

November 9, 2010

Elizabeth M. Murphy  
Secretary  
U.S. Securities and Exchange Commission  
100 F St., NE  
Washington, D.C. 20549

David A. Stawick  
Secretary  
U.S. Commodity Futures Trading Commission  
Three Lafayette Centre,  
1155 21<sup>st</sup> Street, NW,  
Washington, D.C. 20581

Re: Follow-up to September 29, 2010 Meeting with SEC and CFTC Staff

Dear Ms. Murphy and Mr. Stawick:

We write on behalf of the National Association of Insurance Commissioners (NAIC) to follow-up on our meeting of September 29, 2010 and letter comment submitted on September 20 regarding the definitions contained in Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Act). At the meeting, staff at the Securities and Exchange Commission and the Commodity Futures Trading Commission (the Commissions) had several questions for the NAIC to consider, and requested certain information from the NAIC to assist them in the rulemaking process.

**Definition of “Insurance Contract”**

The staff of the Commissions requested the NAIC’s thoughts on the appropriate definition for an insurance contract, presumably for the purpose of considering an exclusion of such contracts from the definitions of swap and security-based swap as is consistent with Congressional intent and required by the McCarran-Ferguson Act of 1945. After careful consideration and consultation with relevant law, we believe an insurance contract constitutes:

1. A contract that exists for a specified period of time;
2. Where one party to the contract (the “insured”) promises to pay one or more payments (the “premium”) to a company licensed by a state to provide such contracts (the “insurer”)
3. In exchange for the insurer’s promise to pay or indemnify the insured or their beneficiary for the loss, destruction, injury or impairment of an identified interest of the insured (the “insurable interest”) as a result of the occurrence of a specified event(s) or contingency(ies); and

---

|                                    |                                      |                            |                  |                  |
|------------------------------------|--------------------------------------|----------------------------|------------------|------------------|
| <b>EXECUTIVE OFFICE</b>            | 444 N. Capitol Street, NW, Suite 701 | Washington, DC 20001-1509  | p   202 471 3990 | f   816 460 7493 |
| <b>CENTRAL OFFICE</b>              | 2301 McGee Street, Suite 800         | Kansas City, MO 64108-2662 | p   816 842 3600 | f   816 783 8175 |
| <b>SECURITIES VALUATION OFFICE</b> | 48 Wall Street, 6th Floor            | New York, NY 10005-2906    | p   212 398 9000 | f   212 382 4207 |

---

4. Where such indemnification or payment is limited to the extent of the value of the insurable interest.

Excluding contracts that meet this definition would carve out insurance products that are already subject to the robust state regulatory regime while ensuring that the Commissions retain the authority over the swap and derivative products that Congress intended for them to regulate; specifically, the products written and traded in the over-the-counter derivatives market.

### **Financial Guaranty Insurance**

Commission staff requested information about state regulation of financial guaranty insurance. As NAIC staff detailed in the meeting, financial guaranty insurers are subject to stringent state regulatory requirements that include specific accounting, disclosure, reserve and capital requirements. To assist with staff's understanding of such requirements, we forward for your review NAIC's Statement of Statutory Accounting Principles No. 60 (SSAP No. 60) relating to financial guaranty insurance (Exhibit A).<sup>1</sup> SSAP No. 60 sets forth the definition of financial guaranty insurance, which differentiates it from other insurance lines and financial products defined in other SSAPs:

“Financial guaranty insurance provides protection against financial loss as a result of default, changes in interest rate levels, differentials in interest rate levels between markets or products, fluctuations in exchange rates between currencies, inconvertibility of one currency into another, inability to withdraw funds held in a foreign country resulting from restrictions imposed by a governmental body, changes in the value of specific assets or commodities, financial or commodity indices, or price levels in general. Financial guaranty insurance does not provide protection from losses which occur due to fortuitous physical events, failure or deficiency in the operation of equipment, or the inability to extract natural resources. Additionally, it does not provide coverage from losses related to various types of bonds (e.g., individual or schedule public official bond; a contract bond; a court bond), credit insurance, guaranteed investment contracts, and residual value insurance.”<sup>2</sup>

SSAP No. 60 also details the disclosure requirements, premium and loss recognition requirements, and contingency reserve requirements for financial guaranty insurance.

As part of the discussion of the financial guaranty insurance business, staff asked for information regarding financial guaranty insurers' use of “transformers” to issue credit default swap contracts that are then insured with the financial guaranty insurance. We have consulted with relevant industry representatives and regulators regarding the use of transformers in the financial guaranty insurance business. Our understanding is that certain financial guaranty insurers have created legally separate affiliates that write credit default swaps (CDS), which are then insured with financial guaranty insurance by a separate state licensed insurance company. While state regulators monitor the insurance company's solvency and have the authority to intervene where necessary to ensure that the financial guaranty insurer is sufficiently capitalized, they do not directly regulate the “transformer,” since it is a separate corporate entity that is not licensed by the state to write insurance. Transactions with these affiliated transformers are subject to regulation under the holding company regulations and must be fair to the interests of the insurer.

---

<sup>1</sup> Please note that the redline text within the guidance is used by the NAIC to denote the most recent updates to the guidance contained in the document.

<sup>2</sup> See, SSAP No. 60 at 60-3.

In light of Congressional intent that the Commissions regulate derivatives including credit default swaps, it would be wholly appropriate for the Commissions to regulate transformers' activity in this regard. However, for the reasons set forth both in our letter of September 20 and in our meeting of September 29, we believe it would be wholly inappropriate for the Commissions to regulate the issuance of financial guaranty insurance by state licensed insurance companies.

Financial guaranty insurance is fundamentally different from the credit default swaps and other derivatives that Congress intended the Commissions to regulate. Unlike CDS and other derivative products, financial guaranty insurance is subject to a robust regulatory regime administered by the states. Moreover, financial guaranty insurance insures a specific "insurable interest," such as a bond, from loss upon default by the bond issuer or impairment of the bond as result of a restructuring. The financial guaranty insurer is also only required to compensate the holder of the specific bond for losses that are allocated to that bond as the losses from the underlying assets are determined over time – a fact that is the case even in transactions involving transformers. By comparison, the typical CDS only requires the purchaser of the CDS to deliver any bond issued by the obligor of the reference obligation delineated in the CDS, and purchasers of CDS typically deliver the cheapest bond they can find on the market.

### **Use of Derivatives by Insurers**

NAIC and the Commissions' staff had constructive discussions regarding insurers' use of derivatives and the state investment laws that govern the extent and nature of such use. The Commissions' staff requested that the NAIC provide the specific accounting and risk-based capital guidance for insurers' use of replications. We provide for the Commissions' staff review:

- The NAIC's Annual Statement (Blank) for Schedule DB (Exhibit B), which is the actual disclosure form;
- The NAIC's Annual Statement Instructions for Schedule DB (Exhibit C);
- SSAP No. 86: The Accounting Requirements for Derivative Instruments and Hedging, Income Generation, and Replication Transactions (Exhibit D); and
- Risk-Based Capital (RBC) Formula Instructions and Disclosure Forms for Replications (Exhibit E).<sup>3</sup>

Part C of both the Annual Statement and the Annual Statement Instructions provide the relevant information regarding replications.

The Commissions' staff also requested certain information regarding any state regulatory limits on the use of derivatives. NAIC staff explained that the extent and nature of the use of derivatives by insurers is governed by the state investment laws referenced above, which vary to some degree by state. While these investment laws dictate the extent and nature of most insurers' investments including derivatives, several states also permit insurers some flexibility to invest in instruments not specifically prohibited, including derivatives up to certain specified aggregate limits. States provide insurers this flexibility in recognition of the unique characteristics insurance companies may possess and the different investment strategies their business needs may require. Commissions' staff requested information as to the extent of such limits, which are generally delineated in these investment laws as a percentage of "admitted

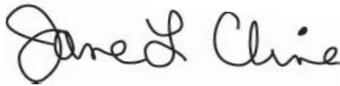
---

<sup>3</sup> These instructions and disclosures are used for life insurers and are provided as examples. However, the information regarding replications called for by these disclosures and the handling of RBC charges for replications/synthetic assets is the same for all insurers filing the RBC calculation.

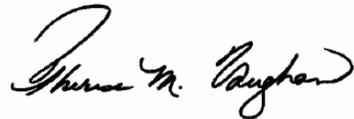
assets,”<sup>4</sup> and are generally within the range of 5 percent or 10 percent of admitted assets, though they can be as high as 20 percent.<sup>5</sup>

In conclusion, we appreciate the open and constructive dialogue we have had to date with the Commissions’ staff. Should you wish to discuss these responses or any other matter relating to the NAIC’s views on the rulemaking process, please do not hesitate to contact Ethan Sonnichsen, Director of Government Relations, at (202) 471-3980, Moira Campion McConaghy, Government Relations Manager, at (202) 649-4997, or Mark Sagat, Government Relations Analyst and Counsel, at (202) 471-3987.

Sincerely,



Jane L. Cline, Commissioner  
West Virginia Insurance Department  
NAIC President



Therese M. Vaughan, Ph.D.  
NAIC Chief Executive Officer

---

<sup>4</sup> Admitted Assets are those assets which an insurer can count towards statutory surplus. Those admitted assets are used in the risk based capital formula, which is a tool state insurance regulators use to take specified action on insurers with capital and surplus below regulatory levels.

<sup>5</sup> See, e.g., CAL. INS. CODE. § 1210 (2010)(5%); FLA. STAT. ANN. § 625.331 (2010) (5%); GA. CODE. ANN. § 33-11-55 (2010)(10%); MINN. STAT. ANN. §§ 60L.07, 61A.28 (2010)(5%); N.Y. INS. LAW §§ 1404, 1405 (2010)(5%-14%); OHIO REV. CODE ANN. § 3925.08(2010)(6%); PA. STAT. 40 P.S. §§ 504.2, 653c (2010)(20%); TEX. INS. CODE ANN. §§ 424.052, 425.152 (2009)(5%).

# Statement of Statutory Accounting Principles No. 60

## Financial Guaranty Insurance

### STATUS

Type of Issue: Common Area  
Issued: Initial Draft  
Effective Date: January 1, 2001  
Affects: No other pronouncements  
Affected by: No other pronouncements  
Interpreted by: INT 00-04

---

---

|  |          |
|--|----------|
| <b>STATUS .....</b>  | <b>1</b> |
| <b>SCOPE OF STATEMENT .....</b>                                | <b>3</b> |
| <b>SUMMARY CONCLUSION.....</b>                                 | <b>3</b> |
| Premium Revenue Recognition .....                              | 3        |
| Unpaid Losses and Loss Adjustment Expense Recognition .....    | 3        |
| Contingency Reserve.....                                       | 4        |
| Disclosures .....  | 5        |
| Effective Date and Transition.....                             | 8        |
| <b>RELEVANT ISSUE PAPERS.....</b>                              | <b>8</b> |
| <b>SSAP NO. 60 - APPENDIX A – DISCLOSURE ILLUSTRATION.....</b> | <b>9</b> |

**This page is intentionally left blank**

## Financial Guaranty Insurance

### SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for financial guaranty insurance and addresses areas where financial guaranty insurance accounting differs from other lines of insurance. To the extent a topic is not covered by this statement, financial guaranty insurance accounting shall comply with statutory accounting guidance for other lines of property and casualty insurance.

### SUMMARY CONCLUSION

2. Financial guaranty insurance provides protection against financial loss as a result of default, changes in interest rate levels, differentials in interest rate levels between markets or products, fluctuations in exchange rates between currencies, inconvertibility of one currency into another, inability to withdraw funds held in a foreign country resulting from restrictions imposed by a governmental body, changes in the value of specific assets or commodities, financial or commodity indices, or price levels in general. Financial guaranty insurance does not provide protection from losses which occur due to fortuitous physical events, failure or deficiency in the operation of equipment, or the inability to extract natural resources. Additionally, it does not provide coverage from losses related to various types of bonds (e.g., individual or schedule public official bond; a contract bond; a court bond), credit insurance, guaranteed investment contracts, and residual value insurance.

### Premium Revenue Recognition

3. Written premium shall be recorded in accordance with *SSAP No. 53—Property Casualty Contracts—Premiums* except that installment premiums, which may vary substantially over the term of the contract since the total amount insured and the premium rate are contingent upon the performance of the insured obligations, shall be recorded when received.

4. When premiums are paid on the installment basis, premium revenue shall be recognized in the statement of operations using the monthly pro-rata method. Premiums not paid on the installment basis shall be recognized in the statement of operations in proportion with the amount and expected coverage period of the insured risk.

5. When the anticipated losses, loss adjustment expenses, and maintenance cost exceed the recorded unearned premium reserve and contingency reserve, a premium deficiency reserve shall be recognized by recording an additional liability for the deficiency with a corresponding charge to operations. Commission and other acquisition costs need not be considered in the premium deficiency analysis since they have previously been expensed. If a reporting entity utilizes anticipated investment income as a factor in the premium deficiency calculation, disclosure of such shall be made in the financial statements.

### Unpaid Losses and Loss Adjustment Expense Recognition

6. Unpaid losses and loss adjustment expenses shall be recognized in accordance with *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* (SSAP No. 55). Each financial guaranty insurer shall establish and maintain reserves for unpaid losses and loss adjustment expenses. The initial date of default shall be considered the incident which gives rise to a claim. Loss reserves shall include a reserve for claims reported and unpaid net of collateral.

7. A deduction from loss reserves shall be allowed for the time value of money by application of a discount rate equal to the average rate of return on the admitted assets of the financial guaranty insurer as of the date of the computation of the reserve. The discount rate shall be adjusted at the end of each calendar year. In addition, a reserve component for incurred but not reported claims shall be reasonably

estimated, if deemed necessary by the financial guaranty insurer or required by the commissioner following an examination or actuarial analysis.

**Contingency Reserve**

8. In addition to the unearned premium reserve and the liability established for unpaid losses and loss adjustment expenses, financial guaranty insurers shall maintain a liability referred to as a statutory contingency reserve. The purpose of this reserve is to protect policyholders against loss during periods of extreme economic contraction.

9. The contingency reserve shall be the greater of fifty percent of premiums written for each category or the amount provided by applying the following percentages to the principal guaranteed in each calendar year. The premiums written shall be net of reinsurance if the reinsurer has established a contingency reserve.

|    |  |              |
|----|--|--------------|
| a. | Municipal obligation bonds   | 0.55 percent |
| b. | Special revenue bonds  | 0.85 percent |
| c. | Investment grade Industrial Development Bonds (IDBs) secured by collateral or having a term of seven years or less, and utility first mortgage obligations | 1.00 percent |
| d. | Other investment grade IDBs  | 1.50 percent |
| e. | Other IDBs   | 2.50 percent |
| f. | Investment grade obligations, secured by collateral or having a term of seven years or less  | 1.00 percent |
| g. | Other investment grade obligations not secured   | 1.50 percent |
| h. | Non-investment grade consumer debt obligations   | 2.00 percent |
| i. | Non-investment grade asset backed securities   | 2.00 percent |
| j. | All other non-investment grade obligations   | 2.50 percent |

10. Additions to the reserve for items a. through e. in paragraph 9, equal to one-eightieth of the amounts derived by applying the appropriate contribution specified above, shall be made each quarter for a period of twenty (20) years. Additions to the reserve for items f. through j. in paragraph 9 above, equal to one-sixtieth of the amounts derived by applying the appropriate contribution specified above, shall be made each quarter for a period of fifteen (15) years.

11. For contingency reserves required to be maintained for 20 years, contributions may be discontinued if the total reserve established for all categories in subparagraphs 9 a. through 9 e. exceeds the sum of the percentages contained therein multiplied by the unpaid principal guaranteed. For contingency reserves required to be maintained for 15 years, contributions may be discontinued if the total reserve established for all categories in subparagraphs 9 f. through 9 j. exceeds the sum of the percentages contained therein multiplied by the unpaid principal guaranteed.

12. The contingency reserve may also be released in the following circumstances:
- a. For contingency reserves required to be maintained for 20 years:
    - i. In any year in which actual incurred losses exceed 35% of the corresponding earned premiums, with commissioner approval;
    - ii. If the reserve has been in existence less than 40 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, with commissioner approval;
    - iii. If the reserve has been in existence more than 40 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, upon 30 days prior written notice to the commissioner.
  - b. For contingency reserves required to be maintained for 15 years:
    - i. In any year in which actual incurred losses exceed 65% of the corresponding earned premiums, with commissioner approval;
    - ii. If the reserve has been in existence less than 30 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, with commissioner approval;
    - iii. If the reserve has been in existence more than 30 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, upon 30 days prior written notice to the commissioner.

Any reductions shall be made on a first-in first-out basis. Changes in the reserve shall be recorded through unassigned funds (surplus).

### Disclosures

13. Financial guaranty insurers shall make all disclosures required by paragraphs 14-16 as well as other statements within the Accounting Practices and Procedures Manual, including but not limited to the requirements of SSAP No.55 and *SSAP No. 1—Disclosure of Accounting Policies, Risks & Uncertainties, and Other Disclosures*. (For disclosures within paragraph 15 and 16, all “expected” amounts and terms should be determined in accordance with management estimates.) In all instances, the insurer shall disclose when they elect to reflect timeframes or recognition principles from FASB Statement No. 163, Accounting for Financial Guarantee Insurance Contracts—an interpretation of FASB Statement No. 60 (FAS 163) as permitted within the disclosure requirements.

14. An insurance enterprise shall disclose information that enables users of its financial statements to understand the factors affecting the present and future recognition and measurement of financial guarantee insurance contracts.

15. To meet the disclosure objective in paragraph 14, an insurance enterprise shall disclose the following information for each annual reporting statement, and in any interim period if a significant change has occurred in that interim period:

- a. For financial guarantee insurance contracts where premiums are received as installment payments over the period of the contract, rather than at inception

- i. The unearned premium revenue as of the reporting date, in proportion with the amount and expected coverage period of the insured risk, which would have been reflected if the premium had been received at inception<sup>1</sup>.
- b. A schedule of premiums (undiscounted) expected to be collected under all installment contracts detailing the following:
  - i. The four quarters of the subsequent annual period and each of the next four annual periods
  - ii. The remaining periods aggregated in five-year increments
- c. A rollforward of the expected future premiums (undiscounted), including:
  - i. Expected future premiums – Beginning of Year
  - ii. Less - Premium payments received for existing installment contracts
  - iii. Add – Expected premium payments for new installment contracts
  - iv. Adjustments to the expected future premium payments
  - v. Expected future premiums – End of Year
- d. For non-installment contracts for which premium revenue recognition has been accelerated, the amount and reasons for acceleration.
- e. A schedule of the future expected earned premium revenue on non-installment contracts as of the latest date of the statement of financial position detailing the following:
  - i. The four quarters of the subsequent annual period and each of the next four annual periods
  - ii. The remaining periods aggregated in five year increments
- f. For the claim liability<sup>2</sup>
  - i. The rate used to discount the claim liability. This rate<sup>3</sup> shall equal the average rate of return on the admitted assets of the financial guaranty insurer as of the annual date of the computation of the reserve
  - ii. The significant component(s) of the change in the claim liability for the period (the accretion of the discount on the claim liability, changes in the timing, establishment of new reserves for defaults of insured contracts, changes or

<sup>1</sup> If desired, a reporting entity that follows FAS 163 for GAAP may elect to report this disclosure in accordance with the revenue recognition principles of FAS 163.

<sup>2</sup> The reference to “claim liability” throughout the disclosure requirements shall reflect the “reserves for unpaid losses and loss adjustment expenses” from paragraphs 6 and 7 of this Statement.

<sup>3</sup> The annual discount rate calculated pursuant to this paragraph shall be utilized for the subsequent year’s quarterly financial statements. Per paragraph 7, the discount rate shall be adjusted at the end of each year.

establishment of deficiency reserves, and changes or establishment of reserves for incurred but not reported claims), and the amount relating to each component(s).

- g. A description of the insurance enterprise's risk management activities used to track and monitor deteriorating insured financial obligations, including the following:
- i. A description of each grouping or category used to track and monitor deteriorating insured financial obligations
  - ii. The insurance enterprise's policies for placing an insured financial obligation in, and monitoring, each grouping or category
  - iii. The insurance enterprise's policies for avoiding or mitigating claim liabilities, the related expense and liability reported during the period for those risk mitigation activities (not including reinsurance), and a description of where that expense and that liability are reported in the statement of income and the statement of financial position, respectively.

16. An insurance enterprise shall disclose the following information for each annual and interim period related to the claim liability:

- a. A schedule of insured financial obligations at the end of each interim period detailing, at a minimum, the following for each category or grouping of these financial obligations (see Appendix A):
- i. Number of issued and outstanding financial guarantee insurance contracts
  - ii. Remaining weighted-average<sup>4</sup> contract period
  - iii. Insured contractual payments outstanding<sup>5</sup>, segregating principal and interest
  - iv. Gross claim liability<sup>6</sup>
  - v. Gross potential recoveries<sup>7</sup>
  - vi. Discount, net (both claim liability and potential recoveries<sup>8</sup>)

---

<sup>4</sup> Weighted average contract period shall be based on management's estimate of the weighted average life of the contracts. If desired, a reporting entity that follows FAS 163 for GAAP may elect to mirror the time period calculated under FAS 163.

<sup>5</sup> Contractual payments outstanding shall be based on management's estimates of receivables. If desired, a reporting entity that follows FAS 163 for GAAP may elect to mirror the time period calculated under FAS 163.

<sup>6</sup> Represents the unpaid losses and loss adjustment expenses calculated in accordance with SSAP No. 55 and SSAP No. 60, but excluding the effects of subrogation recoveries, ceded reinsurance and discounting.

<sup>7</sup> Includes (a) subrogation recoveries, which are deducted from the gross claim liabilities in accordance with paragraph 12 of SSAP No. 55 and (b) ceded reinsurance recoveries on unpaid losses, which are deducted from the gross claim liability in accordance with paragraph 88.a. of SSAP No. 62R.

<sup>8</sup> Represents the discounting effect of the gross claim liability, subrogation recoveries, and reinsurance recoveries.

vii. Net claim liability<sup>9</sup>

viii. Reinsurance recoverables<sup>10</sup>

ix. Unearned premium revenue<sup>11</sup>

14.17. Refer to the preamble for further discussion regarding disclosure requirements.

### Effective Date and Transition

15.18. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

### RELEVANT ISSUE PAPERS

- Issue Paper No. 69—Financial Guaranty Insurance

---

<sup>9</sup> Represents the gross claim liability less gross potential recoveries and the net discount. This line should reconcile to the sum of line 10, column 8 and column 9 (financial guaranty net unpaid losses and net unpaid loss adjustment expenses) of the Underwriting and Investment Exhibit, Part 2a – Unpaid Losses and Loss Adjustment Expenses.

<sup>10</sup> Represents reinsurance recoverables on paid losses which is reported as an asset with paragraph 20 of SSAP No. 62R. This line should reconcile to “Amounts recoverable from reinsurers” on the balance sheet.

<sup>11</sup> Unearned premium revenue (UPR) should be consistent with the UPR measurement principles of SSAP No. 60. UPR reported in this schedule may not reconcile to line 10, column 5 of the Underwriting and Investment Exhibit, Part 1a – Recapitulation of all Premiums. To the extent that this amount does not reconcile to line 10, column 5 of the *Underwriting and Investment Exhibit, Part 1a – Recapitulation of Premiums*, provide an additional reconciliation to line 10, column 5 of the Underwriting and Investment Exhibit, Part 1a in a footnote to the tabular disclosures required in paragraph 16.

**SSAP NO. 60 - APPENDIX A – DISCLOSURE ILLUSTRATION**

A1. The example below assumes the insurance enterprise uses a surveillance list with four surveillance categories to track and monitor its insured financial obligations. The surveillance list and four surveillance categories are used for illustrative purposes only. The surveillance categories shown below describe the claim liability before the mitigating effects of potential recoveries. The following are brief descriptions of each surveillance category to provide context to the example:

- a. Category A includes insured financial obligations that are still currently performing (that is, insured contractual payments are made on time but the likelihood of an event of default has increased since the financial guarantee insurance contract was first issued), but if economic conditions persist for an extended period of time, they may not be performing in the future. The issuer of the insured financial obligation may have experienced credit deterioration as a result of a general economic downturn. As a result, the present value of expected net cash outflows may exceed the unearned premium revenue of the financial guarantee insurance contract some time in the future.
- b. Category B includes insured financial obligations that are currently characterized as potentially nonperforming and may require action by the insurance enterprise to avoid or mitigate an event of default.
- c. Category C includes insured financial obligations that are characterized as nonperforming and for which actions to date by the insurance enterprise have not been successful in avoiding or mitigating an event of default. The insurance enterprise continues its efforts to cure the claim, but an event of default is imminent.
- d. Category D includes insured financial obligations where an event of default has occurred.

|  | <u>Surveillance Categories</u> |                       |                       |                            | <u>Total</u>            |
|--|--------------------------------|-----------------------|-----------------------|----------------------------|-------------------------|
|  | <u>A</u>                       | <u>B</u>              | <u>C</u>              | <u>D</u>                   |                         |
| <u>Number of policies</u>                                    | <u>37</u>                      | <u>16</u>             | <u>5</u>              | <u>4</u>                   | <u>62</u>               |
| <u>Remaining weighted-average contract period (in years)</u> | <u>16</u>                      | <u>14</u>             | <u>11</u>             | <u>12</u>                  |                         |
| <u>Insured contractual payments outstanding:</u>             |                                |                       |                       |                            |                         |
| <u>Principal</u>   | <u>\$ 656,000,000</u>          | <u>\$ 409,000,000</u> | <u>\$ 196,000,000</u> | <u>\$ 111,000,000</u>      | <u>\$ 1,372,000,000</u> |
| <u>Interest</u>  | <u>478,000,000</u>             | <u>298,000,000</u>    | <u>150,000,000</u>    | <u>73,000,000</u>          | <u>999,000,000</u>      |
| <u>Total</u>   | <u>\$ 1,134,000,000</u>        | <u>\$ 707,000,000</u> | <u>\$ 346,000,000</u> | <u>\$ 184,000,000</u>      | <u>\$ 2,371,000,000</u> |
| <u>Gross claim liability</u>                                 | <u>\$ 1,045,000,000</u>        | <u>\$ 690,000,000</u> | <u>\$ 330,000,000</u> | <u>\$ 184,000,000</u>      | <u>\$ 2,249,000,000</u> |
| <u>Less:</u>   |                                |                       |                       |                            |                         |
| <u>Gross potential recoveries</u>                            | <u>752,000,000</u>             | <u>381,000,000</u>    | <u>29,000,000</u>     | <u>7,000,000</u>           | <u>1,169,000,000</u>    |
| <u>Discount, net</u>   | <u>159,000,000</u>             | <u>153,000,000</u>    | <u>125,000,000</u>    | <u>78,000,000</u>          | <u>515,000,000</u>      |
| <u>Net claim liability</u>                                   | <u>\$ 134,000,000</u>          | <u>\$ 156,000,000</u> | <u>\$ 176,000,000</u> | <u>\$ 99,000,000</u>       | <u>\$ 565,000,000</u>   |
| <u>Unearned premium revenue</u>                              | <u>\$ 7,000,000</u>            | <u>\$ 4,000,000</u>   | <u>\$ 2,000,000</u>   | <u>\$ -</u> <sup>(b)</sup> | <u>\$ 13,000,000</u>    |
| <u>Reinsurance recoverables</u>                              | <u>\$ 10,000,000</u>           | <u>\$ 19,000,000</u>  | <u>\$ 25,000,000</u>  | <u>\$ 27,000,000</u>       | <u>\$ 81,000,000</u>    |

(b) In this instance, it is assumed that once an insured financial obligation is in Category D, the only remaining obligation of the insurance enterprise is making claim payments. As such, all related balances of the insured financial obligation are written off, including the unearned premium revenue.



**SCHEDULE DB – PART A – SECTION 2**

Showing all Options, Caps, Floors, Collars, Swaps and Forwards Terminated During Current Year

| 1           | 2                             | 3                            | 4                  | 5                        | 6          | 7                              | 8                | 9   | 10                  | 11              | 12  | 13   | 14   | 15   | 16                  | 17                            | 18   | 19  | 20   | 21                                      | 22                                      | 23  | 24                                    | 25  |  |  |  |  |  |     |  |  |  |     |     |
|-------------|-------------------------------|------------------------------|--------------------|--------------------------|------------|--------------------------------|------------------|---|---------------------|-----------------|---|--|--|--|---------------------|-------------------------------|------|---|--|---|---|---|---------------------------------------|---|--|--|--|--|--|-----|--|--|--|-----|-----|
| Description | Description of Hedged Item(s) | Schedule/ Exhibit Identifier | Type(s) of Risk(s) | Exchange or Counterparty | Trade Date | Date of Maturity or Expiration | Termination Date | Indicate Exercise, Expiration, Maturity or Sale | Number of Contracts | Notional Amount | Strike Price, Rate or Index Received (Paid) | Prior Year Initial Cost of Premium (Received) Paid | Current Year Initial Cost of Premium (Received) Paid | Consideration Received (Paid) on Termination | Current Year Income | Book/ Adjusted Carrying Value | Code | Unrealized Valuation Increase/ (Decrease) | Total Foreign Exchange Change in B./A.C.V. | Current Year's (Amortization)/Accretion | Gain (Loss) on Termination – Recognized | Adjustment to Carrying Value of Hedged Item | Gain (Loss) on Termination – Deferred | Hedge Effectiveness at Inception and at Termination (a) |  |  |  |  |  |     |  |  |  |     |     |
| 1399999     | Subtotal - Hedging Effective  |                              |                    |                          |            |                                |                  |   |                     |                 |   |  |  |  |                     |                               | XXX  |   |  |   |   |   |                                       |   |  |  |  |  |  | XXX |  |  |  |     |     |
| 1409999     | Subtotal - Hedging Other      |                              |                    |                          |            |                                |                  |   |                     |                 |   |  |  |  |                     |                               | XXX  |   |  |   |   |   |                                       |   |  |  |  |  |  |     |  |  |  | XXX |     |
| 1419999     | Subtotal - Replication        |                              |                    |                          |            |                                |                  |   |                     |                 |   |  |  |  |                     |                               | XXX  |   |  |   |   |   |                                       |   |  |  |  |  |  |     |  |  |  | XXX |     |
| 1429999     | Subtotal - Income Generation  |                              |                    |                          |            |                                |                  |   |                     |                 |   |  |  |  |                     |                               | XXX  |   |  |   |   |   |                                       |   |  |  |  |  |  |     |  |  |  |     | XXX |
| 1439999     | Subtotal - Other              |                              |                    |                          |            |                                |                  |   |                     |                 |   |  |  |  |                     |                               | XXX  |   |  |   |   |   |                                       |   |  |  |  |  |  |     |  |  |  |     | XXX |
| 1449999     | Totals                        |                              |                    |                          |            |                                |                  |   |                     |                 |   |  |  |  |                     |                               | XXX  |   |  |   |   |   |                                       |   |  |  |  |  |  |     |  |  |  | XXX |     |

|     |      |  |
|-----|------|--|
| (a) | Code | Financial or Economic Impact of the Hedge at the End of the Reporting Period |
|     |      | .....  |
|     |      | .....  |
|     |      | .....  |
|     |      | .....  |
|     |      | .....  |





