,421
DPO, end of period	<u>\$ 1,528,843</u>	<u>\$ 1,453,824</u>

In connection with the 2019 CPP Upward Adjustment, on October 28, 2019, FGIC made payments of DPO (net of amounts recovered by FGIC) in an aggregate amount of \$108.7 million.

#### DPO Accretion

Activity in the DPO Accretion for the nine months ended September 30, 2019 and the year ended December 31, 2018 is summarized as follows:

	<b>September 30, 2019</b>	<b>December 31, 2018</b>
	<i>(In thousands)</i>	
DPO Accretion, beginning of period	\$ 206,171	\$ 171,972
DPO Accretion for the period	32,768	48,825
Payments of DPO Accretion	–	(14,626)
DPO Accretion, end of period	<u>\$ 238,939</u>	<u>\$ 206,171</u>

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 6. Loss Reserves (continued)

In connection with the 2019 CPP Upward Adjustment, on October 28, 2019, FGIC made payments of DPO Accretion in an aggregate amount of \$17.2 million.

#### Policy Revision Adjustment

Activity in the Policy Revision Adjustment for the nine months ended September 30, 2019 and the year ended December 31, 2018 is summarized as follows:

	<b>September 30, 2019</b>	<b>December 31, 2018</b>
	<i>(In Thousands)</i>	
Policy Revision Adjustment, beginning of period	\$ (1,276,565)	\$ (1,331,071)
Decrease in Policy Revision Adjustment	<b>102,397</b>	54,506
Policy Revision Adjustment, end of period	<b>\$ (1,174,168)</b>	<b>\$ (1,276,565)</b>

#### 7. Loss Adjustment Expense Reserve

The Company estimates a loss adjustment expense reserve based on the ultimate future net cost, determined using internally developed estimates, of the efforts involved in managing and mitigating existing and future policy claims and recovering or mitigating its policy losses and liabilities.

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 7. Loss Adjustment Expense Reserve (continued)

Activity in the loss adjustment expense reserve for the nine months ended September 30, 2019 and the year ended December 31, 2018 is summarized as follows:

	September 30, 2019	December 31, 2018
	<i>(In Thousands)</i>	
Net balance at beginning of period	\$ 16,646	\$ 26,828
(Released) incurred related to:		
Current year	—	—
Prior years	(148)	3,190
Total (released) incurred	(148)	3,190
Paid related to:		
Current year	—	—
Prior years	(5,369)	(13,372)
Total paid	(5,369)	(13,372)
Net balance at end of period	\$ 11,129	\$ 16,646

#### 8. Employee Benefit Plans

Since January 1, 2004, the Company has offered a defined contribution savings plan under Section 401(k) of the Internal Revenue Code. This plan covers substantially all employees who meet minimum age and service requirements and allows participants to defer a portion of their annual compensation on a pre-tax basis. The Company makes matching contributions to the plan on behalf of employees. For the three and nine months ended September 30, 2019 and 2018, the Company contributed to the plan, on behalf of employees, \$0.0 million and \$0.5 million, and \$0.0 million and \$0.5 million, respectively.

Effective April 1, 2014, the Company adopted a Long-Term Incentive Plan, a non-qualified, unfunded deferred compensation plan for certain employees (the “LTIP”). All issued and outstanding LTIP units are valued at least annually by the Compensation Committee of the Board of Directors based on specified metrics in accordance with the LTIP. The LTIP units issued in 2014 vested 100% on December 31, 2016 and the benefits under 50% of the units were paid in the

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### **8. Employee Benefit Plans (continued)**

first quarter of 2017 and the benefits under the remainder were paid in the first quarter of 2019. The LTIP units issued in 2015 vested 100% on December 31, 2017 and the benefits under all such units were paid in the first quarter of 2018. The LTIP units issued in 2016 will vest 100% on December 31, 2019 (or earlier under certain conditions) and the benefits under all such units will be paid in the first quarter of 2020. For the three and nine months ended September 30, 2019 and 2018, the benefits accrued under the LTIP were \$0.3 million and \$1.0 million, and \$0.3 million and \$1.2 million, respectively.

#### **9. Related-Party Transactions**

The Company is a party to cost-sharing agreements with FGIC Corp. and FGIC UK, pursuant to which the Company may provide these affiliates with management, administrative and other services, the Company may incur and pay costs and other expenses that benefit these affiliates, and these affiliates are obligated to pay the Company for the allocated cost of such services and to reimburse the Company for their allocated share of such expenses paid by the Company. Such shared costs and expenses are allocated to affiliates and vary depending on the assumptions underlying the allocations.

The Company is a party to an amended and restated income tax allocation agreement with FGIC Corp. (see Note 5, Income Taxes).

The assets provided by the City of Detroit, Michigan in connection with the settlement of certain claims related to the FGIC-insured certificates of participation (the “COPs”) issued by the Detroit Retirement Systems Funding Trust 2005 and the Detroit Retirement Systems Funding Trust 2006 (together, the “COPs Trusts”) pursuant to Detroit’s bankruptcy plan were transferred to Gotham Motown Recovery, LLC (“GMR”), a Delaware limited liability company formed in 2016 for the purpose of owning, managing, administering, and otherwise dealing with such assets. FGIC is the managing member of GMR and as such is entitled to receive expense reimbursement from GMR, but such membership interest does not entitle FGIC to receive any distributions made by GMR or to any direct economic ownership of GMR. The COPs Trusts are members of GMR holding in the aggregate a 100% economic interest in GMR on behalf of the holders of the COPs (including FGIC to the extent it has acquired or will acquire COPs by paying policy claims in cash or otherwise acquires COPs). All distributions made by GMR are payable to the COPs Trust Members, which in turn generally pay such distributions to the holders of the COPs. As of September 30, 2019, FGIC owned 38.5% of the COPs by virtue of having paid policy claims in cash, and accordingly is entitled to receive 38.5% of all such payments that may be made to the COPs holders. After making the DPO payments required in connection with the 2019 CPP Upward Adjustment, FGIC

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 9. Related Party Transactions (continued)

will own 43.5% of the COPs. All such payments received by FGIC are recorded as reductions to losses incurred when received. In accordance with SAP, FGIC does not assign any value as an asset to its membership interest in GMR or its ownership of COPs. Expense reimbursements that FGIC receives from GMR in connection with acting as the managing member of GMR are recorded as reductions to other underwriting expenses.

#### 10. Legal Proceedings

FGIC may be involved from time to time in various legal proceedings filed against it. In addition, FGIC has received, and may in the future receive, various subpoenas, regulatory inquiries, requests for information and document preservation letters. Defending against legal proceedings and responding to subpoenas, regulatory inquiries, requests for information and document preservation letters may involve significant expense and diversion of management's attention and other FGIC resources.

FGIC has asserted, and from time to time may assert, claims in legal or arbitration proceedings against third parties to recover losses already incurred by FGIC or to mitigate future losses that FGIC may incur, including the lawsuits described below. The amount of losses that FGIC may recover or mitigate as a result of these proceedings is uncertain, although, in the event of favorable outcomes or settlements, such amount could be material to FGIC's results of operations, financial position, profitability or cash flows.

In *Financial Guaranty Insurance Company v. The Putnam Advisory Company, LLC* (U.S. District Court for the Southern District of New York, filed October 1, 2012 and thereafter amended on November 19, 2012), FGIC sued The Putnam Advisory Company ("Putnam"), alleging fraud, negligent misrepresentation and negligence by Putnam in connection with the Pyxis ABS CDO 2006-1 transaction for which Putnam acted as collateral manager. On September 10, 2013, FGIC's complaint was dismissed, with leave to file a further amended complaint. On September 30, 2013, FGIC filed a further amended complaint. On April 28, 2014, the District Court granted Putnam's motion to dismiss FGIC's claims. On April 15, 2015, the United States Court of Appeals for the Second Circuit vacated the District Court's dismissal of FGIC's complaint and remanded the case for further proceedings. On May 18, 2015, Putnam filed its answer to the complaint. On September 10, 2019, the District Court denied FGIC's motion for summary judgment as to its claims arising from Putnam's negligent misrepresentation and negligence, and denied the principal elements of Putnam's motion for summary judgment as to FGIC's claims. The District Court has scheduled FGIC's claims for trial in 2020.



## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 10. Legal Proceedings (continued)

In *Financial Guaranty Insurance Company v. Morgan Stanley ABS Capital I Inc. and Morgan Stanley Mortgage Capital Holdings LLC*, (N.Y. Sup.Ct., Index No. 652853/2014, filed on September 19, 2014), FGIC sued Morgan Stanley ABS Capital I Inc. (“MSAC”) and Morgan Stanley Mortgage Capital Holdings LLC (“MSMC”), alleging, *inter alia*, that defendants breached various warranties and affirmative covenants in connection with the securitization transaction known as Basket of Aggregated Residential NIMS 2007-1, including their obligations to repurchase breaching net interest margin securities that collateralized the insured securities, and to reimburse FGIC for payments made under the related FGIC policy. On January 19, 2017, the trial court denied in its entirety defendants’ motion to dismiss FGIC’s claims. On March 1, 2017, defendants filed their answer to the complaint. On September 13, 2018, the Appellate Division of the Supreme Court of New York, First Department, affirmed the trial court’s decision denying defendants’ motion to dismiss.

In *Financial Guaranty Insurance Company v. Morgan Stanley, et al.*, (N.Y. Sup.Ct., Index No. 652914/2014, filed on September 23, 2014), FGIC sued MSAC, MSMC, Morgan Stanley (MS) and Morgan Stanley & Co. LLC (collectively, “Morgan Stanley”), and Saxon Mortgage Services, Inc. (“Saxon”), alleging, *inter alia*, that (i) Morgan Stanley fraudulently induced FGIC to insure the RMBS transaction known as MSAC 2007-NC4; (ii) MSAC, MSMC and MS breached various warranties and affirmative covenants, including their obligations to repurchase breaching or fraudulent mortgage loans and to reimburse FGIC for payments made under the related FGIC policy; and (iii) Saxon and MS breached their warranties and obligations under the Pooling and Servicing Agreement for the MSAC 2007-NC4 transaction, including their obligation to provide notice of breaching mortgage loans. On January 23, 2017, the trial court denied in its entirety defendant’s motion to dismiss FGIC’s claims. On March 1, 2017, defendants filed their answer to the complaint. On September 13, 2018, the Appellate Division of the Supreme Court of New York, First Department, modified the decision of the trial court and granted defendants’ motion to dismiss FGIC’s fraud claim, but otherwise affirmed the trial court’s decision denying defendants’ motions to dismiss. On December 20, 2018, FGIC’s motion for leave to reargue or appeal this dismissal was denied by the Appellate Division. On July 16, 2019, the trial court granted FGIC’s motion for leave to amend its complaint (i) to expressly plead that Morgan Stanley was grossly negligent and (ii) to assert a cause of action related to Morgan Stanley’s failure to notify FGIC of breaches of warranties that Morgan Stanley discovered.

In *Assured Guaranty Corp., et al. v. Commonwealth of Puerto Rico, et al.*, (D.P.R., Case No. 17-00156-LTS, filed on June 3, 2017, and thereafter amended on July 23, 2017), FGIC, Assured Guaranty Corp., Assured Guaranty Municipal Corp., and National Public Finance Guarantee Corporation commenced an adversary proceeding in the PRHTA Title III case seeking to enforce

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 10. Legal Proceedings (continued)

the special revenue protections of the U.S. Bankruptcy Code (11 U.S.C. §§ 902, 922(d), 928(a)), which Congress incorporated into Title III proceedings under PROMESA, with respect to special revenues pledged to secure the repayment of PRHTA bonds. Plaintiffs seek (i) a declaration that defendants have violated Sections 922(d) and 928(a) of the U.S. Bankruptcy Code, and that efforts to compel defendants to transfer such pledged revenues to pay for debt service on PRHTA bonds are not stayed, (ii) injunctive relief prohibiting defendants from taking or causing to be taken any action that would further violate Sections 922(d) and 928(a) of the U.S. Bankruptcy Code and ordering defendants to remit revenues securing the PRHTA Bonds in accordance with such Sections, and (iii) declaratory relief that all funds held in the PRHTA bond reserve accounts are property of the PRHTA bondholders and are being improperly withheld. On January 30, 2018, the District Court granted defendants' motion to dismiss this adversary proceeding. On March 26, 2019, the United States Court of Appeals for the First Circuit affirmed the District Court's dismissal of this adversary proceeding. On July 31, 2019, the United States Court of Appeals for the First Circuit denied plaintiffs' petition for panel rehearing or rehearing *en banc* of this decision. In September 2019, the other plaintiffs in this proceeding filed with the Supreme Court of the United States a petition for writ of certiorari with respect to the First Circuit's decision.

In *Assured Guaranty Corp., et al. v. Commonwealth of Puerto Rico, et al.*, (D.P.R., Case No. 18-00059-LTS, filed on May 23, 2018), FGIC, Assured Guaranty Corp., and Assured Guaranty Municipal Corp. commenced an adversary proceeding in the Commonwealth of Puerto Rico's Title III case seeking a judgment declaring that the revised fiscal plan for the Commonwealth that was certified by the Oversight Board on April 29, 2018, is unlawful and unconstitutional based on, among other things, violations of various provisions of PROMESA and the Contracts, Takings and Due Process Clauses of the U.S. Constitution, and declaring that the Oversight Board cannot use the revised fiscal plan as the basis for proposing a plan of adjustment in the Commonwealth's Title III case. Since July 24, 2019, this adversary proceeding has been stayed pursuant to the Stay and Mediation Order. This adversary proceeding had previously been stayed by judicial order from August 13, 2018, until June 24, 2019.

In *The Financial Oversight and Management Board for Puerto Rico, et al. v. Ambac Assurance Corporation, et al.* (D.P.R. Case No. 19-00363, filed on May 20, 2019), the Oversight Board, the Official Committee of Unsecured Creditors and PRHTA commenced an adversary proceeding in PRHTA's Title III case against numerous parties, including FGIC and other insurers and holders of PRHTA's bonds, seeking, among other things, declaratory judgments that such parties do not possess a security interest in anything beyond revenues received by PRHTA and deposited in accounts held by the fiscal agent, and that such parties' claims, to the extent they are valid, are unsecured. On June 11, 2019, FGIC filed its answer, counterclaims and third-party claims, seeking

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 10. Legal Proceedings (continued)

declaratory judgments that (i) FGIC has a lawful lien or priority in the revenues and taxes pledged to secure the PRHTA bonds, and that these pledged revenues and taxes are not subject to clawback or the conditions for effectuating any clawback have not been satisfied, (ii) the Oversight Board acted *ultra vires* and in violation of the U.S. and Commonwealth Constitutions when approving certain fiscal plans and budgets for the Commonwealth and PRHTA and (iii) such fiscal plans and budgets are void. FGIC further seeks through its and counterclaims and third-party claims both writs of mandamus and prohibition to: (a) require the Oversight Board to revoke the invalid fiscal plans and budgets and to develop and approve legal fiscal plans and budgets respecting such liens and priorities of the PRHTA bonds; and (b) prohibit the Oversight Board from approving any fiscal plans or budgets that do not respect such liens and priorities and from proposing any plan of adjustment that is *per se* unconfirmable. Since July 24, 2019, this adversary proceeding has been stayed pursuant to the Stay and Mediation Order.

In *The Financial Oversight and Management Board for Puerto Rico, et al v. Autonomy Master Fund Limited, et al.* (D.P.R. Case No. 19-00291, filed on May 2, 2019), the Oversight Board and the Official Committee of Unsecured Creditors commenced an adversary proceeding in the Commonwealth's Title III case against numerous parties, including FGIC and other insurers and holders of the Commonwealth's general obligation and guaranteed debt, seeking, among other things, declaratory judgments that such parties do not hold consensual or statutory liens against the Commonwealth's good faith, credit, and taxing power, available resources, allocable revenues or property tax revenues, and that such parties' claims, to the extent they are valid, are unsecured. Since July 24, 2019, this adversary proceeding has been stayed pursuant to the Stay and Mediation Order.

On June 21, 2019, FGIC filed a joinder to Ambac Assurance Corporation's motion concerning application of the automatic stay to the rum tax revenues securing certain PRIFA bonds (D.P.R. Case No. 17-bk-3283-LTS, filed on May 30, 2019). Ambac's motion requests an order finding that the automatic stay does not apply to two lawsuits relating to these PRIFA bonds or, in the alternative, relief from the automatic stay to pursue the two lawsuits in alternative forums or an order requiring the Commonwealth to provide adequate protection with respect to such PRIFA bonds. Since July 24, 2019, this motion has been stayed pursuant to the Stay and Mediation Order.

In *Financial Guaranty Insurance Company v. Alejandro García Padilla, et al.*, (D.P.R., Case No. 3:16-cv-01095, filed on January 19, 2016), FGIC commenced an action for declaratory judgment and injunctive relief seeking, *inter alia*, to invalidate the executive orders issued by the Governor of Puerto Rico on November 30 and December 7, 2015, authorizing the

## Financial Guaranty Insurance Company

### Notes to Statutory-Basis Financial Statements (continued)

#### 10. Legal Proceedings (continued)

Commonwealth's Treasury Department to clawback certain revenues assigned or pledged to secure the payment of bonds issued by PRIFA, PRHTA and PRCCDA, including bonds insured by FGIC, on the grounds that they are preempted by federal law and/or violate the Contracts, Due Process, Takings, and Equal Protection Clause of the United States Constitution. On January 21, 2016, FGIC's action was consolidated with an analogous action brought by Assured Guaranty Corp., Assured Guaranty Municipal Corp., and Ambac Assurance Corporation.

On October 4, 2016, the District Court entered an order denying all defendants' motions to dismiss FGIC's claims, except that it dismissed FGIC's preemption-based claim. This action was subject to the PROMESA Stay, and it is now stayed by the commencement of the Commonwealth's PROMESA Title III proceeding.

On March 16, 2017, FGIC filed a motion for leave to intervene as a plaintiff in *Lex Claims, LLC, et al. v. The Commonwealth of Puerto Rico, et al.*, (D.P.R. Case No. 3:16-cv-02374, filed on July 20, 2016), which case was filed by a group of holders of the Commonwealth's general obligation bonds challenging, *inter alia*, the validity of the Puerto Rico Emergency Moratorium and Financial Rehabilitation Act, related executive orders, and the availability of resources pledged to pay bonds issued by the Puerto Rico Sales Tax Financing Corporation (also known by its acronym in Spanish, "COFINA"). Before the District Court ruled on FGIC's motion to intervene, the United States Court of Appeals for the First Circuit, on April 4, 2017, ruled that the PROMESA Stay applied to all claims asserted by the original plaintiffs in this action. Therefore, FGIC's motion for leave to intervene was similarly subject to the PROMESA Stay, and it is now stayed by the commencement of the Commonwealth's PROMESA Title III proceeding.

#### 11. Subsequent Events

Subsequent events described elsewhere in the notes to these financial statements include: in Note 1, Organization and Background, Note 6, Loss Reserves, and Note 9, Related-Party Transactions, information relating to the 2019 CPP Upward Adjustment; in Note 6, Loss Reserves, information about developments concerning FGIC's Puerto Rico-related insured exposures; and in Note 10, Legal Proceedings, information about developments concerning certain legal proceedings.

The date through which subsequent events have been evaluated is November 7, 2019.