

MBIA INC  
Form 10-Q  
November 12, 2013  
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**United States**  
**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**Form 10-Q**

X **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2013

or

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from            to

Commission File Number 1-9583

**MBIA INC.**

(Exact name of registrant as specified in its charter)

**Connecticut**  
(State of incorporation)

**06-1185706**  
(I.R.S. Employer

Identification No.)

**113 King Street, Armonk, New York**  
(Address of principal executive offices)

**10504**  
(Zip Code)

**Registrant's telephone number, including area code: (914) 273-4545**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☐ No ☒

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒ Smaller reporting company ☐

Indicate by check mark whether the Registrant is shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

As of November 7, 2013, 192,247,762 shares of Common Stock, par value \$1 per share, were outstanding.

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**Table of Contents****PART 1 FINANCIAL INFORMATION****Item 1. Financial Statements****MBIA INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS (Unaudited)**

(In millions except share and per share amounts)

	September 30, 2013	December 31, 2012
<b>Assets</b>		
Investments:		
Fixed-maturity securities held as available-for-sale, at fair value (amortized cost \$4,516 and \$4,347)	\$ 4,505	\$ 4,485
Fixed-maturity securities at fair value	249	244
Investments pledged as collateral, at fair value (amortized cost \$407 and \$489)	347	443
Short-term investments held as available-for-sale, at fair value (amortized cost \$1,377 and \$662)	1,378	669
Other investments (includes investments at fair value of \$10 and \$12)	16	21
Total investments	6,495	5,862
Cash and cash equivalents	1,057	814
Premiums receivable	1,085	1,228
Deferred acquisition costs	270	302
Insurance loss recoverable	742	3,648
Property and equipment, at cost (less accumulated depreciation of \$87 and \$146)	37	69
Deferred income taxes, net	1,243	1,199
Other assets	247	268
Assets of consolidated variable interest entities:		
Cash	46	176
Investments held-to-maturity, at amortized cost (fair value \$2,566 and \$2,674)	2,809	2,829
Investments held as available-for-sale, at fair value (amortized cost \$156 and \$637)	156	625
Fixed-maturity securities at fair value	626	1,735
Loans receivable at fair value	1,704	1,881
Loan repurchase commitments	1,116	1,086
Other assets	-	2
<b>Total assets</b>	<b>\$ 17,633</b>	<b>\$ 21,724</b>
<b>Liabilities and Equity</b>		
Liabilities:		
Unearned premium revenue	\$ 2,544	\$ 2,938
Loss and loss adjustment expense reserves	688	853
Investment agreements	760	944
Medium-term notes (includes financial instruments carried at fair value of \$204 and \$165)	1,554	1,598
Long-term debt	1,677	1,732
Derivative liabilities	1,370	2,934
Other liabilities	439	245
Liabilities of consolidated variable interest entities:		
Variable interest entity notes (includes financial instruments carried at fair value of \$2,426 and \$3,659)	5,385	7,124

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Derivative liabilities	15	162
<b>Total liabilities</b>	<b>14,432</b>	<b>18,530</b>
Commitments and contingencies (See Note 14)		
Equity:		
Preferred stock, par value \$1 per share; authorized shares 10,000,000; issued and outstanding none	-	-
Common stock, par value \$1 per share; authorized shares 400,000,000; issued shares 277,804,062 and 277,405,039	278	277
Additional paid-in capital	3,113	3,076
Retained earnings	2,157	2,039
Accumulated other comprehensive income (loss), net of tax of \$30 and \$21	(50)	56
Treasury stock, at cost 85,551,418 and 81,733,530 shares	(2,318)	(2,275)
Total shareholders' equity of MBIA Inc.	3,180	3,173
Preferred stock of subsidiary and noncontrolling interest	21	21
<b>Total equity</b>	<b>3,201</b>	<b>3,194</b>
<b>Total liabilities and equity</b>	<b>\$ 17,633</b>	<b>\$ 21,724</b>

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

**Table of Contents****MBIA INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)**

(In millions except share and per share amounts)

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
<b>Revenues:</b>				
Premiums earned:				
Scheduled premiums earned	\$ 80	\$ 85	\$ 236	\$ 291
Refunding premiums earned	24	70	112	173
Premiums earned (net of ceded premiums of \$2, \$3, \$7 and \$12)	104	155	348	464
Net investment income	42	50	118	172
Fees and reimbursements	5	20	17	47
Change in fair value of insured derivatives:				
Realized gains (losses) and other settlements on insured derivatives	(28)	12	(1,548)	(420)
Unrealized gains (losses) on insured derivatives	285	(33)	1,562	1,473
Net change in fair value of insured derivatives	257	(21)	14	1,053
Net gains (losses) on financial instruments at fair value and foreign exchange	5	7	62	(18)
Investment losses related to other-than-temporary impairments:				
Investment losses related to other-than-temporary impairments	-	(3)	-	(58)
Other-than-temporary impairments recognized in accumulated other comprehensive income (loss)	-	(5)	-	(47)
Net investment losses related to other-than-temporary impairments	-	(8)	-	(105)
Net gains (losses) on extinguishment of debt	6	-	49	-
Other net realized gains (losses)	(29)	1	(29)	7
Revenues of consolidated variable interest entities:				
Net investment income	13	17	43	51
Net gains (losses) on financial instruments at fair value and foreign exchange	17	44	128	(17)
Net gains (losses) on extinguishment of debt	-	16	-	49
Other net realized gains (losses)	-	-	1	-
Total revenues	420	281	751	1,703
<b>Expenses:</b>				
Losses and loss adjustment	98	171	92	330
Amortization of deferred acquisition costs	9	8	36	36
Operating	71	72	280	307
Interest	59	69	179	214
Expenses of consolidated variable interest entities:				
Operating	2	5	8	14
Interest	10	13	34	43
Total expenses	249	338	629	944
Income (loss) before income taxes	171	(57)	122	759
Provision (benefit) for income taxes	39	(64)	4	161

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Net income (loss)	\$	132	\$	7	\$	118	\$	598
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## Net income (loss) per common share:

Basic	\$	0.68	\$	0.04	\$	0.61	\$	3.09
Diluted	\$	0.67	\$	0.04	\$	0.60	\$	3.07

## Weighted average number of common shares outstanding:

Basic	192,711,608	193,879,994	193,440,078	193,760,654
Diluted	196,746,771	194,977,642	197,762,488	194,835,537

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

**Table of Contents****MBIA INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)**

(In millions)

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Net income (loss)	\$ 132	\$ 7	\$ 118	\$ 598
Other comprehensive income (loss):				
Unrealized gains (losses) on available-for-sale securities:				
Unrealized gains (losses) arising during the period	(15)	75	(155)	236
Provision (benefit) for income taxes	(6)	18	(55)	70
Total	(9)	57	(100)	166
Reclassification adjustments for (gains) losses included in net income (loss)	13	(8)	(6)	84
Provision (benefit) for income taxes	5	(3)	(2)	29
Total	8	(5)	(4)	55
Available-for-sale securities with other-than-temporary impairments:				
Other-than-temporary impairments and unrealized gains (losses) arising during the period	8	2	15	40
Provision (benefit) for income taxes	2	1	6	14
Total	6	1	9	26
Reclassification adjustments for (gains) losses included in net income (loss)	(1)	6	(5)	52
Provision (benefit) for income taxes	(1)	2	(2)	18
Total	-	4	(3)	34
Foreign currency translation:				
Foreign currency translation gains (losses)	32	(7)	(7)	(18)
Provision (benefit) for income taxes	1	(4)	1	(3)
Total	31	(3)	(8)	(15)
Total other comprehensive income (loss)	36	54	(106)	266
<b>Comprehensive income (loss)</b>	<b>\$ 168</b>	<b>\$ 61</b>	<b>\$ 12</b>	<b>\$ 864</b>

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



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## MBIA INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)

For The Nine Months Ended September 30, 2013

(In millions except share amounts)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)		Treasury Stock		Total Shareholders' Equity of MBIA Inc.	Preferred Stock of Subsidiary and Noncontrolling Interest		Total Equity
	Shares	Amount					Shares	Amount		Shares	Amount	
<b>Balance, December 31, 2012</b>	<b>277,405,039</b>	<b>\$ 277</b>	<b>\$ 3,076</b>	<b>\$ 2,039</b>	<b>\$ 56</b>	<b>(81,733,530)</b>	<b>\$ (2,275)</b>	<b>\$ 3,173</b>	<b>1,315</b>	<b>\$ 21</b>		<b>\$ 3,194</b>
Net income (loss)	-	-	-	118	-	-	-	118	-	-		118
Other comprehensive income (loss)	-	-	-	-	(106)	-	-	(106)	-	-		(106)
Share-based compensation net of tax of \$4	399,023	1	37	-	-	(3,817,888)	(43)	(5)	-	-		(5)
<b>Balance, September 30, 2013</b>	<b>277,804,062</b>	<b>\$ 278</b>	<b>\$ 3,113</b>	<b>\$ 2,157</b>	<b>\$ (50)</b>	<b>(85,551,418)</b>	<b>\$ (2,318)</b>	<b>\$ 3,180</b>	<b>1,315</b>	<b>\$ 21</b>		<b>\$ 3,201</b>

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

**Table of Contents****MBIA INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**

(In millions)

	<b>Nine Months Ended September 30,</b>	
	<b>2013</b>	<b>2012</b>
Cash flows from operating activities:		
Premiums, fees and reimbursements received	\$ 143	\$ 223
Investment income received	326	459
Insured derivative commutations and losses paid	(453)	(463)
Financial guarantee losses and loss adjustment expenses paid	(382)	(620)
Proceeds from recoveries and reinsurance	1,797	131
Operating and employee related expenses paid	(227)	(300)
Interest paid, net of interest converted to principal	(170)	(377)
Income taxes (paid) received	(1)	(8)
Net cash provided (used) by operating activities	1,033	(955)
Cash flows from investing activities:		
Purchase of fixed-maturity securities	(2,704)	(2,032)
Sale and redemption of fixed-maturity securities	3,444	4,283
Proceeds from paydowns on variable interest entity loans	211	203
Redemptions of held-to-maturity investments	20	828
Sale (purchase) of short-term investments, net	(665)	335
Sale (purchase) of other investments, net	5	109
Consolidation (deconsolidation) of variable interest entities, net	(26)	(51)
(Payments) proceeds for derivative settlements	(51)	(266)
Collateral (to) from swap counterparty	65	(298)
Capital expenditures	(2)	(5)
Net cash provided (used) by investing activities	297	3,106
Cash flows from financing activities:		
Proceeds from investment agreements	25	52
Principal paydowns of investment agreements	(218)	(629)
Proceeds from medium-term notes	-	18
Principal paydowns of medium-term notes	(77)	(74)
Principal paydowns of variable interest entity notes	(1,001)	(1,059)
Payments for securities sold under agreements to repurchase	-	(287)
Proceeds from secured loan	50	-
Payments for retirement of debt	(3)	(364)
Change in noncontrolling interest and redemption of subsidiary preferred stock, net	-	(1)
Restricted stock awards settlements, net	-	1
Net cash provided (used) by financing activities	(1,224)	(2,343)
Effect of exchange rate changes on cash and cash equivalents	7	-
Net increase (decrease) in cash and cash equivalents	113	(192)
Cash and cash equivalents beginning of period	990	633

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Cash and cash equivalents end of period	\$	1,103	\$	441
Reconciliation of net income (loss) to net cash provided (used) by operating activities:				
Net income (loss)	\$	118	\$	598
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:				
Change in:				
Premiums receivable		138		98
Deferred acquisition costs		32		35
Unearned premium revenue		(392)		(443)
Loss and loss adjustment expense reserves		(169)		109
Insurance loss recoverable		2,802		(270)
Accrued interest payable		82		-
Accrued expenses		54		(40)
Net investment losses related to other-than-temporary impairments		-		105
Unrealized (gains) losses on insured derivatives		(1,562)		(1,473)
Net (gains) losses on financial instruments at fair value and foreign exchange		(190)		35
Other net realized (gains) losses		28		(7)
Deferred income tax provision (benefit)		2		163
(Gains) losses on extinguishment of debt		(49)		(49)
Interest on variable interest entities, net		65		114
Other operating		74		70
Total adjustments to net income (loss)		915		(1,553)
Net cash provided (used) by operating activities	\$	1,033	\$	(955)

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

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**MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 1: Business Developments and Risks and Uncertainties*****Summary***

MBIA Inc., together with its consolidated subsidiaries, (collectively, MBIA or the Company) operates one of the largest financial guarantee insurance businesses in the industry and is a provider of asset management and advisory services. These activities are managed through three business segments: United States ( U.S. ) public finance insurance; structured finance and international insurance; and advisory services. The Company's U.S. public finance insurance business is primarily operated through National Public Finance Guarantee Corporation and its subsidiaries ( National ), its structured finance and international insurance business is primarily operated through MBIA Insurance Corporation and its subsidiaries ( MBIA Corp. ), and its asset management and advisory services business is primarily operated through Cutwater Holdings, LLC and its subsidiaries ( Cutwater ). The holding company, MBIA, and certain of its subsidiaries also manage certain other business activities, the results of which are reported in its corporate, asset/liability products, and conduit segments. The corporate segment includes revenues and expenses that arise from general corporate activities. While the asset/liability products and conduit businesses represent separate business segments, they may be referred to collectively as wind-down operations as the funding programs managed through those businesses are in wind-down. Refer to Note 11: Business Segments for further information about the Company's reporting segments.

***Business Developments******Operating Cost Reductions***

In order to better position the Company for future business opportunities, in the third quarter of 2013, the Company initiated cost reduction measures focused on its legal, consulting, staffing and head office occupancy costs. As a result, expenses for net compensation costs related to staff reductions totaled \$18 million and were recorded primarily during the third quarter of 2013. These expenses are included in Operating expenses on the Company's consolidated statements of operations. These staff reductions reduced its worldwide June 30, 2013 headcount by approximately 21%. As a result of the potential sale of the office used in its operations, the Company recorded an impairment charge of \$29 million on its Armonk, New York facility. The carrying value of the facility was adjusted to its fair market value, which was determined based on an independent third-party appraisal of the facility. This impairment charge is reflected in the results of the Company's U.S. public finance insurance segment and is reported within Other net realized gains (losses) on the Company's consolidated statements of operations.

In addition, during the nine months ended September 30, 2013, the Company incurred operating expenses of approximately \$89 million related to settlement, consulting and legal expenses associated with the resolution of the litigation matters with Bank of America Corporation, Societe Generale, and Flagstar Bank. Refer below for discussions related to these settlements.

***Bank of America Settlement***

In May of 2013, MBIA Inc., together with its subsidiaries MBIA Corp. and National, entered into a comprehensive settlement agreement and related agreements (the BofA Settlement Agreement) with Bank of America Corporation and certain of its subsidiaries (collectively, Bank of America). As a result of the BofA Settlement Agreement, the repayment of MBIA Insurance Corporation's secured loan from National (the National Secured Loan) and recent credit ratings upgrades, the Company is currently evaluating strategies for re-entry into the U.S. public finance market. As of September 30, 2013, National was rated A with a stable outlook by Standard & Poor's Financial Services LLC ( S&P ) and Baa1 with a positive outlook by Moody's Investors Service, Inc. ( Moody's ). As of September 30, 2013, MBIA Insurance Corporation was rated B with a stable outlook by S&P and B3 with a positive outlook by Moody's. The Company is considering obtaining ratings for National from additional rating agencies.

Under the terms of the BofA Settlement Agreement, MBIA Corp. received a payment of approximately \$1.7 billion, consisting of \$1.6 billion of cash and \$136 million principal amount of MBIA Inc.'s 5.70% Senior Notes due 2034. In exchange for such payment, MBIA Corp. agreed to dismiss the litigation commenced in September 2008 against Countrywide Home Loans, Inc. ( Countrywide ), among other parties, and later amended to include claims against Bank of America, relating to breaches of representations and warranties on certain MBIA-insured securitizations sponsored by Countrywide. Bank of America and MBIA also agreed to the commutation of all of the MBIA Corp. policies held by Bank of America, which had a notional insured amount of approximately \$7.4 billion, of which \$6.1 billion were policies insuring credit default swaps ( CDS ) held by Bank of America referencing commercial real estate ( CRE ) exposures. MBIA Corp. has no further payment obligations under the commuted policies. The New York State Department of Financial Services ( NYDFS ) advised MBIA Corp. that the

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NYSDFS did not object to the BofA Settlement Agreement. The \$1.6 billion of cash received in connection with the BofA Settlement Agreement is included in Proceeds from recoveries and reinsurance presented under the heading Cash flows from operating activities on the Company's consolidated statements of cash flows.

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### **MBIA Inc. and Subsidiaries**

#### **Notes to Consolidated Financial Statements (Unaudited)**

##### **Note 1: Business Developments and Risks and Uncertainties (continued)**

Under the terms of the BofA Settlement Agreement, Blue Ridge Investments, L.L.C. ( "Blue Ridge" ), an affiliate of Bank of America, received a five-year warrant to purchase 9.94 million shares of MBIA common stock at a price of \$9.59 per share. Bank of America has also agreed to dismiss the pending litigation between the parties concerning the restructuring transactions announced by MBIA on February 18, 2009 (the "Transformation" ) and the pending litigation between the parties concerning the senior debt consent solicitation completed by MBIA in the fourth quarter of 2012. In addition, Bank of America agreed to withdraw the purported "notice of default" it sent in connection with such consent solicitation.

Under the terms of the BofA Settlement Agreement, the dismissals of the litigations referenced above are initially being filed on a "without prejudice" basis. The parties will refile such dismissals on a "with prejudice" basis provided that, within the one-year period following execution of the BofA Settlement Agreement, none of the claims released pursuant to the BofA Settlement Agreement are reinstated and neither party is required to make a payment on any such released claims. The Company views the likelihood of such an event as remote, and thus expects that the litigation dismissals will be filed on a "with prejudice" basis at the expiration of such one-year period.

MBIA Corp.'s policies insuring the residential mortgage-backed securities ( "RMBS" ) securitizations originated by Countrywide will continue to be in full force and effect, and MBIA Corp. will continue to make timely payments of principal and interest if there are shortfalls when due under such policies. Bank of America will have no further representation and warranty liability with respect to the origination of the mortgage loans in the MBIA-insured Countrywide and certain other securitizations.

In addition, MBIA Insurance Corporation has entered into a \$500 million three-year secured revolving credit agreement with Blue Ridge (the "Blue Ridge Secured Loan" ). During the third quarter of 2013, MBIA Insurance Corporation borrowed \$50 million under this agreement. Refer to Note 9: Debt for a discussion of the Blue Ridge Secured Loan.

The payment from Bank of America, including the MBIA Inc. notes, was used by MBIA Corp. to repay the outstanding balance and accrued interest on the National Secured Loan. The National Secured Loan balance of \$1.7 billion as of March 31, 2013 was reduced to approximately \$1.6 billion prior to the Bank of America settlement as a result of the receipt of \$110 million in settlement of Flagstar Bank's put-back obligation.

The value of the settlement is consistent with amounts recorded on MBIA Corp.'s statutory balance sheet as of December 31, 2012. MBIA Corp.'s liquidity and capital risk profile has substantially improved as a result of the settlement.

Pursuant to the anti-dilution provisions of warrants that were issued by MBIA to Warburg Pincus Private Equity X, L.P. and certain of its affiliates ( "Warburg Pincus" ) pursuant to an Investment Agreement, dated as of December 10, 2007, as amended and restated as of February 6, 2008, by and between MBIA and Warburg Pincus, the exercise price under such warrants was decreased and the aggregate number of shares of MBIA common stock to be issued upon exercise of such warrants was increased, in each case as a result of the issuance of the warrant to Blue Ridge. The adjustments to the exercise price and number of such underlying shares did not have a material dilutive effect on the MBIA common stock. In addition, under the Investment Agreement, Warburg Pincus has certain gross up rights that are triggered in connection with the offering by the Company of any equity securities. As such, in August of 2013, MBIA issued Warburg Pincus a five-year warrant to purchase 1.91 million shares of MBIA common stock at an exercise price of \$9.59 per share.

##### *Societe Generale Settlement*

In May of 2013, the Company entered into an agreement with Societe Generale pursuant to which the Company commuted \$4.2 billion of gross insured exposure comprising asset-backed securities ( "ABS" ) collateralized debt obligations ( "CDOs" ), structured commercial mortgage-backed securities ( "CMBS" ) pools and CRE CDOs. The amount MBIA paid to Societe Generale in consideration of commuting its insured exposure is consistent with MBIA Corp.'s December 31, 2012 aggregate statutory loss reserves for the exposures commuted. Also, pursuant to the agreement, Societe Generale agreed to dismiss the pending litigation between the parties concerning the Transformation, which includes any appeals of the decision denying the Article 78 petition and the plenary case.



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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

### **Note 1: Business Developments and Risks and Uncertainties (continued)**

#### *Residential Capital LLC Agreement*

In May of 2013, the Company and the other Consenting Claimants, Residential Capital LLC ( "ResCap" ) and Ally Financial Inc. ( "Ally" ), agreed to the terms of a comprehensive plan agreement to support ResCap's Chapter 11 plan. The confirmation of ResCap's Chapter 11 plan would resolve MBIA Corp.'s claims against the Residential Funding Company, LLC ( "RFC" ), GMAC Mortgage LLC ( "GMAC" ) and ResCap estates, and Ally. In June of 2013, the bankruptcy court issued a Memorandum Opinion approving the Plan Support Agreement (the "Plan" ). The Plan is now subject to voting by creditors as well as a confirmation hearing by the bankruptcy court. All creditor ballots were due back by October 21, 2013 and as of the date of this report, the results had not been tallied. There can be no assurance that the Plan will be confirmed. Refer to Note 5: Loss and Loss Adjustment Expense Reserves for a discussion of the ResCap agreement.

#### *Transformation Litigation*

Subsequent to the BofA Settlement Agreement and the Societe Generale settlement, all litigation brought originally by the group of eighteen domestic and international financial institutions relating to the establishment of National has been resolved.

#### *Other*

As of September 30, 2013, the liquidity position of MBIA Inc., which consists of the liquidity positions of the Company's corporate segment and asset/liability products segment, was \$282 million compared with \$239 million as of December 31, 2012. Subsequent to September 30, 2013, National declared and paid a dividend of \$214 million to its ultimate parent, MBIA Inc. During the nine months ended September 30, 2013, \$115 million was released from an escrow account under the MBIA group's tax sharing agreement (the "Tax Escrow Account" ), which resulted in an increase to MBIA's liquidity position. Management believes that MBIA can support its operating needs for the foreseeable future primarily from its existing liquidity position, expected subsidiary dividends and additional anticipated releases of assets from the Tax Escrow Account, which releases are subject to the risks of National incurring net tax losses in the future and/or declines in the value of the assets held in the Tax Escrow Account. As of September 30, 2013 and December 31, 2012, MBIA Corp.'s cash and liquid assets, that were immediately available, totaled \$97 million and \$345 million, respectively. The Company believes MBIA Corp.'s current liquidity position, together with future cash inflows and amounts available under the Blue Ridge Secured Loan, is adequate to make expected future claim payments.

The combination of commutation payments to reduce liabilities and claim payments have placed liquidity pressure on MBIA Corp. MBIA Corp. continues to seek to reduce both the absolute amount and the volatility of its obligations and potential future claim payments through the execution of commutations of insurance policies. During the nine months ended September 30, 2013, MBIA Corp. commuted \$19.9 billion of gross insured exposure, primarily comprising structured CMBS pools, investment grade CDOs, ABS CDOs, first-lien subprime RMBS, high yield corporate CDOs, CRE CDOs, structured insurance securities, and first-lien alternative A-paper ( "Alt-A" ) RMBS.



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**MBIA Inc. and Subsidiaries**

**Notes to Consolidated Financial Statements (Unaudited)**

**Note 1: Business Developments and Risks and Uncertainties (continued)**

***Risks and Uncertainties***

The Company's financial statements include estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. The outcome of certain significant risks and uncertainties could cause the Company to revise its estimates and assumptions or could cause actual results to differ from the Company's estimates. While the Company believes it continues to have sufficient capital and liquidity to meet all of its expected obligations, if one or more possible adverse outcomes were to be realized, its statutory capital, financial position, results of operations and cash flows could be materially and adversely affected. Significant risks and uncertainties that could affect amounts reported in the Company's financial statements in future periods include, but are not limited to, the following:

The amount and timing of potential claims from the Company's second-lien RMBS and remaining insured CMBS pools are potentially volatile, as are the projected collections of excess spread and the remaining put-back recoverables. However, management's expected liquidity and capital forecasts for MBIA Corp., which include expected availability of draws under the Blue Ridge Secured Loan and expected recoveries from the ResCap agreement, reflect adequate resources to pay expected claims. Further, the remaining insured portfolio, aside from these exposures, could deteriorate and result in loss reserves and claim payments. While management believes MBIA Corp. will have adequate resources to pay expected claims, if MBIA Corp. experiences higher than expected claim payments or is unable to commute the remaining exposures that represent substantial risk to the Company, MBIA Corp. may ultimately have insufficient resources to continue to pay claims, which could cause the NYSDFS to put MBIA Insurance Corporation into a rehabilitation or liquidation proceeding. Refer to Note 5: Loss and Loss Adjustment Expense Reserves for information about MBIA Corp.'s reserves and recoveries.

The Company's ability to commute insured transactions is limited by available liquidity, including the availability of the Blue Ridge Secured Loan, recoveries from the ResCap agreement and the use of other available financing structures and liquidity, some of which could be subject to regulatory approval by the NYSDFS and/or the United Kingdom's (U.K.) Prudential Regulation Authority. The Company's primary strategy for managing its CMBS pool and ABS CDO exposures has been commutations. There can be no assurance that the Company will be able to fund further commutations through borrowings or otherwise. Refer to Note 5: Loss and Loss Adjustment Expense Reserves for information about the Company's estimate of losses on its exposures.

As of September 30, 2013, MBIA Insurance Corporation was not in compliance with a requirement under the New York Insurance Law (NYIL) to hold qualifying assets in an amount necessary to satisfy its contingency reserves. MBIA Insurance Corporation has reported the deficit to the NYSDFS. In addition, as of September 30, 2013, MBIA Insurance Corporation exceeded its aggregate risk limits and reported an overage related to its single risk limits under NYIL. MBIA Insurance Corporation plans to notify the NYSDFS of these overages and submit a plan to achieve compliance with its limits. While the NYSDFS has not taken action against MBIA Insurance Corporation, the NYSDFS may impose remedial actions for failing to meet these requirements.

MBIA Inc. continues to have liquidity risk. If invested asset performance deteriorates, or the flow of dividends from subsidiaries is interrupted, its liquidity position would be eroded over time. However, management believes that MBIA Inc. has sufficient liquidity resources to meet all of its obligations for the foreseeable future. In order to meet its liquidity requirements, MBIA Inc. may use free cash or other assets or use its ability to finance through intercompany or third-party facilities, although there can be no assurance that these strategies will be available or adequate. A failure by MBIA Inc. to settle liabilities that are also insured by MBIA Corp. could result in claims on MBIA Corp.

Changes in fair value of insured credit derivatives can be caused by general market conditions, volatility in MBIA Corp. s credit spreads and volatility on the underlying collateral assets on insured credit derivatives. This may result in significant unrealized gains and losses in the Company s reported results of operations. Refer to Note 6: Fair Value of Financial Instruments for information about the Company s valuation of insured credit derivatives.

**Note 2: Significant Accounting Policies**

The Company has disclosed its significant accounting policies in Note 2: Significant Accounting Policies in the Notes to Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2012. The following significant accounting policies provide an update to those included in the Company s Annual Report on Form 10-K.

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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

### **Note 2: Significant Accounting Policies (continued)**

#### ***Basis of Presentation***

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and, accordingly, do not include all of the information and disclosures required by accounting principles generally accepted in the United States of America ( GAAP ) for annual periods. These statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Annual Report on Form 10-K for the year ended December 31, 2012. The accompanying consolidated financial statements have not been audited by an independent registered public accounting firm in accordance with the standards of the Public Company Accounting Oversight Board (U.S.), but in the opinion of management such financial statements include all adjustments, consisting only of normal recurring adjustments, necessary for the fair statement of the Company's consolidated financial position and results of operations. All material intercompany balances and transactions have been eliminated.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. As additional information becomes available or actual amounts become determinable, the recorded estimates are revised and reflected in operating results.

The results of operations for the three and nine months ended September 30, 2013 may not be indicative of the results that may be expected for the year ending December 31, 2013. The December 31, 2012 consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by GAAP for annual periods. Certain amounts have been reclassified in the prior year's financial statements to conform to the current presentation. This includes the reclassification of accrued interest on surplus notes and senior notes from Other liabilities to Long-term debt on the Company's consolidated balance sheets. Refer to Note 9: Debt for information about the amounts of this reclassification. These reclassifications had no impact on total revenues, expenses, assets, liabilities, shareholders' equity, operating cash flows, investing cash flows, or financing cash flows for all periods presented.

### **Note 3: Recent Accounting Pronouncements**

#### ***Recently Adopted Accounting Standards***

##### ***Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income (ASU 2013-02)***

In February 2013, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) 2013-02, Comprehensive Income (Topic 220) Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income that requires an entity to present information about the amounts reclassified out of accumulated other comprehensive income ( AOCI ) by component and to present significant amounts reclassified out of AOCI by the respective line items of net income. The amendment only affects the Company's disclosures and does not affect the Company's consolidated balance sheets, results of operations, or cash flows. The Company adopted this standard in the first quarter of 2013.

##### ***Disclosures about Offsetting Assets and Liabilities (ASU 2011-11)***

In December 2011, the FASB issued ASU 2011-11, Balance Sheet (Topic 210) Disclosures about Offsetting Assets and Liabilities . ASU 2011-11 creates new disclosure requirements about the nature of the Company's rights of setoff and related arrangements associated with its financial instruments and derivative instruments. This amendment does not change the existing offsetting eligibility criteria or the permitted balance sheet presentation for those instruments that meet the eligibility criteria. The disclosure requirement was effective for the Company beginning in the first quarter of 2013. In January 2013, the FASB issued ASU 2013-01, Balance Sheet (Topic 210) Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities . ASU 2013-01 clarifies that ASU 2011-11 applies only to derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with specific criteria

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contained in the FASB Accounting Standards Codification or subject to a master netting arrangement or similar agreement. These standards only affect the Company's disclosures and do not affect the Company's consolidated balance sheets, results of operations, or cash flows. The Company adopted this standard in the first quarter of 2013.

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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 3: Recent Accounting Pronouncements (continued)**

##### ***Recent Accounting Developments***

##### ***Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (ASU 2013-11)***

In July 2013, the FASB issued ASU 2013-11, Income Taxes (Topic 740) Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. ASU 2013-11 requires presentation of an unrecognized tax benefit (UTB) as a reduction to a deferred tax asset when a net operating loss (NOL) carryforward, a similar tax loss, or a tax credit carryforward exists in the same tax year and jurisdiction as the UTB. ASU 2013-11 does not affect the recognition or measurement of uncertain tax positions under Income Taxes (Topic 740) and does not affect any related tax disclosures. ASU 2013-11 is effective for interim and annual periods beginning January 1, 2014 with early adoption permitted. The Company currently presents any UTBs as a reduction to a deferred tax asset in accordance with ASU 2013-11 as all of its UTBs relate to the same tax years and jurisdictions in which NOLs exist, therefore, this standard will not affect the Company's consolidated balance sheets, results of operations, or cash flows.

#### **Note 4: Variable Interest Entities**

##### ***Structured Finance and International Insurance***

Through MBIA's structured finance and international insurance segment, the Company provides credit protection to issuers of obligations that may involve issuer-sponsored special purpose entities (SPEs). An SPE may be considered a variable interest entity (VIE) to the extent the SPE's total equity at risk is not sufficient to permit the SPE to finance its activities without additional subordinated financial support or its equity investors lack any one of the following characteristics: (i) the power to direct the activities of the SPE that most significantly impact the entity's economic performance or (ii) the obligation to absorb the expected losses of the entity or the right to receive the expected residual returns of the entity. A holder of a variable interest or interests in a VIE is required to assess whether it has a controlling financial interest, and thus is required to consolidate the entity as primary beneficiary. An assessment of a controlling financial interest identifies the primary beneficiary as the variable interest holder that has both of the following characteristics: (i) the power to direct the activities of the VIE that most significantly impact the entity's economic performance and (ii) the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the VIE. The primary beneficiary is required to consolidate the VIE. An ongoing reassessment of controlling financial interest is required to be performed based on any substantive changes in facts and circumstances involving the VIE and its variable interests.

The Company evaluates issuer-sponsored SPEs initially to determine if an entity is a VIE, and is required to reconsider its initial determination if certain events occur. For all entities determined to be VIEs, MBIA performs an ongoing reassessment to determine whether its guarantee to provide credit protection on obligations issued by VIEs provides the Company with a controlling financial interest. Based on its ongoing reassessment of controlling financial interest, the Company determines whether a VIE is required to be consolidated or deconsolidated.

The Company makes its determination for consolidation based on a qualitative assessment of the purpose and design of a VIE, the terms and characteristics of variable interests of an entity, and the risks a VIE is designed to create and pass through to holders of variable interests. The Company generally provides credit protection on obligations issued by VIEs, and holds certain contractual rights according to the purpose and design of a VIE. The Company may have the ability to direct certain activities of a VIE depending on facts and circumstances, including the occurrence of certain contingent events, and these activities may be considered the activities of a VIE that most significantly impact the entity's economic performance. The Company generally considers its guarantee of principal and interest payments of insured obligations, given nonperformance by a VIE, to be an obligation to absorb losses of the entity that could potentially be significant to the VIE. At the time the Company determines it has the ability to direct the activities of a VIE that most significantly impact the economic performance of the entity based on facts and circumstances, MBIA is deemed to have a controlling financial interest in the VIE and is required to consolidate the entity as primary beneficiary. The Company performs an ongoing reassessment of controlling financial interest that may result in consolidation or

deconsolidation of any VIE.

***Wind-down Operations***

In its asset/liability products segment, the Company invests in obligations issued by issuer-sponsored SPEs which are included in fixed-maturity securities held as available-for-sale ( AFS ). The Company evaluates issuer-sponsored SPEs to determine if the entity is a VIE. For all entities determined to be VIEs, the Company evaluates whether its investment is determined to have both of the characteristics of a controlling financial interest in the VIE. The Company performs an ongoing reassessment of controlling financial interests in issuer-sponsored VIEs based on investments held. MBIA's wind-down operations do not have a controlling financial interest in any issuer-sponsored VIEs and are not the primary beneficiary of any issuer-sponsored VIEs.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 4: Variable Interest Entities (continued)**

In the conduit segment, the Company has managed and administered two conduits that invested primarily in debt securities and were funded through the issuance of VIE notes and long-term debt. MBIA Corp. insures the debt obligations of the conduits, and provides credit protection on certain assets held by the conduits. The conduits are VIEs and are consolidated by the Company as primary beneficiary. In 2012, all debt securities held by one of the conduits were entirely repaid, and the proceeds were used to repay all outstanding long-term debt of this conduit. The Company subsequently dissolved this conduit, and no longer provides any related credit protection.

**Nonconsolidated VIEs***Insurance*

The following tables present the total assets of nonconsolidated VIEs in which the Company holds a variable interest as of September 30, 2013 and December 31, 2012, through its insurance operations. The following tables also present the Company's maximum exposure to loss for nonconsolidated VIEs and carrying values of the assets and liabilities for its interests in these VIEs as of September 30, 2013 and December 31, 2012. The Company has aggregated nonconsolidated VIEs based on the underlying credit exposure of the insured obligation. The nature of the Company's variable interests in nonconsolidated VIEs is related to financial guarantees, insured CDS contracts and any investments in obligations issued by nonconsolidated VIEs.

In millions	September 30, 2013			Carrying Value of Assets		Carrying Value of Liabilities		
	VIE Assets	Maximum Exposure to Loss	Investments <sup>(1)</sup>	Premiums Receivable <sup>(2)</sup>	Insurance Loss Recoverable <sup>(3)</sup>	Unearned Premium Revenue <sup>(4)</sup>	Adjustment Expense Reserves <sup>(5)</sup>	Derivative Liabilities <sup>(6)</sup>
<b>Insurance:</b>								
<b>Global structured finance:</b>								
Collateralized debt obligations	\$ 13,564	\$ 7,972	\$ 118	\$ 45	\$ 5	\$ 38	\$ 26	\$ 94
Mortgage-backed residential	22,400	9,915	11	57	696	56	374	5
Mortgage-backed commercial	2,010	1,102	-	1	-	1	-	-
Consumer asset-backed	6,788	2,888	9	21	-	20	17	-
Corporate asset-backed	14,258	7,817	-	87	19	103	-	-
Total global structured finance	59,020	29,694	138	211	720	218	417	99
Global public finance	51,060	20,258	-	205	-	250	5	-
Total insurance	\$ 110,080	\$ 49,952	\$ 138	\$ 416	\$ 720	\$ 468	\$ 422	\$ 99

(1) - Reported within Investments on MBIA's consolidated balance sheets.

(2) - Reported within Premiums receivable on MBIA's consolidated balance sheets.

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- (3) - Reported within Insurance loss recoverable on MBIA's consolidated balance sheets.
- (4) - Reported within Unearned premium revenue on MBIA's consolidated balance sheets.
- (5) - Reported within Loss and loss adjustment expense reserves on MBIA's consolidated balance sheets.
- (6) - Reported within Derivative liabilities on MBIA's consolidated balance sheets.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 4: Variable Interest Entities (continued)**

In millions	December 31, 2012 Carrying Value of Assets				Carrying Value of Liabilities Loss and Loss Adjustment Expense Reserves <sup>(5)</sup>			
	VIE Assets	Maximum Exposure to Loss	Investments <sup>(1)</sup>	Premiums Receivable <sup>(2)</sup>	Insurance Loss Recoverable <sup>(3)</sup>	Unearned Premium Revenue <sup>(4)</sup>	Derivative Liabilities <sup>(6)</sup>	
<b>Insurance:</b>								
Global structured finance:								
Collateralized debt obligations	\$ 16,925	\$ 10,873	\$ -	\$ 62	\$ 5	\$ 55	\$ 37	\$ 74
Mortgage-backed residential	34,061	13,075	11	77	3,278	75	440	4
Mortgage-backed commercial	4,801	2,432	-	2	-	2	-	-
Consumer asset-backed	5,820	3,086	10	19	-	19	21	-
Corporate asset-backed	19,980	9,981	-	123	13	140	-	-
Total global structured finance	81,587	39,447	21	283	3,296	291	498	78
Global public finance	39,259	21,346	-	220	-	267	4	-
Total insurance	\$ 120,846	\$ 60,793	\$ 21	\$ 503	\$ 3,296	\$ 558	\$ 502	\$ 78

(1) - Reported within Investments on MBIA's consolidated balance sheets.

(2) - Reported within Premiums receivable on MBIA's consolidated balance sheets.

(3) - Reported within Insurance loss recoverable on MBIA's consolidated balance sheets.

(4) - Reported within Unearned premium revenue on MBIA's consolidated balance sheets.

(5) - Reported within Loss and loss adjustment expense reserves on MBIA's consolidated balance sheets.

(6) - Reported within Derivative liabilities on MBIA's consolidated balance sheets.

The maximum exposure to loss as a result of MBIA's variable interests in VIEs is represented by insurance in force. Insurance in force is the maximum future payments of principal and interest, net of cessions to reinsurers, which may be required under commitments to make payments on insured obligations issued by nonconsolidated VIEs.

*Other*

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During the first quarter of 2013, Trifinium Advisors (UK) Limited ( Trifinium ) began managing a VIE that issues notes for the purpose of funding loans to the U.K. social housing sector. Assets of the VIE totaled approximately \$144 million as of September 30, 2013. Trifinium holds de minimis variable interests in the VIE, has no obligation or commitment to provide the financial support or liquidity to the VIE, and is not the primary beneficiary.

### *Consolidated VIEs*

The carrying amounts of assets and liabilities of consolidated VIEs were \$6.4 billion and \$5.4 billion, respectively, as of September 30, 2013, and \$8.3 billion and \$7.3 billion, respectively, as of December 31, 2012. The carrying amounts of assets and liabilities are presented separately in Assets of consolidated variable interest entities and Liabilities of consolidated variable interest entities on the Company's consolidated balance sheets. Additional VIEs are consolidated or deconsolidated based on an ongoing reassessment of controlling financial interest, when events occur or circumstances arise, and whether the ability to exercise rights that constitute power to direct activities of any VIEs are present according to the design and characteristics of these entities. No additional VIEs were consolidated during the nine months ended September 30, 2013 and 2012. There were no net realized gains or losses recorded in the three months ended September 30, 2013 and 2012. During the nine months ended September 30, 2013, the Company recorded a net realized gain of \$1 million related to the deconsolidation of VIEs. There were no net realized gains or losses recorded in the nine months ended September 30, 2012.

Holders of insured obligations of issuer-sponsored VIEs related to the Company's structured finance and international insurance segment do not have recourse to the general assets of MBIA. In the event of nonpayment of an insured obligation issued by a consolidated VIE, the Company is obligated to pay principal and interest, when due, on the respective insured obligation only. The Company's exposure to consolidated VIEs is limited to the credit protection provided on insured obligations and any additional variable interests held by MBIA. Creditors of the conduits do not have recourse to the general assets of MBIA apart from the financial guarantee insurance policies provided by MBIA Corp. on insured obligations issued by the conduits.

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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 5: Loss and Loss Adjustment Expense Reserves**

##### *Loss and Loss Adjustment Expense Process*

#### **U.S. Public Finance**

U.S. public finance insured transactions consist of municipal bonds, including tax-exempt and taxable indebtedness of U.S. political subdivisions, as well as utility districts, airports, health care institutions, higher educational facilities, student loan issuers, housing authorities and other similar agencies and obligations issued by private entities that finance projects that serve a substantial public purpose. The Company estimates future losses by utilizing probability-weighted scenarios that are customized to each insured transaction. Future loss estimates consider debt service due for each insured transaction, which includes par outstanding and interest due.

The Company has established loss and loss adjustment expense ( LAE ) reserves and an insurance loss recoverable of \$94 million and \$17 million, respectively, as of September 30, 2013. During the nine months ended September 30, 2013, losses and LAE was \$105 million, primarily related to certain general obligation bonds and the loss related to the difference in the value of the salvage receivable previously recorded and the fair market value of the marketable securities received in connection with the restructuring of a gaming revenue transaction.

Certain local governments remain under extreme financial and budgetary stress and several have filed for protection under the United States Bankruptcy Code, or have entered into state statutory proceedings established to assist municipalities in managing through periods of severe fiscal stress. This could lead to an increase in defaults by such entities on the payment of their obligations and losses or impairments on a greater number of the Company's insured transactions. The Company monitors and analyzes these situations closely, however, the overall extent and duration of such events are uncertain. As of September 30, 2013, the Company had \$131.5 billion of gross par outstanding on general obligations, of which \$251 million was reflected on the Company's Classified List. Capital appreciation bonds are reported at the par amount at the time of issuance of the insurance policy.

#### **Structured Finance and International**

As of September 30, 2013, the majority of the structured finance and international insurance segment's case basis reserves and insurance loss recoveries recorded in accordance with GAAP were related to insured second-lien and first-lien RMBS transactions. These reserves and recoveries do not include estimates for policies insuring credit derivatives and do not include losses and recoveries on financial guarantee VIEs that are eliminated in consolidation. Policies insuring credit derivative contracts are accounted for as derivatives and carried at fair value under GAAP. The fair values of insured derivative contracts are influenced by a variety of market and transaction-specific factors that may be unrelated to potential future claim payments under the Company's insurance policies. In the absence of credit impairments on insured derivative contracts or the early termination of such contracts at a loss, the cumulative unrealized losses recorded from fair valuing these contracts should reverse before or at the maturity of the contracts.

Notwithstanding the difference in accounting under GAAP for financial guarantee policies and the Company's insured derivatives, insured derivatives have similar terms, conditions, risks, and economic profiles to financial guarantee insurance policies, and therefore, are evaluated by the Company for loss (referred to as credit impairment herein) and LAE periodically in a manner similar to the way that loss and LAE reserves are estimated for financial guarantee insurance policies. Credit impairments represent actual payments and collections plus the present value of estimated expected future claim payments, net of recoveries. MBIA Insurance Corporation's expected future claim payments for insured derivatives were discounted using a rate of 5.72%, the same rate it used to calculate its statutory loss reserves as of September 30, 2013. These credit impairments, calculated in accordance with statutory accounting principles ( U.S. STAT ), differ from the fair values recorded in the Company's consolidated financial statements. The Company considers its credit impairment estimates as critical information for investors as it provides information about loss payments the Company expects to make on insured derivative contracts. As a result, the following loss and LAE process discussion includes information about loss and LAE activity recorded in accordance with GAAP for financial guarantee insurance policies and credit impairments estimated in accordance with U.S. STAT for insured derivative contracts. Refer to Note 6: Fair Value of Financial Instruments included herein for additional information about the Company's insured credit derivative contracts.

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To date, the Company has resolved or agreed to resolve substantially all of its contract claims (referred to as "put-back" claims) related to those mortgage loans whose inclusion in insured securitizations failed to comply with representations and warranties ("ineligible loans"), with the exception of those ineligible loans securitized by Credit Suisse 2007-2 in the home equity mortgage trust ("HEMT") securitization. Credit Suisse has challenged the Company's assessment of the ineligibility of individual mortgage loans and the dispute is the subject of litigation for which there is no assurance that the Company will prevail.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 5: Loss and Loss Adjustment Expense Reserves (continued)***RMBS Case Basis Reserves and Recoveries (Financial Guarantees)*

The Company's RMBS reserves and recoveries relate to financial guarantee insurance policies. The Company calculated RMBS case basis reserves as of September 30, 2013 for both second-lien and first-lien RMBS transactions using a process called the Roll Rate Methodology. The Roll Rate Methodology is a multi-step process using a database of loan level information, a proprietary internal cash flow model, and a commercially available model to estimate expected ultimate cumulative losses on insured bonds. Roll Rate is defined as the probability that current loans become delinquent and that loans in the delinquent pipeline are charged-off or liquidated. Generally, Roll Rates are calculated for the previous three months and averaged. The loss reserve estimates are based on a probability-weighted average of three scenarios of loan losses (base case, stress case, and an additional stress case).

In calculating ultimate cumulative losses for RMBS, the Company estimates the amount of loans that are expected to be charged-off (deemed uncollectible by servicers of the transactions) or liquidated in the future. The Company assumes that charged-off loans have zero recovery values.

**Second-lien RMBS Reserves**

The Company's second-lien RMBS case basis reserves as of September 30, 2013 relate to RMBS backed by home equity lines of credit ( HELOC ) and closed-end second mortgages ( CES ).

The Roll Rates for 30-59 day delinquent loans and 60-89 day delinquent loans are calculated on a transaction-specific basis. The Company assumes that the Roll Rate for 90+ day delinquent loans, excluding foreclosures and Real Estate Owned ( REO ) is 95%. The Roll Rates are applied to the amounts in the respective delinquency buckets based on delinquencies as of August 31, 2013 to estimate future losses from loans that are delinquent as of the current reporting period.

Roll Rates for loans that are current as of August 31, 2013 ( Current Roll to Loss ) are also calculated on a transaction-specific basis. A proportion of loans reported current as of August 31, 2013 is assumed to become delinquent every month, at a Current Roll to Loss rate that persists at a high level for a time and subsequently starts to decline. A key assumption in the model is the period of time in which the Company projects high levels of Current Roll to Loss to persist. The Company runs multiple scenarios, each with varying periods of time, for which the high levels of Current Roll to Loss rates persist. Loss reserves are calculated by using a weighted average of these scenarios, with the majority of the probability assigned to stressful scenarios where the high levels of Current Roll to Loss rates persist for six or twenty four months before reverting to historic levels. In the base case scenario, the Company assumes that the Current Roll to Loss begins to decline immediately and continues to decline over the next six months to 25% of their levels as of August 31, 2013. For example, in the base case, as of August 31, 2013, if the amount of current loans which become 30-59 days delinquent is 10%, and recent performance suggests that 30% of those loans will be charged-off, the Current Roll to Loss for the transaction is 3%. In the base case, it is then assumed that the Current Roll to Loss will reduce linearly to 25% of its original value over the next six months (i.e., 3% will linearly reduce to 0.75% over the six months from September 2013 to February 2014). After that six-month period, the Company further reduces the Current Roll to Loss to 0% by early to mid-2014 with the expectation that the performing seasoned loans will eventually result in loan performance reverting to lower levels of default consistent with history.

In addition, in the Company's loss reserve models for transactions secured by HELOCs, the Company considers borrower draw and prepayment rates and factors that could affect the excess spread generated by current loans, which offsets losses and reduces payments. For HELOCs, the current three-month average draw rate is generally used to project future draws on the line. For HELOCs and transactions secured by fixed-rate CES, the three-month average conditional prepayment rate is generally used to start the projection for trends in voluntary principal prepayments. Due to the current volatility in mortgage prepayment rates, which influence mortgage refinancing and voluntary principal prepayment rates, the Company used historical average mortgage rates to model its loss reserves in the third quarter of 2013. Projected cash flows are also based on an assumed constant basis spread between floating rate assets and floating rate insured debt obligations (the difference between prime and London

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Interbank Offered Rate ( LIBOR ) interest rates, minus any applicable fees). For all transactions, cash flow models consider allocations and other structural aspects of the transactions, including managed amortization periods, rapid amortization periods and claims against MBIA Corp. 's insurance policy consistent with such policy 's terms and conditions. In developing multiple loss scenarios, stress is applied by elongating the Current Roll to Loss rate for various periods, simulating a slower improvement in the transaction performance. The estimated net claims from the procedure above are then discounted using a risk-free rate to a net present value reflecting MBIA 's general obligation to pay claims over time and not on an accelerated basis. The above assumptions represent MBIA 's probability-weighted estimates of how transactions will perform over time.

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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 5: Loss and Loss Adjustment Expense Reserves (continued)**

The Company monitors portfolio performance on a monthly basis against projected performance, reviewing delinquencies, Roll Rates, and prepayment rates (including voluntary and involuntary). However, loan performance remains difficult to predict and losses may exceed expectations. In the event of a material deviation in actual performance from projected performance, the Company would increase or decrease the case basis reserves accordingly. If actual performance were to remain at the peak levels for six additional months compared to the probability-weighted outcome currently used by the Company, the addition to the case basis reserves would be approximately \$85 million.

#### **Second-lien RMBS Recoveries**

The Company primarily records two types of recoveries related to insured second-lien RMBS exposures; recoveries related to put-back claims on ineligible mortgages and excess spread that is generated from performing loans in the insured transactions.

#### *Ineligible Mortgage Loans*

As of September 30, 2013, the Company recorded estimated recoveries of \$1.1 billion, gross of income taxes, related to second-lien RMBS put-back claims on ineligible mortgage loans, consisting of \$18 million included in Insurance loss recoverable and \$1.1 billion included in Loan repurchase commitments presented under the heading Assets of consolidated variable interest entities on the Company's consolidated balance sheets. As of September 30, 2013 and December 31, 2012, the Company's estimated recoveries after income taxes calculated at the federal statutory rate of 35%, were \$737 million and \$2.3 billion, respectively, which was 23% and 73% of the consolidated total shareholders' equity of MBIA, excluding preferred stock of subsidiaries and noncontrolling interests, respectively. As of September 30, 2013, the remaining estimated recoveries relate to the Company's claims based on ineligible mortgage loans asserted against Credit Suisse and the agreed to claims and recoveries against the bankruptcy estates of RFC, GMAC and ResCap as reflected in a disclosure statement filed in August of 2013.

On May 14, 2012, ResCap and its wholly-owned subsidiary companies, RFC and GMAC, each filed *for bankruptcy protection under Chapter 11 of the United States Bankruptcy Code*. MBIA asserted claims based on the inclusion of ineligible loans against RFC, GMAC and ResCap, based upon the direct contractual relationship between the Company, RFC and GMAC.

As of May 23, 2013, Ally, ResCap, RFC, GMAC and the Consenting Claimants (which includes MBIA), among other parties, executed a term sheet and supplemental term sheet agreeing to, among other things, a settlement amount of \$796 million to be paid to MBIA as part of a proposed plan to resolve claims against Ally and RFC, GMAC and ResCap. In August of 2013, a disclosure statement filed indicated an increased expected recovery for MBIA of approximately \$828 million. The increased recovery was primarily due to the favorable disposition of assets and settlements of claims. The settlement and anticipated recoveries are consistent with the put-back recoveries recorded by the Company. The agreement will be implemented through a plan of reorganization in ResCap's Chapter 11 cases, subject to bankruptcy court approval. In June of 2013, the bankruptcy court issued a Memorandum Opinion approving the Plan. The Plan is subject to confirmation by the bankruptcy court, with confirmation hearings currently scheduled in November 2013. MBIA anticipates an initial distribution of funds to the Company and other claimants in late 2013 or early 2014. This anticipated timeline may change due to developments related to the Junior Secured Note litigation, which occurred in October of 2013, or other matters that develop in the course of events in the bankruptcy court plan confirmation process.

The Company continues to refine the indicative scenarios used to calculate put-back recoveries for ResCap based upon information received during the bankruptcy process. The Company has made additional adjustments to its recovery calculations related to ResCap in consideration of the agreed upon recovery amount as described in the executed term sheet, supplemental term sheet and plan support agreement submitted in motions filed in May of 2013. During the third quarter of 2013, MBIA made additional refinements to the probability assumptions utilized to calculate the Company's expected recoveries. The revisions were based upon the submission of documents related to the Plan.

In addition, the Company believes that it will prevail in enforcing its contractual put-back rights against Credit Suisse. Based on the Company's assessment of the strength of these claims, the Company believes it is entitled to collect the full amount of its incurred losses, and interest on amounts paid. However, uncertainty remains with respect to the ultimate outcome of the litigation with Credit Suisse, which is contemplated in

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the scenario based-modeling the Company utilizes. The Credit Suisse recovery scenarios are based on the amount of incurred losses measured against certain probabilities of ultimate resolution of the dispute with Credit Suisse over the inclusion of ineligible mortgage loans in the HEMT securitization. Most of the probability weight is assigned to partial recovery scenarios.

Expected cash inflows from put-back recoveries are discounted using the current risk-free discount rates associated with the underlying transaction's cash flows which ranged from 1.4% to 2.7%, depending upon the transaction's expected average life, which ranged from 5.0 years to 10.4 years.



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### **MBIA Inc. and Subsidiaries**

#### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 5: Loss and Loss Adjustment Expense Reserves (continued)**

The Company consistently reviews the approach and assumptions it applies to calculate put-back recoveries. The same transactional documents that provide the Company with its put-back rights against Credit Suisse also provide that the Company is entitled to reimbursement of interest on paid claims at a prescribed interest rate. Following Judge Jed Rakoff's decision on February 7, 2013 in the Assured Guaranty v. Flagstar case (Assured Guaranty Municipal Corp. v. Flagstar Bank, 11-cv-02375, U.S. District Court, Southern District of New York (Manhattan)), in which he confirmed Assured Guaranty's analogous right to recover contractual interest in addition to claims paid, the Company has refined its put-back recovery assumptions against Credit Suisse to increase the probability that it will be reimbursed for contractual interest owed on paid claims. Consistent with the Company's probability based put-back recovery calculations, it has determined the interest owed contemplating litigation risk and repayment risk, as well as the potential value in the context of a settlement. The Company continues to maintain that in the context of its put-back litigation, the Company is entitled to receive interest at the New York State statutory rate. However, the Company currently calculates its put-back recoveries using the contractual interest rate, which is lower than the New York State statutory rate.

To date, MBIA has either settled or agreed to settle the majority of the Company's put-back claims, with only Credit Suisse remaining as an outstanding dispute. The settlement amounts have been consistent with the put-back recoveries previously included in the Company's financial statements. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the BofA Settlement Agreement. Additional information on the status of the litigation against Credit Suisse can be found in the Recovery Litigation discussion within Note 14: Commitments and Contingencies.

The Company's assessment of the remaining unsettled recoveries related to insured Credit Suisse second-lien RMBS is principally based on the following factors:

1. the settlement of the majority of the Company's put-back claims with sellers/servicers, including those with Bank of America and Flagstar Bank in May of 2013;
2. Assured Guaranty's favorable court ruling in its put-back litigation against Flagstar Bank, awarding it the vast majority of the claims paid on the relevant transactions plus interest, fees and expenses, as well as their subsequent settlement with Flagstar Bank, which resolved Assured Guaranty's put-back claims; and
3. the court rulings in MBIA's put-back litigations.

The Company continues to consider all relevant facts and circumstances, including the factors described above, in developing its assumptions on expected cash inflows, probability of potential recoveries (including the outcome of litigation) and recovery period. The estimated amount and likelihood of potential recoveries are expected to be revised and supplemented to the extent there are developments in the pending litigation and/or changes to the financial condition of Credit Suisse. While the Company believes it will be successful in realizing recoveries from contractual claims, the ultimate amounts recovered may be materially different from those recorded by the Company given the inherent uncertainty of the manner of resolving the claims (e.g., litigation) and the assumptions used in the required estimation process for accounting purposes which are based, in part, on judgments and other information that are not easily corroborated by historical data or other relevant benchmarks.

All of the Company's policies insuring second-lien RMBS for which litigation has been initiated against sellers/servicers are in the form of financial guarantee insurance contracts. In accordance with GAAP, the Company has not recorded a gain contingency with respect to pending litigation.

*Excess Spread*

As of September 30, 2013, the Company recorded estimated recoveries of \$756 million in reimbursement of past and future expected claims through excess spread in insured second-lien RMBS transactions. Of the expected reimbursement from excess spread, \$669 million is included in Insurance loss recoverable and \$87 million is included in Loss and loss adjustment expense reserves on the Company's consolidated balance sheets. Excess spread is generated by performing loans within insured RMBS securitizations and is the difference between interest inflows on mortgage loan collateral and interest outflows on insured beneficial interests. The amount of excess spread depends on the future delinquency and loss trends, future prime and LIBOR interest rates and borrower refinancing behavior, which results in voluntary prepayments.

First-lien RMBS Reserves

The Company's first-lien RMBS case basis reserves as of September 30, 2013, which primarily relate to RMBS backed by Alt-A and subprime mortgage loans, were determined using the Roll Rate Methodology. The Company assumes that the Roll Rate for loans in foreclosure, REO and bankruptcy are 90%, 90% and 75%, respectively. Roll Rates for current, 30-59 day delinquent loans, 60-89 day delinquent loans and 90+ day delinquent loans are calculated on a transaction-specific basis. The Current Roll to Loss rates stay at the August 31, 2013 level for one month before declining to 25% of this level over a 24-month period.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 5: Loss and Loss Adjustment Expense Reserves (continued)**

The Company estimates future losses by utilizing three different probability-weighted scenarios: base; stress; and additional stress. The three scenarios differ in the roll rates to loss of 90+ day delinquent loans. In the base scenario, the Company uses deal-specific roll rates obtained from historic loan level roll rate data. In the stress scenario, the Company assumes a 90% roll rate for all 90+ day delinquent loans. In the additional stress scenario, the roll rates for each deal are an average of the deal-specific roll rate used in the base scenario and the 90% rate. The Roll Rates are applied to the amounts in each deal's respective 90+ delinquency bucket based on delinquencies as of August 31, 2013 in order to estimate future losses from loans that are delinquent as of September 30, 2013.

In calculating ultimate cumulative losses for first-lien RMBS, the Company estimates the amount of loans that are expected to be liquidated through foreclosure or short sale. The time to liquidation for a defaulted loan is specific to the loan's delinquency bucket with the latest three-month average loss severities generally used to start the projection for trends in loss severities at loan liquidation. The loss severities are reduced over time to account for reduction in the amount of foreclosure inventory, anticipated future increases in home prices, principal amortization of the loan and government foreclosure moratoriums.

*ABS CDOs (Financial Guarantees and Insured Derivatives)*

MBIA's insured ABS CDOs are transactions that include a variety of collateral ranging from corporate bonds to structured finance assets (which includes but are not limited to RMBS related collateral, ABS CDOs, corporate CDOs and collateralized loan obligations). These transactions were insured as either financial guarantee insurance policies or credit derivatives with the majority currently insured in the form of financial guarantees. Since the fourth quarter of 2007, MBIA's insured par exposure within the ABS CDO portfolio has been substantially reduced through a combination of terminations and commutations. Accordingly, as of September 30, 2013, the insured par exposure of the ABS CDO financial guarantee insurance policies and credit derivatives portfolio has declined by approximately 96% of the insured amount as of December 31, 2007.

The Company's ABS CDOs originally benefited from two sources of credit enhancement. First, the subordination in the underlying securities collateralizing the transaction must be fully eroded and second, the subordination below the insured tranche in the CDO transaction must be fully eroded before the insured tranche is subject to a claim. The Company's payment obligations after a default are timely interest and ultimate principal.

The primary factor in estimating reserves on insured ABS CDO policies written as financial guarantee insurance policies and in estimating impairments on insured ABS CDO credit derivatives is the losses associated with the underlying collateral in the transactions. MBIA's approach to establishing reserves or impairments in this portfolio employs a methodology which is similar to other structured finance asset classes insured by MBIA. The Company utilizes up to a total of four probability-weighted scenarios in order to estimate its reserves or impairments for ABS CDOs.

As of September 30, 2013, the Company established loss and LAE reserves totaling \$87 million related to ABS CDO financial guarantee insurance policies after the elimination of \$196 million as a result of consolidating VIEs. For the nine months ended September 30, 2013, the Company had a benefit of \$47 million of losses and LAE recorded in earnings related to ABS CDO financial guarantee insurance policies after the elimination of a \$39 million benefit as a result of consolidating VIEs. In the event of further deteriorating performance of the collateral referenced or held in ABS CDO transactions, the amount of losses estimated by the Company could increase substantially.

*Credit Impairments Related to Structured CMBS Pools, CRE CDOs and CRE Loan Pools (Financial Guarantees and Insured Derivatives)*

Most of the structured CMBS pools, CRE CDOs and CRE loan pools insured by MBIA are accounted for as insured credit derivatives and are carried at fair value in the Company's consolidated financial statements. Since the Company's insured credit derivatives have similar terms, conditions, risks, and economic profiles to its financial guarantee insurance policies, the Company evaluates them for impairment in the same way that it estimates loss and LAE for its financial guarantee policies. The following discussion provides information about the Company's process for estimating credit impairments on these contracts using its statutory loss reserve methodology, determined as the present value of the

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probability-weighted potential future losses, net of estimated recoveries, across multiple scenarios, plus actual payments and collections.

The Company has developed multiple scenarios to consider the range of potential outcomes in the CRE market and their impact on MBIA. The approaches require substantial judgments about the future performance of the underlying loans, and include the following:

The first approach considers the range of commutation agreements achieved over the past several years with multiple counterparties and results in an estimated price to commute the remaining policies. It is customized by counterparty and is dependent upon the level of dialogue with the counterparty and the credit quality and payment profile of the underlying exposure.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 5: Loss and Loss Adjustment Expense Reserves (continued)**

The second approach considers current delinquency rates and uses current and projected net operating income ( NOI ) and capitalization rates ( Cap Rates ) to project losses under two scenarios. These scenarios assume that property performance remains flat for the near term and then improves gradually. Additionally, certain large loans are reviewed individually so that performance and loss severity can be more accurately determined. Other loans are reviewed for factors that may mitigate potential performance. This approach utilizes two scenarios which vary in the levels of expected future defaults.

The last approach is based on a proprietary model developed by reviewing performance data on over 80,000 securitized CRE loans originated between 1992 and 2011. The time period covered during the performance review includes the years 2006 through 2011 because they encompass a period of extreme stress in the economy and the CRE markets. The Company found property type and the debt service coverage ratio to be the most significant determinants of a loan 's average annual default probability, and developed a model based on these factors. The Company then ran Monte Carlo simulations to estimate the timing of defaults and losses at the property level by applying property type-based Cap Rates to estimate the property 's NOI.

The loss severities projected by these scenarios vary widely, from moderate to substantial losses. Actual losses will be a function of the proportion of loans in the pools that are foreclosed and liquidated and the loss severities associated with those liquidations. If the deductibles in the Company 's insured transactions and underlying referenced CMBS transactions are fully eroded, additional property level losses upon foreclosures and liquidations could result in substantial losses for MBIA. Ultimate loss rates remain uncertain because many loans are still delinquent and have not yet been resolved, others have been modified and others do not mature for another three to four years at which time they will face the need to refinance. The Company assigns a wide range of probabilities to these scenarios and incorporates views that liquidations will continue to be mitigated by loan extensions and modifications, and that property values and NOIs have bottomed for many sectors and markets in the U.S. The weightings are customized for each counterparty. If macroeconomic stress were to increase or the U.S. enters into a recession, higher delinquencies, liquidations and/or higher severities of loss upon liquidation may result and the Company may incur substantial additional losses. The foreclosure and REO pipelines are still relatively robust, with several restructurings and liquidations yet to occur, so the range of possible outcomes is wider than those for the Company 's exposures to ABS CDOs and second-lien RMBS. Prior to June 30, 2013, the Company incorporated an additional approach based on recent Roll Rates experienced within each of the commercial mortgage-backed index series. This actuarial approach was eliminated as a result of more emphasis being placed on loan-specific scenarios.

In the CRE CDO portfolio, transaction-specific structures require certain reporting and management protocols and often require the Company to incorporate these structural distinctions into its models. None of the CRE CDOs insured by the Company allow for reinvesting at this time, and many of the senior bonds have begun to amortize.

For the nine months ended September 30, 2013, the Company had a benefit of \$28 million of losses and LAE recorded in earnings related to CRE CDO financial guarantee insurance policies. For the nine months ended September 30, 2013, additional credit impairments and LAE for insured derivatives on structured CMBS pools, CRE CDOs and CRE loan pools were estimated to be \$487 million as a result of additional delinquencies and loan level liquidations, as well as continued refinements of MBIA 's assessment of various commutation possibilities. The cumulative credit impairments and LAE on structured CMBS pools, CRE CDOs and CRE loan pools were estimated to be \$4.1 billion through September 30, 2013. Though the pace of increases in the delinquency rate has slowed, many loans are being modified and liquidations continue to take place. Loan level losses have ranged from 1% to 2%, to near complete losses, and in a few cases severities exceeded 100%. These liquidations have led to bond level losses which have reduced the level of enhancement to the individual CMBS bonds referenced by the insured structured CMBS pools and in certain cases have resulted in deductible erosion. Bond level enhancement and pool level deductibles are structural features intended to mitigate losses to the Company, however, some of the transactions reference similar rated subordinate tranches of CMBS bonds. When there are broad-based declines in property performance, this leverage can result in rapid deterioration in pool performance. Beginning in the second quarter of 2013, the Company paid claims on a CMBS pool transaction that experienced deterioration such that all remaining deductible was eliminated.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 5: Loss and Loss Adjustment Expense Reserves (continued)*****Loss and LAE Activity*****Financial Guarantee Insurance Losses (Non-Derivative)**

The Company's financial guarantee insurance losses and LAE for the nine months ended September 30, 2013 are presented in the following table:

**Losses and LAE**

In millions	Nine Months Ended September 30, 2013			
	Second-lien RMBS	First-lien RMBS	Other <sup>(1)</sup>	Total
Losses and LAE related to actual and expected payments	\$ 85	\$ 12	\$ 108	\$ 205
Recoveries of actual and expected payments	(177)	(11)	76	(112)
Gross losses incurred	(92)	1	184	93
Reinsurance	-	-	(1)	(1)
Losses and LAE	\$ (92)	\$ 1	\$ 183	\$ 92

(1) - Includes ABS CDOs, CMBS, U.S. public finance and other issues.

The losses and LAE related to actual and expected payments included in the preceding table primarily related to \$108 million in other exposures, including \$86 million of losses related to U.S. public finance transactions primarily related to certain general obligation issues. The second-lien RMBS losses and LAE related to actual and expected payments comprise net increases of previously established reserves. The recoveries of actual and expected payments were primarily related to second-lien RMBS recoveries of \$177 million, including \$316 million in recoveries primarily resulting from ineligible mortgage loans included in insured exposures that are subject to contractual obligations by sellers/servicers to repurchase or replace such mortgages, partially offset by a \$139 million reduction in excess spread. Partially offsetting increases in second-lien RMBS recoveries of actual and expected payments were decreases of \$76 million related to other issues primarily resulting from a reversal of recoveries related to high yield corporate CDOs.

The following table provides information about the financial guarantees and related claim liability included in each of MBIA's surveillance categories as of September 30, 2013:

\$ in millions	Surveillance Categories				Total
	Caution List Low	Caution List Medium	Caution List High	Classified List	
Number of policies	89	20	6	192	307

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Number of issues <sup>(1)</sup>	31	15	5	135	186
Remaining weighted average contract period (in years)	10.8	5.3	9.6	9.6	9.8
Gross insured contractual payments outstanding: <sup>(2)</sup>					
Principal	\$ 5,686	\$ 1,099	\$ 65	\$ 8,332	\$ 15,182
Interest	3,998	279	32	4,819	9,128
Total	\$ 9,684	\$ 1,378	\$ 97	\$ 13,151	\$ 24,310
Gross claim liability	\$ -	\$ -	\$ -	\$ 1,504	\$ 1,504
Less:					
Gross potential recoveries	-	-	-	1,264	1,264
Discount, net	-	-	-	272	272
Net claim liability (recoverable)	\$ -	\$ -	\$ -	\$ (32)	\$ (32)
Unearned premium revenue	\$ 129	\$ 20	\$ 1	\$ 101	\$ 251

(1) - An issue represents the aggregate of financial guarantee policies that share the same revenue source for purposes of making debt service payments.

(2) - Represents contractual principal and interest payments due by the issuer of the obligations insured by MBIA.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 5: Loss and Loss Adjustment Expense Reserves (continued)**

The following table provides information about the financial guarantees and related claim liability included in each of MBIA's surveillance categories as of December 31, 2012:

\$ in millions	Surveillance Categories				Total
	Caution List Low	Caution List Medium	Caution List High	Classified List	
Number of policies	54	25	10	206	295
Number of issues <sup>(1)</sup>	29	15	10	136	190
Remaining weighted average contract period (in years)	8.1	4.0	7.6	9.5	8.7
Gross insured contractual payments outstanding: <sup>(2)</sup>					
Principal	\$ 4,250	\$ 1,176	\$ 373	\$ 9,458	\$ 15,257
Interest	2,721	256	120	5,264	8,361
<b>Total</b>	<b>\$ 6,971</b>	<b>\$ 1,432</b>	<b>\$ 493</b>	<b>\$ 14,722</b>	<b>\$ 23,618</b>
Gross claim liability	\$ -	\$ -	\$ -	\$ 1,589	\$ 1,589
Less:					
Gross potential recoveries	-	-	-	4,109	4,109
Discount, net	-	-	-	229	229
<b>Net claim liability (recoverable)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (2,749)</b>	<b>\$ (2,749)</b>
Unearned premium revenue	\$ 142	\$ 11	\$ 3	\$ 122	\$ 278

(1) - An "issue" represents the aggregate of financial guarantee policies that share the same revenue source for purposes of making debt service payments.

(2) - Represents contractual principal and interest payments due by the issuer of the obligations insured by MBIA.

The gross claim liability as of September 30, 2013 and December 31, 2012 in the preceding tables represents the Company's estimate of undiscounted probability-weighted future claim payments, which principally relate to insured first and second-lien RMBS transactions and U.S. public finance transactions. The gross potential recoveries represent the Company's estimate of undiscounted probability-weighted recoveries of actual claim payments and recoveries of estimated future claim payments, and principally relate to insured second-lien RMBS transactions and U.S. public finance transactions. The Company's recoveries have been, and remain based on either salvage rights, the rights conferred to MBIA through the transactional documents (inclusive of the insurance agreement), or subrogation rights embedded within financial guarantee insurance policies. Expected salvage and subrogation recoveries, as well as recoveries from other remediation efforts, reduce the Company's claim liability. Once a claim payment has been made, the claim liability has been satisfied and MBIA's right to recovery is no longer considered an offset to future expected claim payments, it is recorded as a salvage asset. The amount of recoveries recorded by the Company is limited to paid claims plus the present value of projected future claim payments. As claim payments are made, the recorded amount of potential recoveries may exceed the remaining amount of the claim liability for a given policy. The gross claim liability and gross potential recoveries reflect the elimination of claim liabilities and potential recoveries related to VIEs consolidated by the Company.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 5: Loss and Loss Adjustment Expense Reserves (continued)**

The following table presents the components of the Company's loss and LAE reserves and insurance loss recoverable as reported on the Company's consolidated balance sheets as of September 30, 2013 and December 31, 2012 for insured obligations within MBIA's Classified List. The loss reserves (claim liability) and insurance claim loss recoverable included in the following table represent the present value of the probability-weighted future claim payments and recoveries reported in the preceding tables.

<b>In millions</b>	<b>As of September 30, 2013</b>	<b>As of December 31, 2012</b>
Loss reserves (claim liability)	\$ 635	\$ 790
LAE reserves	53	63
<b>Loss and LAE reserves</b>	<b>\$ 688</b>	<b>\$ 853</b>
Insurance claim loss recoverable	\$ (737)	\$ (3,610)
LAE insurance loss recoverable	(5)	(38)
<b>Insurance loss recoverable</b>	<b>\$ (742)</b>	<b>\$ (3,648)</b>
Reinsurance recoverable on unpaid losses	\$ 7	\$ 14
Reinsurance recoverable on paid losses	-	1
<b>Reinsurance recoverable on paid and unpaid losses</b>	<b>\$ 7</b>	<b>\$ 15</b>

As of September 30, 2013, loss and LAE reserves include \$1.0 billion of reserves for expected future payments offset by expected recoveries of such future payments of \$326 million. As of December 31, 2012, loss and LAE reserves included \$1.2 billion of reserves for expected future payments offset by expected recoveries of such future payments of \$332 million. As of September 30, 2013, the insurance loss recoverable principally related to expected future recoveries on second-lien RMBS transactions resulting from expected excess spread generated by performing loans in such transactions. As of December 31, 2012, the insurance loss recoverable principally related to estimated recoveries of payments made by the Company resulting from ineligible mortgage loans in certain insured second-lien residential mortgage loan securitizations that are subject to a contractual obligation by the sellers/servicers to repurchase or replace the ineligible mortgage loans and expected future recoveries on second-lien RMBS transactions resulting from expected excess spread generated by performing loans in such transactions.

To date, as a result of the Bank of America and Flagstar Bank settlements, as well as the agreement between Consenting Claimants, ResCap and Ally, in the ResCap bankruptcy proceeding discussed above, the Company expects to be reimbursed for the majority of its potential recoveries related to ineligible mortgage loans by the end of 2013 or early 2014, which are primarily included in "Loan repurchase commitments" presented under the heading "Assets of consolidated variable interest entities" on the Company's consolidated balance sheets.

For the nine months ended September 30, 2013, the Company collected approximately \$2.9 billion, net of reinsurance, of which \$2.8 billion, net of reinsurance, related to insured second-lien RMBS transactions. The Company made payments of \$372 million, of which \$166 million related to insured second-lien RMBS transactions and \$134 million related to U.S. public finance issues.

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For the nine months ended September 30, 2013, the decrease in insurance loss recoverable related to paid losses totaled \$2.9 billion, and primarily resulted from the collections of previously established recoveries related to the settlement with Bank of America on the ineligible mortgage loans related to insured second-lien RMBS transactions.

The following table presents the amounts of the Company's second-lien RMBS exposure, gross undiscounted claim liability and potential recoveries related to non-consolidated VIEs and consolidated VIEs, included in the Company's Classified List, as of September 30, 2013.

### Second-lien RMBS Exposure

\$ in billions	Issues	Outstanding		Gross Undiscounted	
		Gross Principal	Gross Interest	Claim Liability	Potential Recoveries
Non-consolidated VIEs	23	\$ 3.6	\$ 1.3	\$ 0.2	\$ 0.9
Consolidated VIEs	11	\$ 1.8	\$ 0.7	\$ 0.1	\$ 1.4

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 5: Loss and Loss Adjustment Expense Reserves (continued)**

The following table presents changes in the Company's loss and LAE reserves for the nine months ended September 30, 2013. Changes in the loss and LAE reserves attributable to the accretion of the claim liability discount, changes in discount rates, changes in the timing and amounts of estimated payments and recoveries, changes in assumptions and changes in LAE reserves are recorded in Losses and loss adjustment expenses in the Company's consolidated statements of operations. As of September 30, 2013, the weighted average risk-free rate used to discount the Company's loss reserves (claim liability) was 2.11%. LAE reserves are expected to be settled within a one-year period and are not discounted.

Changes in Loss and LAE Reserves for the Nine Months Ended September 30, 2013								
In millions	Loss Payments for Cases with Reserves	Accretion of Claim Liability Discount	Changes in Discount Rates	Changes in Assumptions	Changes in Unearned Premium Revenue	Changes in LAE Reserves	Other <sup>(1)</sup>	Gross Loss and LAE Reserves as of September 30, 2013
Gross Loss and LAE Reserves as of December 31, 2012								
\$ 853	\$ (293)	\$ 10	\$ (71)	\$ 116	\$ 2	\$ (10)	\$ 81	\$ 688

(1) - Primarily changes in amount and timing of payments.

The decrease in the Company's gross loss and LAE reserves reflected in the preceding table was primarily due to a decrease in reserves related to loss payments on insured first and second-lien RMBS securitizations and U.S. public finance issues, partially offset by changes in assumptions.

Current period changes in the Company's estimate of potential recoveries may be recorded as an insurance loss recoverable asset, netted against the gross loss and LAE reserve liability, or both. The following table presents changes in the Company's insurance loss recoverable and changes in recoveries on unpaid losses reported within the Company's claim liability for the nine months ended September 30, 2013. Changes in insurance loss recoverable attributable to the accretion of the discount on the recoverable, changes in discount rates, changes in the timing and amounts of estimated collections, changes in assumptions and changes in LAE recoveries are recorded in Losses and loss adjustment expenses in the Company's consolidated statements of operations.

Changes in Insurance Loss Recoverable and Recoveries on Unpaid Losses for the Nine Months Ended September 30, 2013								
In millions	Gross Reserve as of December 31, 2012	Collections for Cases with Recoveries	Accretion of Recoveries	Changes in Discount Rates	Changes in Assumptions	Changes in LAE Recoveries	Other <sup>(1)</sup>	Gross Reserve as of September 30, 2013
Insurance loss recoverable	\$ 3,648	\$ (2,981)	\$ 16	\$ (25)	\$ 129	\$ (33)	\$ (12)	\$ 742
Recoveries on unpaid losses	332	-	4	(27)	15	2	-	326

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Total	\$	3,980	\$	(2,981)	\$	20	\$	(52)	\$	144	\$	(31)	\$	(12)	\$	1,068
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(1) Primarily changes in amount and timing of collections.

The Company's insurance loss recoverable decreased during 2013 primarily due to recoveries associated with issues outstanding as of December 31, 2012, which related to the settlement with Bank of America on the ineligible mortgage loans included in insured second-lien residential mortgage securitization exposures that are subject to contractual obligations by sellers/servicers to repurchase or replace such mortgages. Recoveries on unpaid losses decreased primarily due to changes in discount rates, partially offset by changes in assumptions.

The following table presents the Company's total estimated recoveries from ineligible mortgage loans included in certain insured second-lien mortgage loan securitizations as of September 30, 2013. The total estimated recoveries from ineligible mortgage loans of \$1.1 billion include \$18 million recorded as Insurance loss recoverable and \$1.1 billion recorded as Loan repurchase commitments presented under the heading Assets of consolidated variable interest entities on the Company's consolidated balance sheets.

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### MBIA Inc. and Subsidiaries

### Notes to Consolidated Financial Statements (Unaudited)

#### Note 5: Loss and Loss Adjustment Expense Reserves (continued)

In millions						
Total Estimated Recoveries from Ineligible Mortgage Loans as of December 31,						Total Estimated Recoveries from Ineligible Mortgage Loans as of September 30, 2013
2012	Accretion of Future Collections	Changes in Discount Rates	Recoveries (Collections)	Changes in Assumptions	Other <sup>(1)</sup>	
\$ 3,583	\$ 20	\$ (7)	\$ (2,897)	\$ 433	\$ 1	\$ 1,133

(1) Primarily changes in amount and timing of collections.

The decrease in the Company's total estimated recoveries from ineligible mortgage loans in the preceding table primarily resulted from the collections of previously established recoveries related to the settlement with Bank of America and Flagstar Bank on the ineligible mortgage loans related to insured second-lien RMBS securitizations.

Remediation actions may involve, among other things, waivers or renegotiations of financial covenants or triggers, waivers of contractual provisions, the granting of consents, transfer of servicing, consideration of restructuring plans, acceleration, security or collateral enforcement, actions in bankruptcy or receivership, litigation and similar actions. The types of remedial actions pursued are based on the insured obligation's risk type and the nature and scope of the event giving rise to the remediation. As part of any such remedial actions, MBIA seeks to improve its security position and to obtain concessions from the issuer of the insured obligation. From time to time, the issuer of an MBIA-insured obligation may, with the consent of MBIA, restructure the insured obligation by extending the term, increasing or decreasing the par amount or decreasing the related interest rate, with MBIA insuring the restructured obligation.

Costs associated with remediating insured obligations assigned to the Company's Caution List Low, Caution List Medium, Caution List High and Classified List are recorded as LAE. LAE is primarily recorded as part of the Company's provision for its loss reserves and included in Losses and loss adjustment expenses on the Company's consolidated statements of operations. The following table presents the gross expenses related to remedial actions for insured obligations:

In millions	Nine Months Ended September 30,	
	2013	2012
Loss adjustment expense incurred, gross	\$ 31	\$ 113

#### Note 6: Fair Value of Financial Instruments

##### Fair Value Measurement

Fair value is a market-based measure considered from the perspective of a market participant. Therefore, even when market assumptions are not readily available, the Company's own assumptions are set to reflect those which it believes market participants would use in pricing an asset or liability at the measurement date. The fair value measurements of financial instruments held or issued by the Company are determined through the use of observable market data when available. Market data is obtained from a variety of third-party sources, including dealer quotes. If dealer quotes are not available for an instrument that is infrequently traded, the Company uses alternate valuation methods, including either dealer

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quotes for similar instruments or modeling using market data inputs. The use of alternate valuation methods generally requires considerable judgment in the application of estimates and assumptions and changes to such estimates and assumptions may produce materially different fair values.

The accounting guidance for fair value measurement establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available and reliable. Observable inputs are those the Company believes that market participants would use in pricing an asset or liability based on available market data. Unobservable inputs are those that reflect the Company's beliefs about the assumptions market participants would use in pricing an asset or liability based on the best information available. The fair value hierarchy is broken down into three levels based on the observability and reliability of inputs, as follows:

Level 1 Valuations based on quoted prices in active markets for identical assets or liabilities that the Company can access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail any degree of judgment.



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### **MBIA Inc. and Subsidiaries**

#### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 6: Fair Value of Financial Instruments (continued)**

Level 2 Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly. Level 2 assets include debt securities with quoted prices that are traded less frequently than exchange-traded instruments, securities which are priced using observable inputs and derivative contracts whose values are determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

Level 3 Valuations based on inputs that are unobservable and supported by little or no market activity and that are significant to the overall fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques where significant inputs are unobservable, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The availability of observable inputs can vary from product to product and period to period and is affected by a wide variety of factors, including, for example, the type of product, whether the product is new and not yet established in the marketplace, and other characteristics particular to the product. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the Company assigns the level in the fair value hierarchy for which the fair value measurement in its entirety falls, based on the least observable input that is significant to the fair value measurement.

#### *Financial Assets (excluding derivative assets)*

Financial assets, excluding derivative assets, held by the Company primarily consist of investments in debt securities. Substantially all of the Company's investments are priced by independent third parties, including pricing services and brokers. Typically the Company receives one pricing service value or broker quote for each instrument, which represents a non-binding indication of value. The Company reviews the assumptions, inputs and methodologies used by pricing services and brokers to obtain reasonable assurance that the prices used in its valuations reflect fair value. When the Company believes a third-party quotation differs significantly from its internally developed expectation of fair value, whether higher or lower, the Company reviews its data or assumptions with the provider. This review includes comparing significant assumptions such as prepayment speeds, default ratios, forward yield curves, credit spreads and other significant quantitative inputs to internal assumptions, and working with the price provider to reconcile the differences. The price provider may subsequently provide an updated price. In the event that the price provider does not update its price, and the Company still does not agree with the price provided, the Company will try to obtain a price from another third-party provider, such as a broker, or use an internally developed price which it believes represents the fair value of the investment. The fair values of investments for which internal prices were used were not significant to the aggregate fair value of the Company's investment portfolio as of September 30, 2013 or December 31, 2012. All challenges to third-party prices are reviewed by staff of the Company with relevant expertise to ensure reasonableness of assumptions.

In addition to challenging pricing assumptions, the Company obtains reports from the independent accountants for significant third-party pricing services attesting to the effectiveness of the controls over data provided to the Company. These reports are obtained annually and are reviewed by the Company to ensure key controls are applied by the pricing services, and that appropriate user controls are in place at the third-party pricing services organization to ensure proper measurement of the fair values of its investments. In the event that any controls in these reports are deemed as ineffective by independent accountants, the Company will take the necessary actions to ensure that internal user controls are in place to mitigate the control risks. No deficiencies were noted for significant third-party pricing services used.

#### *Financial Liabilities (excluding derivative liabilities)*

Financial liabilities, excluding derivative liabilities, issued by the Company primarily consist of investment agreements and medium-term notes (MTNs) within its wind-down operations, debt issued for general corporate purposes and debt in VIEs. Investment agreements, MTNs, and corporate debt are typically recorded at face value adjusted for premiums or discounts. Financial liabilities that the Company has elected to fair value or that require fair value reporting or disclosures are valued based on the estimated value of the underlying collateral, the Company's or a third-party's estimate of discounted cash flow model estimates, or quoted market values for similar products. These valuations include

adjustments for expected nonperformance risk of the Company.

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**MBIA Inc. and Subsidiaries**

**Notes to Consolidated Financial Statements (Unaudited)**

**Note 6: Fair Value of Financial Instruments (continued)**

*Derivative Liabilities*

The Company's derivative liabilities are primarily insured credit derivatives that reference structured pools of cash securities and CDSs. The Company generally insured the most senior liabilities of such transactions, and at the inception of transactions its exposure generally had more subordination than needed to achieve triple-A ratings from credit rating agencies. The types of collateral underlying its insured derivatives consist of cash securities and CDSs referencing primarily corporate, asset-backed, residential mortgage-backed, commercial mortgage-backed, CRE loans, and CDO securities.

The Company's insured credit derivative contracts are non-traded structured credit derivative transactions. Since insured derivatives are highly customized and there is generally no observable market for these derivatives, the Company estimates their fair values in a hypothetical market based on internal and third-party models simulating what a similar company would charge to assume the Company's position in the transaction at the measurement date. This pricing would be based on the expected loss of the exposure. The Company reviews its valuation model results on a quarterly basis to assess the appropriateness of the assumptions and results in light of current market activity and conditions. This review is performed by internal staff with relevant expertise. If live market spreads or securities prices are observable for similar transactions, those spreads are an integral part of the analysis. New insured transactions that resemble existing (previously insured) transactions, if any, would be considered, as well as negotiated settlements of existing transactions.

The Company may from time to time make changes in its valuation techniques if the change results in a measurement that it believes is equally or more representative of fair value under current circumstances.

*Internal Review Process*

All significant financial assets and liabilities, including derivative assets and liabilities, are reviewed by committees created by the Company to ensure compliance with the Company's policies and risk procedures in the development of fair values of financial assets and liabilities. These valuation committees review, among other things, key assumptions used for internally developed prices, significant changes in sources and uses of inputs, including changes in model approaches, and any adjustments from third-party inputs or prices to internally developed inputs or prices. The committees also review any significant impairment or improvements in fair values of the financial instruments from prior periods. From time to time, these committees will reach out to the Company's valuation experts to better understand key methods and assumptions used for the determination of fair value, including understanding significant changes in fair values. These committees are comprised of senior finance team members with the relevant experience in the financial instruments their committee is responsible for. For each quarter, these committees document their agreement with the fair values developed by management of the Company as reported in the quarterly and annual financial statements.

***Valuation Techniques***

Valuation techniques for financial instruments measured at fair value or disclosed at fair value are described below.

***Fixed-Maturity Securities (including short-term investments) Held as Available-For-Sale, Fixed-Maturity Securities at Fair Value, Investments Pledged as Collateral, Investments Held-to-Maturity, and Other Investments***

Fixed-maturity securities (including short-term investments) held as AFS, fixed-maturity securities at fair value, investments pledged as collateral, and other investments include investments in U.S. Treasury and government agencies, foreign governments, corporate obligations, mortgage-backed securities ( MBS ) and ABS (including CMBS and CDOs), state and municipal bonds and perpetual debt and equity securities (including money market mutual funds).

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These investments are generally valued based on recently executed transaction prices or quoted market prices. When quoted market prices are not available, fair value is generally determined using quoted prices of similar investments or a valuation model based on observable and unobservable inputs. Inputs vary depending on the type of investment. Observable inputs include contractual cash flows, interest rate yield curves, CDS spreads, prepayment and volatility scores, diversity scores, cross-currency basis index spreads, and credit spreads for structures similar to the financial instrument in terms of issuer, maturity and seniority. Unobservable inputs include cash flow projections and the value of any credit enhancement.

The fair value of the held-to-maturity ( HTM ) investments is determined using discounted cash flow models. Key inputs include unobservable cash flows projected over the expected term of the investment discounted using observable interest rate yield curves of similar securities.

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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 6: Fair Value of Financial Instruments (continued)**

Investments based on quoted market prices of identical investments in active markets are classified as Level 1 of the fair value hierarchy. Level 1 investments generally consist of U.S. Treasury and foreign government and agency investments. Quoted market prices of investments in less active markets, as well as investments which are valued based on other than quoted prices for which the inputs are observable, such as interest rate yield curves, are categorized in Level 2 of the fair value hierarchy. Investments that contain significant inputs that are not observable are categorized as Level 3.

#### *Cash and Cash Equivalents, Receivable for Investments Sold, Net Cash Collateral Pledged to Swap Counterparties, Payable for Investments Purchased, Secured Loan and Accrued Investment Income*

The carrying amounts of cash and cash equivalents, receivable for investments sold, net cash collateral pledged to swap counterparties, payable for investments purchased, secured loan and accrued investment income approximate fair values due to the short-term nature and credit worthiness of these instruments.

#### *Loans Receivable at Fair Value*

Loans receivable at fair value are comprised of loans held by consolidated VIEs consisting of residential mortgage loans, commercial mortgage loans and other whole business loans. Fair values of residential mortgage loans are determined using quoted prices for MBS issued by the respective VIE and adjustments for the fair values of the financial guarantees provided by MBIA Corp. on the related MBS. Fair values of commercial mortgage loans and other whole business loans are valued based on quoted prices of similar collateralized MBS. Loans receivable at fair value are categorized in Level 3 of the fair value hierarchy.

#### *Loan Repurchase Commitments*

Loan repurchase commitments are obligations owed by the sellers/servicers of mortgage loans to either MBIA as reimbursement of paid claims or to the RMBS trusts as defined in the transaction documents. Loan repurchase commitments are assets of the consolidated VIEs. This asset represents the rights of MBIA against the sellers/servicers for breaches of representations and warranties that the securitized residential mortgage loans sold to the trust to comply with stated underwriting guidelines and for the sellers/servicers to cure, replace, or repurchase mortgage loans. Fair value measurements of loan repurchase commitments represent the amounts owed by the sellers/servicers to MBIA as reimbursement of paid claims. Loan repurchase commitments are not securities and no quoted prices or comparable market transaction information are observable or available. Loan repurchase commitments at fair value are categorized in Level 3 of the fair value hierarchy. Fair values of loan repurchase commitments are determined using discounted cash flow techniques based on inputs including:

breach rates representing the rate at which the sellers/servicers failed to comply with stated representations and warranties;

recovery rates representing the estimates of future cash flows for the asset, including estimates about possible variations in the amount of cash flows expected to be collected;

expectations about possible variations in the timing of collections of the cash flows; and

time value of money, represented by the rate on risk-free monetary assets.

*Investment Agreements*

The fair values of investment agreements are determined using discounted cash flow techniques based on contractual cash flows and observable interest rates currently being offered for similar agreements with comparable maturity dates. Investment agreements contain collateralization and termination agreements that substantially mitigate the nonperformance risk of the Company. As the terms of the notes are private, and the contract cash flows are not observable, these investment agreements are categorized as Level 3 of the fair value hierarchy.

*Medium-Term Notes*

The fair values of certain MTNs are based on quoted market prices provided by third-party sources, where available. When quoted market prices are not available, the Company applies a matrix pricing grid based on the quoted market prices received and the MTNs' stated maturity and interest rate to determine fair value. Nonperformance risk is included in the quoted market prices and the matrix pricing grid.

The Company has elected to record these MTNs at fair value as they contain embedded derivatives which cannot accurately be separated from the host debt instrument and fair valued separately, therefore, these MTNs are carried at fair value with changes in fair value reflected in earnings. The remaining MTNs, which are not carried at fair value, do not contain embedded derivatives.

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### **MBIA Inc. and Subsidiaries**

#### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 6: Fair Value of Financial Instruments (continued)**

As these MTNs are illiquid and the prices reflect significant unobservable inputs, they are categorized as Level 3 of the fair value hierarchy.

#### *Variable Interest Entity Notes*

The fair values of VIE notes are determined based on recently executed transaction prices or quoted prices where observable. When position-specific quoted prices are not observable, fair values are based on quoted prices of similar securities. Fair values based on quoted prices of similar securities may be adjusted for factors unique to the securities, including any credit enhancement. When observable quoted prices are not available, fair value is determined based on discounted cash flow techniques of the underlying collateral using observable and unobservable inputs. Observable inputs include interest rate yield curves and bond spreads of similar securities. Unobservable inputs include the value of any credit enhancement. VIE notes are categorized in Level 2 or Level 3 of the fair value hierarchy based on the lowest level input that is significant to the fair value measurement in its entirety.

#### *Long-term Debt*

Long-term debt consists of notes, debentures, surplus notes and accrued interest on this debt. The fair value of long-term notes, debentures and surplus notes are estimated based on quoted prices for the identical or similar securities. The fair value of the accrued interest expense on the surplus notes due 2033 is determined based on the scheduled interest payments discounted by the market's perception of the credit risk related to the repayment of the surplus notes. The credit risk related to the repayment of the surplus notes is based on recent trades of the surplus notes. The deferred interest payment will be due on the first business day on or after which the Company obtains approval to make such payment.

The carrying amounts of accrued interest expense on all other long-term debt approximate fair value due to the short-term nature of these instruments.

#### *Derivatives Asset/Liability Products*

The asset/liability products business has entered into derivative transactions primarily consisting of interest rate swaps, cross currency swaps, and CDS contracts. Fair values of over-the-counter derivatives are determined using valuation models based on observable inputs, nonperformance risk of the Company's own credit and nonperformance risk of the counterparties. Observable and market-based inputs include interest rate yields, credit spreads and volatilities. These derivatives are categorized in Level 2 or Level 3 of the fair value hierarchy based on the input that is significant to the fair value measurement in its entirety.

The Company has policies and procedures in place regarding counterparties, including review and approval of the counterparty and the Company's exposure limit, collateral posting requirements, collateral monitoring and margin calls on collateral. The Company manages counterparty credit risk on an individual counterparty basis through master netting arrangements covering derivative transactions in the asset/liability products and corporate segments. These agreements allow the Company to contractually net amounts due from a counterparty with those amounts due to such counterparty when certain triggering events occur. The Company only executes swaps under master netting agreements, which typically contain mutual credit downgrade provisions that generally provide the ability to require assignment or termination in the event either the Company or the counterparty is downgraded below a specified credit rating. The netting agreements minimize the potential for losses related to credit exposure and thus serve to mitigate the Company's nonperformance risk under these derivatives.

In certain cases, the Company also manages credit risk through collateral agreements that give the Company the right to hold or the obligation to provide collateral when the current market value of derivative contracts exceeds an exposure threshold. Under these arrangements, the Company may provide U.S. Treasury and other highly rated securities or cash to secure the derivative. The delivery of high-quality collateral can minimize credit exposure and mitigate the potential for nonperformance risk impacting the fair values of the derivatives.

*Derivatives Insurance*

The derivative contracts insured by the Company cannot be legally traded and generally do not have observable market prices. The Company determines the fair values of insured credit derivatives using valuation models. The fair valuation models are consistently applied from period to period, with refinements to the fair value estimation approach being applied as and when the information becomes available. Negotiated settlements are also considered when determining fair value to provide the best estimate of how another market participant would evaluate fair value.



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**MBIA Inc. and Subsidiaries**

**Notes to Consolidated Financial Statements (Unaudited)**

**Note 6: Fair Value of Financial Instruments (continued)**

Approximately 98% of the balance sheet fair value of insured credit derivatives as of September 30, 2013 was valued based on the Binomial Expansion Technique ( BET ) Model. Approximately 2% of the balance sheet fair value of insured credit derivatives as of September 30, 2013 was valued based on the internally developed Direct Price Model and the dual-default model. The valuation of insured derivatives includes the impact of its credit standing. All of these derivatives are categorized as Level 3 of the fair value hierarchy as their fair value is derived using significant unobservable inputs.

**Description of the BET Model**

**1. Valuation Model Overview**

The BET Model estimates what a bond insurer would charge to guarantee a transaction at the measurement date, based on the market-implied default risk of the underlying collateral and the remaining structural protection in a deductible or subordination.

Inputs to the process of determining fair value for structured transactions using the BET Model include estimates of collateral loss, allocation of loss to separate tranches of the capital structure, and calculation of the change in value.

Estimates of aggregated collateral losses are calculated by reference to the following (described in further detail under BET Model Inputs below):

credit spreads of underlying collateral based on actual spreads or spreads on similar collateral with similar ratings, or in some cases, are benchmarked; for collateral pools where the spread distribution is characterized by extremes, each segment of the pool is modeled separately instead of using an overall pool average;

diversity score of the collateral pool as an indication of correlation of collateral defaults; and

recovery rate for all defaulted collateral.

Allocation of losses to separate tranches of the capital structure according to priority of payments in a transaction.

The inception-to-date unrealized gain or loss on a transaction is the difference between the original price of the risk (the original market-implied expected loss) and the current price of the risk based on the assumed market-implied expected losses derived from the model.

Additional structural assumptions of the BET Model are:

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Default probabilities are determined by three factors: MBIA Corp.'s credit spread, MBIA Corp.'s recovery rate after default, and the time period under risk;

Frequencies of defaults are modeled evenly over time;

Collateral assets are generally considered on an average basis rather than being modeled on an individual basis; and

Collateral asset correlation is modeled using a diversity score which is calculated based on industry or sector concentrations.

Recovery rates are based on historical averages and updated based on market evidence.

### 2. BET Model Inputs

#### a. Credit spreads

The average spread of collateral is a key input as the Company assumes credit spreads reflect the market's assessment of default probability for each piece of collateral. Spreads are obtained from market data sources published by third parties (e.g., dealer spread tables for assets most closely resembling collateral within the Company's transactions) as well as collateral-specific spreads on the underlying reference obligations provided by trustees or market sources. Also, when these sources are not available, the Company benchmarks spreads for collateral against market spreads or prices. This data is reviewed on an ongoing basis for reasonableness and applicability to the Company's derivative portfolio. The Company also calculates spreads based on quoted prices and on internal assumptions about expected life, when pricing information is available and spread information is not.

The Company uses the spread hierarchy listed below in determining which source of spread information to use, with the rule being to use CDS spreads where available and cash security spreads as the next alternative.

Spread Hierarchy:

Collateral-specific credit spreads when observable;

Sector-specific spread tables by asset class and rating;

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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 6: Fair Value of Financial Instruments (continued)**

Corporate spreads, including Bloomberg spread tables based on rating; and

Benchmark from most relevant market source when corporate spreads are not directly relevant.

There were some transactions where the Company incorporated multiple levels within the hierarchy, including using actual collateral-specific credit spreads in combination with a calculated spread based on an assumed relationship. In those cases, MBIA classified the transaction as being benchmarked from the most relevant spread source even though the majority of the average spread was from actual collateral-specific spreads. As of September 30, 2013, sector-specific spreads were used in 8% of the transactions valued using the BET Model. Corporate spreads were used in 50% of the transactions and spreads benchmarked from the most relevant spread source were used for 42% of the transactions. The spread source can also be identified by whether or not it is based on collateral weighted average rating factor ( WARF ). No collateral-specific spreads are based on WARF. Sector-specific spreads, corporate spreads and some benchmarked spreads are based on WARF. WARF-sourced and/or ratings-sourced credit spreads were used for 76% of the transactions.

Over time, the data inputs change as new sources become available, existing sources are discontinued or are no longer considered to be reliable or the most appropriate. It is always the Company's objective to use more observable spread hierarchies defined above. However, the Company may on occasion move to less observable spread inputs due to the discontinuation of data sources or due to the Company considering certain spread inputs no longer representative of market spreads.

#### **b. Diversity Scores**

Diversity scores are a means of estimating the diversification in a portfolio. The diversity score estimates the number of uncorrelated assets that are assumed to have the same loss distribution as the actual portfolio of correlated assets. While diversity score is a required input into the BET model, due to current high levels of default within the collateral of the structures, diversity score does not have a significant impact on valuation.

#### **c. Recovery Rate**

The recovery rate represents the percentage of par expected to be recovered after an asset defaults, indicating the severity of a potential loss. MBIA generally uses rating agency recovery assumptions which may be adjusted to account for differences between the characteristics and performance of the collateral used by the rating agencies and the actual collateral in MBIA-insured transactions. The Company may also adjust rating agency assumptions based on the performance of the collateral manager and on empirical market data.

#### **d. Nonperformance Risk**

The Company's valuation methodology for insured credit derivative liabilities incorporates MBIA Corp.'s own nonperformance risk. The Company calculates the fair value by discounting the market value loss estimated through the BET Model at discount rates which include MBIA Corp.'s CDS spreads as of September 30, 2013. The CDS spreads assigned to each deal are based on the weighted average life of the deal. The Company limits the nonperformance impact so that the derivative liability could not be lower than MBIA Corp.'s recovery derivative price multiplied by the unadjusted derivative liability.

#### **Overall Model Results**

As of September 30, 2013 and December 31, 2012, the Company's net insured derivative liability was \$1.4 billion and \$2.9 billion, respectively, and was primarily related to the fair values of insured credit derivatives, based on the results of the aforementioned pricing models. In the current environment, the most significant driver of changes in fair value is MBIA Corp.'s nonperformance risk. In aggregate, the nonperformance calculation resulted in a pre-tax net insured derivative liability that was \$548 million and \$4.4 billion lower than the net liability that would have

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been estimated if MBIA Corp. excluded nonperformance risk in its valuation as of September 30, 2013 and December 31, 2012, respectively. Nonperformance risk is a fair value concept and does not contradict MBIA Corp. s internal view, based on fundamental credit analysis of MBIA Corp. s economic condition, that MBIA Corp. will be able to pay all claims when due.

### *Warrants*

Stock warrants issued by the Company are recorded at fair value based on a modified Black-Scholes model. Inputs into the warrant valuation include interest rates, stock volatilities and dividend data. As all significant inputs are market-based and observable, warrants are categorized in Level 2 of the fair value hierarchy.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)***Financial Guarantees*

**Gross Financial Guarantees** The fair value of gross financial guarantees is determined using discounted cash flow techniques based on inputs that include (i) assumptions of expected losses on financial guarantee policies where loss reserves have not been recognized, (ii) amount of losses expected on financial guarantee policies where loss reserves have been established, net of expected recoveries, (iii) the cost of capital reserves required to support the financial guarantee liability, (iv) operating expenses, and (v) discount rates. The MBIA Corp. CDS spread and recovery rate are used as the discount rate for MBIA Corp., while the CDS spread and recovery rate of a similar municipal bond insurance company are used as the discount rate for National, as National does not have a published CDS spread and recovery rate.

The carrying value of the Company's gross financial guarantees consists of unearned premium revenue and loss and LAE reserves, net of the insurance loss recoverable as reported on MBIA's consolidated balance sheets.

**Ceded Financial Guarantees** The fair value of ceded financial guarantees is determined by applying the percentage ceded to reinsurers to the related fair value of the gross financial guarantees. The carrying value of ceded financial guarantees consists of prepaid reinsurance premiums and reinsurance recoverable on paid and unpaid losses as reported within Other assets on the Company's consolidated balance sheets.

*Significant Unobservable Inputs*

The following tables provide quantitative information regarding the significant unobservable inputs used by the Company for assets and liabilities measured at fair value on a recurring basis as of September 30, 2013 and December 31, 2012. These tables exclude inputs used to measure fair value that are not developed by the Company, such as broker prices and other third-party pricing service valuations.

In millions	Fair Value as of September 30, 2013	Valuation Techniques	Unobservable Input	Range (Weighted Average)
<b>Assets of consolidated VIEs:</b>				
Loans receivable at fair value	\$ 1,704	Quoted market prices adjusted for financial guarantees provided to VIE obligations	Impact of financial guarantee	0% - 17% (4%)
Loan repurchase commitments	1,116	Discounted cash flow	Recovery rates	0% - 98% (81%)
<b>Liabilities of consolidated VIEs:</b>				
Variable interest entity notes	745	Quoted market prices of VIE assets adjusted for financial guarantees provided	Impact of financial guarantee	0% - 27% (10%)
<b>Credit derivative liabilities, net:</b>				
CMBS	956	BET Model	Recovery rates	25% - 90% (60%)
			Nonperformance risk	12% - 57% (28%)
			Weighted average life (in years)	1.4 - 28.3 (3.5)
			CMBS spreads	1% - 27% (13%)
Multi-sector CDO	16	Direct Price Model	Nonperformance risk	57% - 57% (57%)
Other	391	BET Model	Recovery rates	42% - 70% (46%)

Nonperformance risk	18% - 31% (27%)
Weighted average life (in years)	0.2 - 3.8 (2.2)

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

In millions	Fair Value as of December 31, 2012	Valuation Techniques	Unobservable Input	Range (Weighted Average)
<b>Assets of consolidated VIEs:</b>				
Loans receivable at fair value	\$ 1,881	Quoted market prices adjusted for financial guarantees provided to VIE obligations	Impact of financial guarantee	0% - 14% (3%)
Loan repurchase commitments	1,086	Discounted cash flow	Recovery rates Breach rates	10% - 75% (47%) 66% - 94% (78%)
<b>Liabilities of consolidated VIEs:</b>				
Variable interest entity notes	1,932	Quoted market prices of VIE assets adjusted for financial guarantees provided	Impact of financial guarantee	0% - 23% (6%)
<b>Credit derivative liabilities, net:</b>				
CMBS	1,590	BET Model	Recovery rates Nonperformance risk Weighted average life (in years) CMBS spreads	21% - 90% (51%) 19% - 59% (58%) 0.1 - 5.6 (4.4) 1% - 23% (13%)
Multi-sector CDO	525	Direct Price Model	Nonperformance risk	59% - 59% (59%)
Other	806	BET Model	Recovery rates Nonperformance risk Weighted average life (in years)	42% - 75% (47%) 42% - 59% (58%) 0.1 - 19.6 (3.0)

***Sensitivity of Significant Unobservable Inputs***

The significant unobservable input used in the fair value measurement of the Company's loans receivable at fair value of consolidated VIEs is the impact of the financial guarantee. The fair value of loans receivable is calculated by subtracting the value of the financial guarantee from the market value of VIE liabilities. The value of a financial guarantee is estimated by the Company as the present value of expected cash payments under the policy. As expected cash payments provided by the Company under the insurance policy increase, there is a lower expected cash flow on the underlying loans receivable of the VIE. This results in a lower fair value of the loans receivable in relation to the obligations of the VIE.

The significant unobservable inputs used in the fair value measurement of the Company's loan repurchase commitments of consolidated VIEs are the recovery rates. Recovery rates reflect the estimates of future cash flows reduced for litigation delays and risks and/or potential financial distress of the sellers/servicers. The estimated recoveries of the loan repurchase commitments may differ from the actual recoveries that may be received in the future. Significant increases or decreases in the recovery rates would result in significantly higher or lower fair values of the loan repurchase commitments, respectively. Additionally, changes in the legal environment and the ability of the counterparties to pay would impact the recovery rate assumptions, which could significantly impact the fair value measurement.

The significant unobservable input used in the fair value measurement of the Company's VIE notes of consolidated VIEs is the impact of the financial guarantee. The fair value of VIE notes is calculated by adding the value of the financial guarantee to the market value of VIE assets. The value of a financial guarantee is estimated by the Company as the present value of expected cash payments under the policy. As the value of the guarantee provided by the Company to the obligations issued by the VIE increases, the credit support adds value to the liabilities of the VIE. This results in an increase in the fair value of the liabilities of the VIE.

The significant unobservable inputs used in the fair value measurement of MBIA Corp.'s CMBS credit derivatives, which are valued using the BET Model, are CMBS spreads, recovery rates, nonperformance risk and weighted average life. The CMBS spread is an indicator of credit risk of the collateral securities. The recovery rate represents the percentage of notional expected to be recovered after an asset defaults, indicating the severity of a potential loss. The nonperformance risk is an assumption of MBIA Corp.'s own ability to pay and whether MBIA Corp. will have

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the necessary resources to pay the obligations as they come due. Weighted average life is based on the Company's estimate of when the principal of the underlying collateral of the CMBS structure will be repaid. A significant increase or decrease in CMBS spreads would result in an increase or decrease in the fair value of the derivative liability, respectively. A significant increase in weighted average life can result in an increase or decrease in the fair value of the derivative liability, depending on the discount rate and the timing of significant losses. Any significant increase or decrease in recovery rates, or MBIA Corp.'s nonperformance risk would result in a decrease or increase in the fair value of the derivative liabilities, respectively. CMBS spreads, recovery rates, nonperformance risk and weighted average lives are determined independently. Changes in one input will not necessarily have any impact on the other inputs.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

The significant unobservable input used in the fair value measurement of MBIA Corp.'s multi-sector CDO credit derivatives, which are valued using the Direct Price Model, is nonperformance risk. The nonperformance risk is an assumption of MBIA Corp.'s own ability to pay and whether MBIA Corp. will have the necessary resources to pay the obligations as they come due. Any significant increase or decrease in MBIA Corp.'s nonperformance risk would result in a decrease or increase in the fair value of the derivative liabilities, respectively.

The significant unobservable inputs used in the fair value measurement of MBIA Corp.'s other credit derivatives, which are valued using the BET Model, are recovery rates, nonperformance risk and weighted average life. The recovery rate represents the percentage of notional expected to be recovered after an asset defaults, indicating the severity of a potential loss. The nonperformance risk is an assumption of MBIA Corp.'s own ability to pay and whether MBIA Corp. will have the necessary resources to pay the obligations as they come due. Weighted average life is based on MBIA Corp.'s estimate of when the principal of the underlying collateral will be repaid. A significant increase in weighted average life can result in an increase or decrease in the fair value of the derivative liability, depending on the discount rate and the timing of significant losses. Any significant increase or decrease in recovery rates or MBIA Corp.'s nonperformance risk would result in a decrease or increase in the fair value of the derivative liabilities, respectively. Recovery rates, nonperformance risk and weighted average lives are determined independently. Changes in one input will not necessarily have any impact on the other inputs.

**Fair Value Measurements**

The following tables present the fair value of the Company's assets (including short-term investments) and liabilities measured and reported at fair value on a recurring basis as of September 30, 2013 and December 31, 2012:

In millions	Fair Value Measurements at Reporting Date Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance as of September 30, 2013
<b>Assets:</b>					
Fixed-maturity investments:					
U.S. Treasury and government agency	\$ 424	\$ 137	\$ -	\$ -	\$ 561
State and municipal bonds	-	1,551	62 <sup>(1)</sup>	-	1,613
Foreign governments	87	109	5 <sup>(1)</sup>	-	201
Corporate obligations	-	1,717	47 <sup>(1)</sup>	-	1,764
Mortgage-backed securities:					
Residential mortgage-backed agency	-	945	17 <sup>(1)</sup>	-	962
Residential mortgage-backed non-agency	-	79	-	-	79
Commercial mortgage-backed	-	26	14 <sup>(1)</sup>	-	40
Asset-backed securities:					
Collateralized debt obligations	-	70	88 <sup>(1)</sup>	-	158
Other asset-backed	-	89	57 <sup>(1)</sup>	-	146
Total fixed-maturity investments	511	4,723	290	-	5,524
Money market securities	910	3	-	-	913
Perpetual debt and equity securities	27	14	11 <sup>(1)</sup>	-	52

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Cash and cash equivalents	1,057	-	-	-	1,057
Derivative assets:					
Non-insured derivative assets:					
Interest rate derivatives	-	57	-	(53)	4
Total derivative assets	-	57	-	(53)	4

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

In millions	Fair Value Measurements at Reporting Date Using				Balance as of September 30, 2013
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	
Assets of consolidated VIEs:					
Corporate obligations	-	46	48 <sup>(1)</sup>	-	94
Mortgage-backed securities:					
Residential mortgage-backed non-agency	-	255	4 <sup>(1)</sup>	-	259
Commercial mortgage-backed	-	103	2 <sup>(1)</sup>	-	105
Asset-backed securities:					
Collateralized debt obligations	-	33	20 <sup>(1)</sup>	-	53
Other asset-backed	-	65	50 <sup>(1)</sup>	-	115
Money market securities	156	-	-	-	156
Cash	46	-	-	-	46
Loans receivable	-	-	1,704	-	1,704
Loan repurchase commitments	-	-	1,116	-	1,116
<b>Total assets</b>	<b>\$ 2,707</b>	<b>\$ 5,299</b>	<b>\$ 3,245</b>	<b>\$ (53)</b>	<b>\$ 11,198</b>
Liabilities:					
Medium-term notes	\$ -	\$ -	\$ 204 <sup>(1)</sup>	\$ -	\$ 204
Derivative liabilities:					
Insured derivatives:					
Credit derivatives	-	7	1,363	-	1,370
Non-insured derivatives:					
Interest rate derivatives	-	195	-	(195)	-
Currency derivatives	-	1	-	(1)	-
Other liabilities:					
Warrants	-	48	-	-	48
Liabilities of consolidated VIEs:					
Variable interest entity notes	-	1,681	745	-	2,426
Derivative liabilities:					
Currency derivatives	-	-	15 <sup>(1)</sup>	-	15
<b>Total liabilities</b>	<b>\$ -</b>	<b>\$ 1,932</b>	<b>\$ 2,327</b>	<b>\$ (196)</b>	<b>\$ 4,063</b>

(1) - Unobservable inputs are either not developed by the Company or do not significantly impact the overall fair values of the aggregate financial assets and liabilities.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

In millions	Fair Value Measurements at Reporting Date Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance as of December 31, 2012
<b>Assets:</b>					
Fixed-maturity investments:					
U.S. Treasury and government agency	\$ 784	\$ 100	\$ -	\$ -	\$ 884
State and municipal bonds	-	1,429	103 <sup>(1)</sup>	-	1,532
Foreign governments	86	107	3 <sup>(1)</sup>	-	196
Corporate obligations	-	1,140	76 <sup>(1)</sup>	-	1,216
Mortgage-backed securities:					
Residential mortgage-backed agency	-	988	-	-	988
Residential mortgage-backed non-agency	-	94	4 <sup>(1)</sup>	-	98
Commercial mortgage-backed	-	20	28 <sup>(1)</sup>	-	48
Asset-backed securities:					
Collateralized debt obligations	-	65	31 <sup>(1)</sup>	-	96
Other asset-backed	-	119	26 <sup>(1)</sup>	-	145
Total fixed-maturity investments	870	4,062	271	-	5,203
Money market securities	585	8	-	-	593
Perpetual debt and equity securities	23	20	14 <sup>(1)</sup>	-	57
Cash and cash equivalents	814	-	-	-	814
Derivative assets:					
Non-insured derivative assets:					
Interest rate derivatives	-	89	5 <sup>(1)</sup>	(90)	4
Total derivative assets	-	89	5	(90)	4

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

In millions	Fair Value Measurements at Reporting Date Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance as of December 31, 2012
<b>Assets of consolidated VIEs:</b>					
State and municipal bonds	-	41	-	-	41
Corporate obligations	-	215	78 <sup>(1)</sup>	-	293
<b>Mortgage-backed securities:</b>					
Residential mortgage-backed non-agency	-	869	6 <sup>(1)</sup>	-	875
Commercial mortgage-backed	-	410	7 <sup>(1)</sup>	-	417
<b>Asset-backed securities:</b>					
Collateralized debt obligations	-	215	125 <sup>(1)</sup>	-	340
Other asset-backed	-	120	64 <sup>(1)</sup>	-	184
Money market securities	210	-	-	-	210
Cash	176	-	-	-	176
Loans receivable	-	-	1,881	-	1,881
Loan repurchase commitments	-	-	1,086	-	1,086
<b>Total assets</b>	<b>\$ 2,678</b>	<b>\$ 6,049</b>	<b>\$ 3,537</b>	<b>\$ (90)</b>	<b>\$ 12,174</b>
<b>Liabilities:</b>					
Medium-term notes	\$ -	\$ -	\$ 165 <sup>(1)</sup>	\$ -	\$ 165
<b>Derivative liabilities:</b>					
<b>Insured derivatives:</b>					
Credit derivatives	-	13	2,921	-	2,934
<b>Non-insured derivatives:</b>					
Interest rate derivatives	-	287	4 <sup>(1)</sup>	(293)	(2)
Currency derivatives	-	1	1 <sup>(1)</sup>	-	2
<b>Other liabilities:</b>					
Warrants	-	6	-	-	6
<b>Liabilities of consolidated VIEs:</b>					
Variable interest entity notes	-	1,727	1,932	-	3,659
<b>Derivative liabilities:</b>					
Interest rate derivatives	-	141	-	-	141
Currency derivatives	-	-	21 <sup>(1)</sup>	-	21
<b>Total liabilities</b>	<b>\$ -</b>	<b>\$ 2,175</b>	<b>\$ 5,044</b>	<b>\$ (293)</b>	<b>\$ 6,926</b>

(1) - Unobservable inputs are either not developed by the Company or do not significantly impact the overall fair values of the aggregate financial assets and liabilities.

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Level 3 assets at fair value, as of September 30, 2013 and December 31, 2012 represented approximately 29% of total assets measured at fair value. Level 3 liabilities at fair value, as of September 30, 2013 and December 31, 2012 represented approximately 57% and 73%, respectively, of total liabilities measured at fair value.

The following tables present the fair values and carrying values of the Company's assets and liabilities that are disclosed at fair value but not reported at fair value on the Company's consolidated balance sheets as of September 30, 2013 and December 31, 2012:

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

	Fair Value Measurements at Reporting Date Using				Carry Value Balance as of September 30, 2013
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value Balance as of September 30, 2013	
<b>In millions</b>					
<b>Assets:</b>					
Other investments	\$ -	\$ -	\$ 6	\$ 6	\$ 6
Accrued investment income <sup>(1)</sup>	44	-	-	44	44
Receivable for investments sold <sup>(1)</sup>	23	-	-	23	23
Net cash collateral pledged <sup>(1)</sup>	62	-	-	62	62
<b>Assets of consolidated VIEs:</b>					
Investments held-to-maturity	-	-	2,566	2,566	2,809
<b>Total assets</b>	<b>\$ 129</b>	<b>\$ -</b>	<b>\$ 2,572</b>	<b>\$ 2,701</b>	<b>\$ 2,944</b>
<b>Liabilities:</b>					
Investment agreements	\$ -	\$ -	\$ 902	\$ 902	\$ 760
Medium-term notes	-	-	1,035	1,035	1,350
Long-term debt	10	1,282	-	1,292	1,677
Payable for investments purchased <sup>(2)</sup>	150	-	-	150	150
Secured loan <sup>(2)</sup>	-	-	50	50	50
<b>Liabilities of consolidated VIEs:</b>					
Variable interest entity notes	-	-	2,689	2,689	2,959
<b>Total liabilities</b>	<b>\$ 160</b>	<b>\$ 1,282</b>	<b>\$ 4,676</b>	<b>\$ 6,118</b>	<b>\$ 6,946</b>
<b>Financial Guarantees:</b>					
Gross	\$ -	\$ -	\$ 3,097	\$ 3,097	\$ 2,490
Ceded	-	-	69	69	77

(1) - Reported within Other assets on MBIA's consolidated balance sheets.

(2) - Reported within Other liabilities on MBIA's consolidated balance sheets.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

	Fair Value Measurements at Reporting Date Using					Carry Value Balance as of December 31, 2012
	Quoted Prices in	Significant	Significant	Fair Value		
	Active Markets for	Other Observable	Unobservable	Balance as of		
	Identical Assets (Level 1)	Inputs (Level 2)	Inputs (Level 3)	December 31, 2012	December 31, 2012	
In millions						
Assets:						
Other investments	\$ -	\$ -	\$ 9	\$ 9	\$ 9	
Accrued investment income <sup>(1)</sup>	43	-	-	43	43	
Receivable for investments sold <sup>(1)</sup>	17	-	-	17	17	
Net cash collateral pledged <sup>(1)</sup>	66	-	-	66	66	
Assets of consolidated VIEs:						
Investments held-to-maturity	-	-	2,674	2,674	2,829	
Total assets	\$ 126	\$ -	\$ 2,683	\$ 2,809	\$ 2,964	
Liabilities:						
Investment agreements	\$ -	\$ -	\$ 1,175	\$ 1,175	\$ 944	
Medium-term notes	-	-	860	860	1,433	
Long-term debt	9	702	-	711	1,732	
Payable for investments purchased <sup>(2)</sup>	50	-	-	50	50	
Liabilities of consolidated VIEs:						
Variable interest entity notes	-	-	3,147	3,147	3,465	
Total liabilities	\$ 59	\$ 702	\$ 5,182	\$ 5,943	\$ 7,624	
Financial Guarantees:						
Gross	\$ -	\$ -	\$ 650	\$ 650	\$ 143	
Ceded	-	-	97	97	91	

(1) - Reported within Other assets on MBIA's consolidated balance sheets.

(2) - Reported within Other liabilities on MBIA's consolidated balance sheets.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

The following tables present information about changes in Level 3 assets (including short-term investments) and liabilities measured at fair value on a recurring basis for the three months ended September 30, 2013 and 2012:

**Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Three Months Ended September 30, 2013**

In millions	Balance, Beginning of Period	Realized Gains / (Losses)	Unrealized Gains / (Losses) Included in Earnings	Unrealized Gains / (Losses) Included in OCI	Foreign Exchange Recognized in OCI or Earnings	Purchases	Issuances	Settlements	Sales	Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets still held as of September 30, 2013
Assets:													
Foreign governments	\$ 3	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (3)	\$ -	\$ 5	\$ -	\$ 5	\$ -
Corporate obligations	63	(7)	1	7	2	-	-	(14)	(6)	1	-	47	1
Residential mortgage-backed agency	3	-	-	-	-	-	-	-	-	17	(3)	17	-
Residential mortgage-backed non-agency	1	-	-	-	-	-	-	-	-	-	(1)	-	-
Commercial mortgage-backed	13	-	-	-	-	-	-	(1)	-	2	-	14	-
Collateralized debt obligations	85	-	-	7	-	-	-	(3)	-	10	(11)	88	-
Other asset-backed	64	-	-	(5)	-	-	-	(4)	-	3	(1)	57	-
State and municipal bonds	63	-	-	-	-	-	-	(1)	-	-	-	62	-
Perpetual debt and equity securities	10	-	-	-	1	-	-	-	-	-	-	11	-
Assets of consolidated VIEs:													

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Corporate obligations	48	-	-	-	-	-	-	-	-	-	-	48	-
Residential mortgage-backed non-agency	2	-	-	-	-	-	-	-	-	2	-	4	-
Commercial mortgage-backed	4	-	(1)	-	-	-	-	(1)	-	-	-	2	-
Collateralized debt obligations	35	-	1	-	-	-	-	(4)	-	-	(12)	20	(1)
Other asset-backed	63	-	(7)	-	-	-	-	(1)	-	1	(6)	50	(1)
Loans receivable	1,790	-	(12)	-	-	-	-	(74)	-	-	-	1,704	(12)
Loan repurchase commitments	1,115	-	1	-	-	-	-	-	-	-	-	1,116	1
Total assets	\$ 3,362	\$ (7)	\$ (17)	\$ 9	\$ 3	\$ -	\$ -	\$ (106)	\$ (6)	\$ 41	\$ (34)	\$ 3,245	\$ (12)

In millions	Balance, Beginning of Period	Realized (Gains) / Losses	Unrealized (Gains) / Losses Included in Earnings	Unrealized (Gains) / Losses Included in OCI	Foreign Exchange Recognized in OCI or Earnings	Purchases	Issuances	Settlements	Sales	Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	Change in Unrealized (Gains) Losses for the Period Included in Earnings for Liabilities still held as of September 30, 2013
Liabilities:													
Medium-term notes	\$ 188	\$ -	\$ 9	\$ -	\$ 7	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 204	\$ 17
Credit derivatives, net	1,648	28	(285)	-	-	-	-	(28)	-	-	-	1,363	(285)
Interest rate derivatives, net	-	-	-	-	-	-	-	-	-	-	-	-	(15)
Liabilities of consolidated VIEs:													
VIE notes	824	-	(6)	-	-	-	-	(73)	-	-	-	745	(6)
Currency derivatives, net	16	-	-	-	(1)	-	-	-	-	-	-	15	(1)
Total liabilities	\$ 2,676	\$ 28	\$ (282)	\$ -	\$ 6	\$ -	\$ -	\$ (101)	\$ -	\$ -	\$ -	\$ 2,327	\$ (290)

(1) - Transferred in and out at the end of the period.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)****Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Three Months Ended September 30, 2012**

In millions	Balance, Beginning of Period	Realized Gains / (Losses)	Unrealized Gains / (Losses) Included in Earnings	Unrealized Gains / (Losses) Included in OCI	Foreign Exchange Recognized in OCI or Earnings	Purchases	Issuances	Settlements	Sales	Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets still held as of September 30, 2012
<b>Assets:</b>													
Foreign governments	\$ 12	\$ -	\$ -	\$ -	\$ 1	\$ 9	\$ -	\$ (10)	\$ -	\$ -	\$ -	\$ 12	\$ -
Corporate obligations	98	-	4	(2)	-	2	-	(13)	-	10	(8)	91	3
Residential mortgage-backed agency	4	-	-	-	-	-	-	(1)	-	-	(3)	-	-
Residential mortgage-backed non-agency	33	(1)	-	2	-	-	-	(5)	-	1	(23)	7	-
Commercial mortgage-backed	27	-	-	1	-	1	-	-	-	1	-	30	-
Collateralized debt obligations	29	(4)	-	9	-	-	-	(4)	-	4	(4)	30	-
Other asset-backed	69	(2)	-	2	-	1	-	(1)	-	4	-	73	-
State and municipal bonds	25	-	-	-	-	-	-	(2)	-	71	-	94	-
Perpetual debt and equity securities	13	-	1	-	-	-	-	-	-	-	-	14	-
<b>Assets of consolidated VIEs:</b>													
Corporate obligations	95	-	(10)	-	-	-	-	(2)	-	3	(3)	83	1
Residential mortgage-backed	10	-	-	-	-	-	-	(1)	-	2	(3)	8	-

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non-agency														
Commercial mortgage-backed	12	-	1	-	-	-	-	-	-	-	-	13	1	
Collateralized debt obligations	140	-	(5)	2	-	-	-	(1)	-	37	-	173	(2)	
Other														
asset-backed	42	-	(1)	-	-	-	-	(5)	-	30	-	66	1	
Loans receivable	1,903	-	61	-	-	-	-	(72)	-	-	-	1,892	61	
Loan repurchase commitments	1,032	-	19	-	-	-	-	-	-	-	-	1,051	19	
Total assets	\$ 3,544	\$ (7)	\$ 70	\$ 14	\$ 1	\$ 13	\$ -	\$ (117)	\$ -	\$ 163	\$ (44)	\$ 3,637	\$ 84	

																		Change in Unrealized (Gains) Losses for the Period Included in Earnings for Liabilities still held as of September 30,
	Balance, Beginning of Period	Realized (Gains) / Losses	Unrealized (Gains) / Losses Included in Earnings	Unrealized (Gains) / Losses Included in OCI	Foreign Exchange Recognized in OCI or Earnings	Purchases	Issuances	Settlements	Sales	Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	September 30, 2012					
In millions																		
Liabilities:																		
Medium-term notes	\$ 151	\$ -	\$ 14	\$ -	\$ 3	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 168	\$ 14					
Credit derivatives, net	3,285	(12)	32	-	-	-	-	12	-	-	-	3,317	33					
Interest rate derivatives, net	(4)	-	-	-	-	-	-	-	-	4	-	-	5					
Currency derivatives, net	-	-	-	-	-	-	-	-	-	1	-	1	-					
Liabilities of consolidated VIEs:																		
VIE notes	1,867	-	128	-	-	-	-	(110)	-	-	-	1,885	128					
Currency derivatives, net	21	-	2	-	-	-	-	-	-	-	-	23	2					
Total liabilities	\$ 5,320	\$ (12)	\$ 176	\$ -	\$ 3	\$ -	\$ -	\$ (98)	\$ -	\$ 5	\$ -	\$ 5,394	\$ 182					

(1) - Transferred in and out at the end of the period.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

Transfers into and out of Level 3 were \$41 million and \$34 million, respectively, for the three months ended September 30, 2013. Transfers into and out of Level 2 were \$34 million and \$41 million, respectively, for the three months ended September 30, 2013. Transfers into Level 3 were principally related to RMBS agency, CDOs and foreign governments, where inputs, which are significant to their valuation, became unobservable during the quarter. CDOs and other ABS, comprised the majority of the transferred instruments out of Level 3 where inputs, which are significant to their valuation, became observable during the quarter. These inputs included spreads, prepayment speeds, default speeds, default severities, yield curves observable at commonly quoted intervals, and market corroborated inputs. There were no transfers into or out of Level 1.

Transfers into and out of Level 3 were \$168 million and \$44 million, respectively, for the three months ended September 30, 2012. Transfers into and out of Level 2 were \$44 million and \$168 million, respectively, for the three months ended September 30, 2012. Transfers into Level 3 were principally related to state and municipal bonds, CDOs, other ABS and corporate obligations where inputs, which are significant to their valuation, became unobservable during the quarter. RMBS non-agency and corporate obligations comprised the majority of the transferred instruments out of Level 3 where inputs, which are significant to their valuation, became observable during the quarter. These inputs included spreads, prepayment speeds, default speeds, default severities, yield curves observable at commonly quoted intervals, and market corroborated inputs. There were no transfers into or out of Level 1.

All Level 1, 2 and 3 designations are made at the end of each accounting period.

The following tables present information about changes in Level 3 assets (including short-term investments) and liabilities measured at fair value on a recurring basis for the nine months ended September 30, 2013 and 2012:

**Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Nine Months Ended September 30, 2013**

																		Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets still held as of September 30,
	Balance, Beginning of Year	Realized Gains / (Losses)	Unrealized Gains / (Losses) Included in Earnings	Unrealized Gains / (Losses) Included in OCI	Foreign Exchange Recognized in OCI or Earnings	Purchases	Issuances	Settlements	Sales	Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	September 30,					
In millions																		
Assets:																		
Foreign governments	\$ 3	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (11)	\$ -	\$ 16	\$ (3)	\$ 5	\$ -					
	76	(5)	6	11	-	1	-	(14)	(29)	1	-	47	6					

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Corporate obligations													
Residential mortgage-backed agency	-	-	-	-	-	-	-	-	-	20	(3)	17	-
Residential mortgage-backed non-agency	4	-	-	-	-	-	-	(3)	-	-	(1)	-	-
Commercial mortgage-backed	28	-	-	4	-	-	-	(2)	(18)	3	(1)	14	-
Collateralized debt obligations	31	(2)	-	11	-	61	-	(14)	(5)	28	(22)	88	1
Other asset-backed	26	-	-	(5)	-	3	-	(9)	-	47	(5)	57	-
State and municipal bonds	103	2	-	(1)	-	-	-	(4)	(12)	42	(68)	62	-
Perpetual debt and equity securities	14	-	-	-	-	-	-	-	-	-	(3)	11	-
Assets of consolidated VIEs:													
Corporate obligations	78	(4)	(7)	6	-	-	-	(3)	(25)	3	-	48	-
Residential mortgage-backed non-agency	6	-	6	-	-	-	-	(7)	-	3	(4)	4	-
Commercial mortgage-backed	7	-	(1)	-	-	-	-	-	(24)	20	-	2	1
Collateralized debt obligations	125	-	(8)	5	-	-	-	(5)	(84)	1	(14)	20	2
Other asset-backed	64	-	(7)	-	-	-	-	(10)	(2)	11	(6)	50	3
Loans receivable	1,881	-	208	-	-	-	-	(211)	(174)	-	-	1,704	194
Loan repurchase commitments	1,086	-	140	-	-	-	-	(110)	-	-	-	1,116	140
Total assets	\$ 3,532	\$ (9)	\$ 337	\$ 31	\$ -	\$ 65	\$ -	\$ (403)	\$ (373)	\$ 195	\$ (130)	\$ 3,245	\$ 347

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

In millions	Balance, Beginning of Year	Realized (Gains) / Losses	Unrealized (Gains) / Losses Included in Earnings	Unrealized (Gains) / Losses Included in OCI	Foreign Exchange Recognized in OCI or Earnings	Purchases	Issuances	Settlements	Sales	Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	Change in Unrealized (Gains) Losses for the Period Included in Earnings for Liabilities still held as of September 30, 2013
Liabilities:													
Medium-term notes	\$ 165	\$ -	\$ 34	\$ -	\$ 5	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 204	\$ 39
Credit derivatives, net	2,921	1,548	(1,562)	-	-	-	-	(1,548)	-	4	-	1,363	301
Interest rate derivatives, net	(1)	-	2	-	-	-	-	-	-	-	(1)	-	(21)
Currency derivatives, net	1	-	-	-	-	-	-	-	-	-	(1)	-	-
Liabilities of consolidated VIEs:													
VIE notes	1,932	-	140	-	-	-	-	(251)	(1,076)	-	-	745	53
Currency derivatives, net	21	-	(5)	-	(1)	-	-	-	-	-	-	15	(6)
Total liabilities	\$ 5,039	\$ 1,548	\$ (1,391)	\$ -	\$ 4	\$ -	\$ -	\$ (1,799)	\$ (1,076)	\$ 4	\$ (2)	\$ 2,327	\$ 366

(1) - Transferred in and out at the end of the period.

**Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Nine Months Ended September 30, 2012**

In millions

Purchases Issuances Settlements Sales

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	Balance, Beginning of Year	Realized Gains / (Losses)	Unrealized Gains / (Losses) Included in Earnings	Unrealized Gains / (Losses) Included in OCI	Foreign Exchange Recognized in OCI or Earnings					Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets still held as of September 30, 2012
Assets:													
Foreign governments	\$ 11	\$ -	\$ -	\$ -	\$ 1	\$ 22	\$ -	\$ (19)	\$ (3)	\$ -	\$ -	\$ 12	\$ -
Corporate obligations	207	(15)	9	24	-	18	-	(29)	(140)	25	(8)	91	8
Residential mortgage-backed agency	8	-	-	1	-	-	-	(1)	-	4	(12)	-	-
Residential mortgage-backed non-agency	17	(1)	-	(1)	-	-	-	(11)	(3)	31	(25)	7	-
Commercial mortgage-backed	24	-	-	5	-	1	-	-	-	1	(1)	30	-
Collateralized debt obligations	60	(9)	-	18	-	-	-	(12)	(10)	14	(31)	30	-
Other asset-backed	317	(58)	-	71	-	5	-	(11)	(250)	5	(6)	73	-
State and municipal bonds	28	-	-	-	-	-	-	(5)	-	71	-	94	-
Perpetual debt and equity securities	11	-	1	1	-	-	-	-	-	4	(3)	14	-
Assets of consolidated VIEs:													
Corporate obligations	69	-	(15)	(6)	-	28	-	(5)	-	15	(3)	83	3
Residential mortgage-backed non-agency	21	-	6	-	-	-	-	(5)	(15)	5	(4)	8	3
Commercial mortgage-backed	22	-	3	-	-	-	-	(3)	(8)	5	(6)	13	2
Collateralized debt obligations	203	-	(5)	(1)	-	-	-	(1)	(74)	51	-	173	5
Other asset-backed	67	-	4	-	-	4	-	(8)	(35)	34	-	66	5
Loans receivable	2,046	-	52	-	-	-	-	(204)	(2)	-	-	1,892	52
Loan repurchase commitments	1,077	-	(26)	-	-	-	-	-	-	-	-	1,051	(26)
Total assets	\$ 4,188	\$ (83)	\$ 29	\$ 112	\$ 1	\$ 78	\$ -	\$ (314)	\$ (540)	\$ 265	\$ (99)	\$ 3,637	\$ 52



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

In millions	Balance, Beginning of Year	Realized (Gains) / Losses	Unrealized (Gains) / Losses Included in Earnings	Unrealized (Gains) / Losses Included in OCI	Foreign Exchange Recognized in OCI or Earnings	Purchases	Issuances	Settlements	Sales	Transfers into Level 3 <sup>(1)</sup>	Transfers out of Level 3 <sup>(1)</sup>	Ending Balance	Change in Unrealized (Gains) Losses for the Period Included in Earnings for Liabilities still held as of September 30, 2012
Liabilities:													
Medium-term notes	\$ 165	\$ -	\$ 3	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 168	\$ 4
Credit derivatives, net	4,790	420	(1,473)	-	-	-	-	(420)	-	-	-	3,317	(538)
Interest rate derivatives, net	(3)	-	(1)	-	-	-	-	-	-	4	-	-	12
Currency derivatives, net	-	-	-	-	-	-	-	-	-	1	-	1	-
Liabilities of consolidated VIEs:													
VIE notes	2,889	-	348	-	-	-	-	(369)	(983)	-	-	1,885	292
Credit derivatives, net	80	-	2	-	-	-	-	-	(82)	-	-	-	-
Currency derivatives, net	17	-	6	-	-	-	-	-	-	-	-	23	6
Total liabilities	\$ 7,938	\$ 420	\$ (1,115)	\$ -	\$ -	\$ -	\$ -	\$ (789)	\$ (1,065)	\$ 5	\$ -	\$ 5,394	\$ (224)

(1) - Transferred in and out at the end of the period.

Transfers into and out of Level 3 were \$199 million and \$132 million, respectively, for the nine months ended September 30, 2013. Transfers into and out of Level 2 were \$132 million and \$199 million, respectively, for the nine months ended September 30, 2013. Transfers into Level 3 were principally related to other ABS, state and municipal bonds, CDOs, RMBS agency and CMBS where inputs, which are significant to their valuation, became unobservable during the period. State and municipal bonds and CDOs comprised the majority of the transferred instruments

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out of Level 3 where inputs, which are significant to their valuation, became observable during the period. These inputs included spreads, prepayment speeds, default speeds, default severities, yield curves observable at commonly quoted intervals, and market corroborated inputs. There were no transfers into or out of Level 1.

Transfers into and out of Level 3 were \$270 million and \$99 million, respectively, for the nine months ended September 30, 2012. Transfers into and out of Level 2 were \$99 million and \$270 million, respectively, for the nine months ended September 30, 2012. Transfers into Level 3 were principally related to state and municipal bonds, CDOs, other asset backed, RMBS non-agency and corporate obligations where inputs, which are significant to their valuation, became unobservable during the period. CDOs, RMBS non-agency, RMBS agency and corporate obligations comprised the majority of the transferred instruments out of Level 3 where inputs, which are significant to their valuation, became observable during the period. These inputs included spreads, prepayment speeds, default speeds, default severities, yield curves observable at commonly quoted intervals, and market corroborated inputs. There were no transfers into or out of Level 1.

All Level 1, 2 and 3 designations are made at the end of each accounting period.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

Gains and losses (realized and unrealized) included in earnings related to Level 3 assets and liabilities for the three months ended September 30, 2013 and 2012 are reported on the Company's consolidated statements of operations as follows:

	Three Months Ended September 30, 2013		Three Months Ended September 30, 2012	
		Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets and Liabilities still held as of September 30, 2013		Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets and Liabilities still held as of September 30, 2012
In millions	Total Gains (Losses) Included in Earnings		Total Gains (Losses) Included in Earnings	
<b>Revenues:</b>				
Unrealized gains (losses) on insured derivatives	\$ 285	\$ 285	\$ (32)	\$ (33)
Realized gains (losses) and other settlements on insured derivatives	(28)	-	12	-
Net gains (losses) on financial instruments at fair value and foreign exchange	(24)	(1)	(9)	(16)
Net investment losses related to other-than-temporary impairments	-	-	(7)	-
<b>Revenues of consolidated VIEs:</b>				
Net gains (losses) on financial instruments at fair value and foreign exchange	(11)	(6)	(65)	(49)
<b>Total</b>	<b>\$ 222</b>	<b>\$ 278</b>	<b>\$ (101)</b>	<b>\$ (98)</b>

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

Gains and losses (realized and unrealized) included in earnings relating to Level 3 assets and liabilities for the nine months ended September 30, 2013 and 2012 are reported on the Company's consolidated statements of operations as follows:

	Nine Months Ended September 30, 2013		Nine Months Ended September 30, 2012	
		Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets and Liabilities still held as of September 30, 2013	Total Gains (Losses) Included in Earnings	Change in Unrealized Gains (Losses) for the Period Included in Earnings for Assets and Liabilities still held as of September 30, 2012
<b>In millions</b>	<b>Total Gains (Losses) Included in Earnings</b>			
Revenues:				
Unrealized gains (losses) on insured derivatives	\$ 1,562	\$ (301)	\$ 1,473	\$ 538
Realized gains (losses) and other settlements on insured derivatives	(1,548)	-	(420)	-
Net gains (losses) on financial instruments at fair value and foreign exchange	(39)	(11)	(8)	(8)
Net investment losses related to other-than-temporary impairments	-	-	(67)	-
Revenues of consolidated VIEs:				
Net gains (losses) on financial instruments at fair value and foreign exchange	193	293	(337)	(254)
Total	\$ 168	\$ (19)	\$ 641	\$ 276

***Fair Value Option***

The Company elected to record at fair value certain financial instruments of VIEs that have been consolidated in connection with the adoption of the accounting guidance for consolidation of VIEs, among others.

The following table presents the changes in fair value included in the Company's consolidated statements of operations for the three and nine months ended September 30, 2013 and 2012 for all financial instruments for which the fair value option was elected:

In millions	Net Gains (Losses) on Financial Instruments at Fair Value and Foreign Exchange			
	Three Months Ended September 30, 2013		Three Months Ended September 30, 2012	
	2013	2012	2013	2012
Fixed-maturity securities held at fair value	\$ (37)	\$ 21	\$ (35)	\$ (36)
Loans receivable at fair value:				
Residential mortgage loans	(87)	(4)	(16)	(103)
Other loans	-	(7)	13	(48)
Loan repurchase commitments	1	19	140	62
Variable interest entity notes	164	12	85	140

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 6: Fair Value of Financial Instruments (continued)**

The following table reflects the difference between the aggregate fair value and the aggregate remaining contractual principal balance outstanding as of September 30, 2013 and December 31, 2012 for loans and VIE notes for which the fair value option was elected:

In millions	As of September 30, 2013			As of December 31, 2012		
	Contractual Outstanding Principal	Fair Value	Difference	Contractual Outstanding Principal	Fair Value	Difference
Loans receivable at fair value:						
Residential mortgage loans	\$ 1,932	\$ 1,622	\$ 310	\$ 2,307	\$ 1,735	\$ 572
Residential mortgage loans (90 days or more past due)	221	82	139	244	54	190
Other loans	-	-	-	22	22	-
Other loans (90 days or more past due)	-	-	-	197	70	127
Total loans receivable at fair value	\$ 2,153	\$ 1,704	\$ 449	\$ 2,770	\$ 1,881	\$ 889
Variable interest entity notes	\$ 3,859	\$ 2,426	\$ 1,433	\$ 9,021	\$ 3,659	\$ 5,362

Substantially all gains and losses included in earnings during the periods ended September 30, 2013 and December 31, 2012 on loans receivable and VIE notes reported in the preceding table are attributable to credit risk. This is primarily due to the high rate of defaults on loans and the collateral supporting the VIE notes, resulting in depressed pricing of the financial instruments.

**Note 7: Investments**

Investments, excluding those elected under the fair value option, include debt and equity securities classified as either AFS or HTM. Other invested assets designated as AFS are primarily comprised of money market funds.

The following tables present the amortized cost, fair value, corresponding gross unrealized gains and losses and other-than-temporary impairments ( OTTI ) for AFS and HTM investments in the Company's consolidated investment portfolio as of September 30, 2013 and December 31, 2012:

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)**

In millions	September 30, 2013				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Other-Than-Temporary Impairments <sup>(1)</sup>
<b>AFS Investments</b>					
Fixed-maturity investments:					
U.S. Treasury and government agency	\$ 526	\$ 19	\$ (8)	\$ 537	\$ -
State and municipal bonds	1,632	30	(52)	1,610	-
Foreign governments	192	9	-	201	-
Corporate obligations	1,616	32	(26)	1,622	-
Mortgage-backed securities:					
Residential mortgage-backed agency	942	10	(18)	934	-
Residential mortgage-backed non-agency	67	13	(6)	74	3
Commercial mortgage-backed	34	1	(1)	34	-
Asset-backed securities:					
Collateralized debt obligations	210	2	(57)	155	(12)
Other asset-backed	148	2	(17)	133	-
Total fixed-maturity investments	5,367	118	(185)	5,300	(9)
Money market securities	911	-	-	911	-
Perpetual debt and equity securities	9	1	-	10	-
Assets of consolidated VIEs:					
Money market securities	156	-	-	156	-
Total AFS investments	\$ 6,443	\$ 119	\$ (185)	\$ 6,377	\$ (9)
<b>HTM Investments</b>					
Assets of consolidated VIEs:					
Corporate obligations	\$ 2,809	\$ 8	\$ (251)	\$ 2,566	\$ -
Total HTM investments	\$ 2,809	\$ 8	\$ (251)	\$ 2,566	\$ -

(1) - Represents unrealized gains or losses on other than temporarily impaired securities recognized in AOCI, which includes the non-credit component of impairments, as well as all subsequent changes in fair value of such impaired securities reported in AOCI.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)**

In millions	December 31, 2012				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Other-Than-Temporary Impairments <sup>(1)</sup>
<b>AFS Investments</b>					
Fixed-maturity investments:					
U.S. Treasury and government agency	\$ 819	\$ 40	\$ (1)	\$ 858	\$ -
State and municipal bonds	1,446	97	(12)	1,531	-
Foreign governments	183	13	-	196	-
Corporate obligations	1,058	54	(20)	1,092	5
Mortgage-backed securities:					
Residential mortgage-backed agency	939	19	(1)	957	-
Residential mortgage-backed non-agency	86	11	(8)	89	-
Commercial mortgage-backed	46	-	(4)	42	-
Asset-backed securities:					
Collateralized debt obligations	161	1	(71)	91	(25)
Other asset-backed	145	3	(11)	137	-
Total fixed-maturity investments	4,883	238	(128)	4,993	(20)
Money market securities	580	-	-	580	-
Perpetual debt and equity securities	22	1	-	23	-
Assets of consolidated VIEs:					
State and municipal bonds	38	3	-	41	-
Corporate obligations	177	9	(6)	180	-
Mortgage-backed securities:					
Residential mortgage-backed non-agency	92	-	(10)	82	-
Asset-backed securities:					
Collateralized debt obligations	97	-	(8)	89	-
Other asset-backed	23	-	-	23	-
Money market securities	210	-	-	210	-
Total AFS investments	\$ 6,122	\$ 251	\$ (152)	\$ 6,221	\$ (20)
<b>HTM Investments</b>					
Assets of consolidated VIEs:					
Corporate obligations	\$ 2,829	\$ 2	\$ (157)	\$ 2,674	\$ -
Total HTM investments	\$ 2,829	\$ 2	\$ (157)	\$ 2,674	\$ -

(1) - Represents unrealized gains or losses on other than temporarily impaired securities recognized in AOCI, which includes the non-credit component of impairments, as well as all subsequent changes in fair value of such impaired securities reported in AOCI.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)**

The following table presents the distribution by contractual maturity of AFS and HTM fixed-maturity securities at amortized cost and fair value as of September 30, 2013. Contractual maturity may differ from expected maturity as borrowers may have the right to call or prepay obligations.

In millions	AFS Securities		HTM Securities Consolidated VIEs	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ 551	\$ 552	\$ -	\$ -
Due after one year through five years	913	929	-	-
Due after five years through ten years	926	925	-	-
Due after ten years	1,576	1,564	2,809	2,566
Mortgage-backed and asset-backed	1,401	1,330	-	-
Total fixed-maturity investments	\$ 5,367	\$ 5,300	\$ 2,809	\$ 2,566

***Deposited and Pledged Securities***

The fair value of securities on deposit with various regulatory authorities was \$11 million and \$10 million as of September 30, 2013 and December 31, 2012, respectively. These deposits are required to comply with state insurance laws.

The Company enters into securities borrowing and lending contracts in connection with MBIA's collateralized investment agreement activities. Such contracts are only transacted with high-quality dealer firms. It is the Company's policy to take possession of securities borrowed under these contracts. The Company minimizes credit risk from counterparties that might be unable to fulfill their contractual obligations by monitoring customer credit exposure and collateral values and requiring additional collateral to be deposited with the Company when deemed necessary.

Substantially all of the obligations under investment agreements require the Company to pledge securities as collateral. Securities pledged in connection with investment agreement activities may not be repledged by the investment agreement counterparty. As of September 30, 2013 and December 31, 2012, the fair value of securities pledged as collateral for these investment agreements approximated \$750 million and \$820 million, respectively. The Company's collateral as of September 30, 2013 consisted principally of RMBS, U.S. Treasury and government agency bonds and state and municipal bonds, and was primarily held with major U.S. banks. Additionally, the Company pledged cash and money market securities as collateral under investment agreements in the amount of \$24 million and \$144 million as of September 30, 2013 and December 31, 2012, respectively.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)*****Impaired Investments***

The following tables present the gross unrealized losses related to AFS and HTM investments as of September 30, 2013 and December 31, 2012:

In millions	September 30, 2013					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>AFS Investments</b>						
Fixed-maturity investments:						
U.S. Treasury and government agency	\$ 208	\$ (8)	\$ 2	\$ -	\$ 210	\$ (8)
State and municipal bonds	730	(48)	58	(4)	788	(52)
Foreign governments	12	-	-	-	12	-
Corporate obligations	610	(23)	20	(3)	630	(26)
Mortgage-backed securities:						
Residential mortgage-backed agency	528	(18)	32	-	560	(18)
Residential mortgage-backed non-agency	5	-	23	(6)	28	(6)
Commercial mortgage-backed	22	(1)	1	-	23	(1)
Asset-backed securities:						
Collateralized debt obligations	9	(1)	128	(56)	137	(57)
Other asset-backed	22	-	56	(17)	78	(17)
Total fixed-maturity investments	2,146	(99)	320	(86)	2,466	(185)
Perpetual debt and equity securities	4	-	-	-	4	-
Total AFS investments	\$ 2,150	\$ (99)	\$ 320	\$ (86)	\$ 2,470	\$ (185)
<b>HTM Investments</b>						
Assets of consolidated VIEs:						
Corporate obligations	\$ -	\$ -	\$ 1,174	\$ (251)	\$ 1,174	\$ (251)
Total HTM investments	\$ -	\$ -	\$ 1,174	\$ (251)	\$ 1,174	\$ (251)

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)**

In millions	Less than 12 Months		December 31, 2012 12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>AFS Investments</b>						
Fixed-maturity investments:						
U.S. Treasury and government agency	\$ 234	\$ (1)	\$ -	\$ -	\$ 234	\$ (1)
State and municipal bonds	69	-	87	(12)	156	(12)
Foreign governments	11	-	1	-	12	-
Corporate obligations	202	(2)	57	(18)	259	(20)
Mortgage-backed securities:						
Residential mortgage-backed agency	173	(1)	38	-	211	(1)
Residential mortgage-backed non-agency	4	-	28	(8)	32	(8)
Commercial mortgage-backed	3	-	27	(4)	30	(4)
Asset-backed securities:						
Collateralized debt obligations	1	-	80	(71)	81	(71)
Other asset-backed	4	-	65	(11)	69	(11)
Total fixed-maturity investments	701	(4)	383	(124)	1,084	(128)
Perpetual debt and equity securities	1	-	1	-	2	-
Assets of consolidated VIEs:						
Corporate obligations	-	-	31	(6)	31	(6)
Mortgage-backed securities:						
Residential mortgage-backed non-agency	-	-	82	(10)	82	(10)
Asset-backed securities:						
Collateralized debt obligations	-	-	85	(8)	85	(8)
Total AFS investments	\$ 702	\$ (4)	\$ 582	\$ (148)	\$ 1,284	\$ (152)
<b>HTM Investments</b>						
Assets of consolidated VIEs:						
Corporate obligations	\$ 297	\$ (19)	\$ 1,287	\$ (138)	\$ 1,584	\$ (157)
Total HTM investments	\$ 297	\$ (19)	\$ 1,287	\$ (138)	\$ 1,584	\$ (157)

Gross unrealized losses on AFS securities increased as of September 30, 2013 compared with December 31, 2012 primarily due to market price depreciation caused by rising interest rates and not the result of OTTI. Gross unrealized losses on HTM securities increased as of September 30, 2013 compared with December 31, 2012 primarily due to market price depreciation driven by a credit ratings downgrade on one of the HTM corporate obligations and not the result of OTTI.

With the weighting applied on the fair value of each security relative to the total fair value, the weighted average contractual maturity of securities in an unrealized loss position as of September 30, 2013 and December 31, 2012 was 19 and 23 years, respectively. As of September 30, 2013 and December 31, 2012, there were 64 and 153 securities, respectively, that were in an unrealized loss position for a continuous twelve-month period or longer, of which the fair values of 39 and 89 securities, respectively, were below book value by more than

5%.

The following table presents the distribution of securities in an unrealized loss position for a continuous twelve-month period or longer by percentage of fair value below book value by more than 5%:

Percentage of Fair Value Below Book Value	Number of Securities	AFS Securities		Number of Securities	HTM Securities	
		Book Value (in millions)	Fair Value (in millions)		Book Value (in millions)	Fair Value (in millions)
> 5% to 15%	13	\$ 110	\$ 101	-	\$ -	\$ -
> 15% to 25%	12	66	52	-	-	-
> 25% to 50%	5	53	36	1	575	345
> 50%	8	52	9	-	-	-
Total	38	\$ 281	\$ 198	1	\$ 575	\$ 345

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)**

The following table presents the fair values and gross unrealized losses by credit rating category of ABS, MBS and corporate obligations included in the Company's consolidated AFS investment portfolio as of September 30, 2013 for which fair value was less than amortized cost. The credit ratings are based on ratings from Moody's as of September 30, 2013 or an alternate ratings source, such as S&P, when a security is not rated by Moody's. For investments that are insured by various third-party guarantee insurers, the credit rating reflects the higher of the insurer's rating or the underlying bond's rating.

Asset Type	Aaa		Aa		A		Baa		Below Investment Grade		Not Rated		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Corporate obligations	\$ 13	\$ -	\$ 59	\$ (5)	\$ 1	\$ -	\$ 3	\$ -	\$ 135	\$ (69)	\$ 4	\$ -	\$ 215	\$ -
	558	(18)	8	-	4	-	17	(1)	9	(1)	15	(5)	611	-
	129	(1)	205	(8)	205	(12)	74	(4)	17	(1)	-	-	630	-
	\$ 700	\$ (19)	\$ 272	\$ (13)	\$ 210	\$ (12)	\$ 94	\$ (5)	\$ 161	\$ (71)	\$ 19	\$ (5)	\$ 1,456	\$ -

The total ABS, MBS and corporate obligations reported in the preceding table include those which are guaranteed by financial guarantors. In addition, the following table presents information on ABS, MBS and corporate obligations guaranteed by the Company and third-party financial guarantors.

Asset Type	Average Credit Rating with the Effect of Guarantee	Average Credit Rating without the Effect of Guarantee	Insured Securities Rated Below Investment Grade without the Effect of Guarantee (in millions)	
			Fair Value	Percentage
ABS	Below investment grade	Below investment grade	\$ 101	64%
MBS	Baa	Below investment grade	20	99%
Corporate obligations	A	A	-	- %

Refer to the table in the Determination of Credit Loss Guaranteed by the Company and Other Third-Party Guarantors section within the OTTI section of this note for information on the insured securities included in the table above.

The Company concluded that it does not have the intent to sell securities in an unrealized loss position and it is more likely than not, that it would not have to sell these securities before recovery of their cost basis. In making this conclusion, the Company examined the cash flow projections for its investment portfolios, the potential sources and uses of cash in its businesses, and the cash resources available to its business other than sales of securities. It also considered the existence of any risk management or other plans as of September 30, 2013 that would require the sale of impaired securities. Impaired securities that the Company intends to sell before the expected recovery of such securities' fair values have been written down to fair value.

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

***Evaluating AFS Securities for OTTI***

The Company has an ongoing review process for all securities in its investment portfolio, including a quarterly assessment of OTTI. This evaluation includes both qualitative and quantitative considerations. In assessing whether a decline in value is related to a credit loss, the Company considers several factors, including but not limited to (i) the magnitude and duration of declines in fair value; (ii) the reasons for the declines in fair value, such as general credit spread movements in each asset-backed sector, transaction-specific changes in credit spreads, credit rating downgrades, modeled defaults, and principal and interest payment priorities within each investment structure; and (iii) any guarantees associated with a security such as those provided by financial guarantee insurance companies, including MBIA Corp. and National.

In calculating credit-related losses, the Company utilizes cash flow modeling based on the type of security. The Company's cash flow analysis considers all sources of cash, including credit enhancement, that support the payment of amounts owed by an issuer of a security. This includes the consideration of cash expected to be provided by financial guarantors, including MBIA Corp., resulting from an actual or potential insurance policy claim. In general, any change in the amount and/or timing of cash flows received or expected to be received, whether or not such cash flows are contractually defined, is reflected in the Company's cash flow analysis for purposes of assessing an OTTI loss on an impaired security.

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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 7: Investments (continued)**

Each quarter, an internal committee, comprising staff that is independent of the Company's evaluation process for determining OTTI of securities, reviews and approves the valuation of investments. Among other responsibilities, this committee ensures that the Company's process for identifying and calculating OTTI, including the use of models and assumptions, is reasonable and complies with the Company's internal policy.

#### *Determination of Credit Loss on ABS, MBS and Corporate Obligations*

Investments with unrealized losses that met the above criteria were tested for OTTI and principally related to ABS, MBS and corporate obligations.

ABS investments are evaluated for OTTI using historical collateral performance, deal waterfall and structural protections, credit ratings, and forward looking projections of collateral performance based on business and economic conditions specific to each collateral type and risk. The underlying collateral is evaluated to identify any specific performance concerns, and stress scenarios are considered in forecasting ultimate returns of principal. Based on this evaluation, if a principal default is projected for a security, estimated future cash flows are discounted at the security's interest rate used to recognize interest income on the security. For CDO investments, the Company utilizes the same tools as for RMBS investments discussed below, aggregating the bond level cash flows to the CDO investment level. If the present value of cash flows is less than the Company's amortized cost for the security, the difference is recorded as an OTTI loss.

RMBS investments are evaluated for OTTI using several quantitative tools. Loan level data are obtained and analyzed in a model that produces prepayment, default, and severity vectors. The model utilizes macro inputs, including housing price assumptions and interest rates. The vector outputs are used as inputs to a third-party cash flow model, which considers deal waterfall dynamics and structural features, to generate cash flows for an RMBS investment. The expected cash flows of the security are then discounted at the interest rate used to recognize interest income of the security to arrive at a present value amount. If the present value of the cash flows is less than the Company's amortized cost for the investment, the difference is recorded as an OTTI loss.

Corporate obligation investments are evaluated for OTTI using credit analysis techniques. The Company's analysis includes a detailed review of a number of quantitative and qualitative factors impacting the value of an individual security. These factors include the interest rate of the security (fixed or floating), the security's current market spread, any collateral supporting the security, the security's position in the issuer's capital structure, and credit rating upgrades or downgrades. Additionally, these factors include an assessment of various issuer-related credit metrics including market capitalization, earnings, cash flow, capitalization, interest coverage, leverage, liquidity, management and a third-party quantitative default probability model. The Company's analysis is augmented by comparing market prices for similar securities of other issuers in the same sector, as well as any recent corporate or government actions that may impact the ultimate return of principal. If the Company determines that, after considering these factors, a principal default is projected, a recovery analysis is performed using the above data. If the Company's estimated recovery value for the security is less than its amortized cost, the difference is recorded as an OTTI loss.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)**

For the nine months ended September 30, 2012, the credit losses recognized in earnings were related to RMBS and CDOs. The following table presents a summary of the significant inputs considered in determining the measurement of the credit losses on securities in which a portion of the impairment is included in AOCI:

	<b>Nine Months Ended September 30, 2012</b>
<b>Asset-backed Securities</b>	
Expected size of losses <sup>(1)</sup> :	
Range <sup>(2)</sup>	12.13% to 97.70%
Weighted average <sup>(3)</sup>	88.48%
Current subordination levels <sup>(4)</sup> :	
Range <sup>(2)</sup>	0.00% to 0.00%
Weighted average <sup>(3)</sup>	0.00%
Prepayment speed (annual constant prepayment rate) <sup>(5)</sup> :	
Range <sup>(2)</sup>	0.00% to 30.91%
Weighted average <sup>(3)</sup>	12.16%

(1) - Represents future expected credit losses on impaired assets expressed as a percentage of total outstanding balance.

(2) - Represents the range of inputs/assumptions based upon the individual securities within each category.

(3) - Calculated by weighting the relevant input/assumption for each individual security by the outstanding notional of the security.

(4) - Represents current level of credit protection (subordination) for the securities, expressed as a percentage of the balance of the collateral group backing the bond.

(5) - Values represent high and low points of lifetime vectors of constant prepayment rates.

***Determination of Credit Loss Guaranteed by the Company and Other Third-Party Guarantors***

The Company does not record OTTI related to credit concerns about issuers of securities insured by MBIA Corp. and National since investors in these securities, including MBIA, are guaranteed payment of principal and interest when due by MBIA. Securities insured by the Company, whether or not owned by the Company, are evaluated for impairment as part of its insurance surveillance process and, therefore, losses on securities insured by the Company are recorded in accordance with its loss reserving policy. Refer to Note 2: Significant Accounting Policies in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 for information about the Company's loss reserving policy and Note 5: Loss and Loss Adjustment Expense Reserves for information about loss reserves.

In considering cash expected to be provided from other third-party financial guarantors, the Company assesses the financial guarantor's ability to make claim payments under a variety of scenarios that test the guarantor's ultimate claims paying ability. The weighted average outcome of these scenarios, combined with the cash flows provided by the insured security, are used to determine the recoverability of the Company's amortized cost.



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The following table provides information about securities held by the Company as of September 30, 2013 that were in an unrealized loss position and insured by a financial guarantor, along with the amount of insurance loss reserves corresponding to the par amount owned by the Company:

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)**

<b>In millions</b>	<b>Fair Value</b>	<b>Unrealized Loss</b>	<b>Insurance Loss Reserve <sup>(2)</sup></b>
<b>Asset-backed:</b>			
MBIA <sup>(1)</sup>	\$ 148	\$ (58)	\$ 15
Other	9	(5)	-
Total asset-backed	157	(63)	15
<b>Mortgage-backed:</b>			
MBIA <sup>(1)</sup>	5	-	-
Other	15	-	-
Total mortgage-backed	20	-	-
<b>Corporate obligations:</b>			
Other	6	(2)	-
Total corporate obligations	6	(2)	-
<b>Other:</b>			
MBIA <sup>(1)</sup>	104	(6)	-
Other	19	-	-
Total other	123	(6)	-
Total	\$ 306	\$ (71)	\$ 15

(1) - Includes investments insured by MBIA Corp. and National.

(2) - Insurance loss reserve estimates are based on the proportion of par value owned to the total amount of par value insured.

***Credit Loss Rollforward***

The portion of certain OTTI losses on fixed-maturity securities that does not represent credit losses is recognized in AOCI. For these impairments, the net amount recognized in earnings represents the difference between the amortized cost of the security and the net present value of its projected future discounted cash flows prior to impairment. Any remaining difference between the fair value and amortized cost is recognized in AOCI. The following table presents the amount of credit loss impairments recognized in earnings on fixed-maturity securities held by MBIA as of the dates indicated, for which a portion of the OTTI losses was recognized in AOCI, and the corresponding changes in such amounts.

<b>In millions</b>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
<b>Credit Losses Recognized in Earnings Related to</b>	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>

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### Other-Than-Temporary Impairments

Beginning balance	\$	186	\$	269	\$	197	\$	341
Additions for credit loss impairments recognized in the current period on securities previously impaired		-		5		-		8
Reductions for credit loss impairments previously recognized on securities sold during the period		(4)		(2)		(14)		(18)
Reductions for credit loss impairments previously recognized on securities impaired to fair value during the period <sup>(1)</sup>		-		(52)		-		(111)
Reductions for increases in cash flows expected to be collected over the remaining life of the security		(4)		-		(5)		-
Ending balance	\$	178	\$	220	\$	178	\$	220

(1) - Represents circumstances where the Company determined in the current period that it intends to sell the security or it is more likely than not that it will be required to sell the security before recovery of the security's amortized cost.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 7: Investments (continued)*****Sales of Available-For-Sale Investments***

Gross realized gains and losses are recorded within Net gains (losses) on financial instruments at fair value and foreign exchange on the Company's consolidated statements of operations. The proceeds and gross realized gains and losses from sales of AFS investments for the three and nine months ended September 30, 2013 and 2012 are as follows:

In millions	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Proceeds from sales	\$ 695	\$ 1,163	\$ 3,009	\$ 5,697
Gross realized gains	\$ 4	\$ 42	\$ 52	\$ 100
Gross realized losses	\$ (15)	\$ (6)	\$ (25)	\$ (101)

**Note 8: Derivative Instruments*****Overview***

MBIA has entered into derivative instruments through its financial guarantee of CDS and for purposes of hedging risks associated with existing assets and liabilities and forecasted transactions. The Company accounts for derivative instruments in accordance with the accounting principles for derivative and hedging activities, which requires that all such instruments be recorded on the balance sheet at fair value. Refer to Note 6: Fair Value of Financial Instruments for the method of determining the fair value of derivative instruments.

***U.S. Public Finance Insurance***

The Company's derivative exposure within its U.S. public finance insurance operations primarily consists of insured interest rate and inflation-linked swaps related to insured U.S. public finance debt issues. These derivatives do not qualify for the financial guarantee scope exception. The Company has also purchased certain investments containing embedded derivatives. All derivatives are recorded at fair value on the Company's consolidated balance sheets with the changes in fair value recorded on the Company's consolidated statements of operations within Unrealized gains (losses) on insured derivatives, for the insured derivatives, or Net gains (losses) on financial instruments at fair value and foreign exchange for the embedded derivatives.

***Structured Finance and International Insurance***

The Company entered into derivative instruments that it viewed as an extension of its core financial guarantee business but which do not qualify for the financial guarantee scope exception and, therefore, must be recorded at fair value on the balance sheet. These insured CDS contracts, primarily referencing corporate, asset-backed, residential mortgage-backed, commercial mortgage-backed, CRE loans and CDO securities, are intended to be held for the entire term of the contract absent a negotiated settlement with the counterparty.

Changes in the fair value of derivatives, excluding insured derivatives, are recorded each period in current earnings within Net gains (losses) on financial instruments at fair value and foreign exchange. Changes in the fair value of insured derivatives are recorded each period in current earnings within Net change in fair value of insured derivatives. The net change in the fair value of the Company's insured derivatives has two primary components: (i) realized gains (losses) and other settlements on insured derivatives and (ii) unrealized gains (losses) on insured derivatives. Realized gains (losses) and other settlements on insured derivatives include (i) premiums received and receivable on sold CDS contracts, (ii) premiums paid and payable to reinsurers in respect to CDS contracts, (iii) net amounts received or paid on reinsurance

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commutations, (iv) losses paid and payable to CDS contract counterparties due to the occurrence of a credit event or settlement agreement, (v) losses recovered and recoverable on purchased CDS contracts due to the occurrence of a credit event or settlement agreement and (vi) fees relating to CDS contracts. The Unrealized gains (losses) on insured derivatives include all other changes in fair value of the insured derivative contracts.

In certain instances, the Company's structured finance and international insurance business purchased or issued securities that contain embedded derivatives. In accordance with the accounting guidance for derivative instruments and hedging activities, the balance sheet location of the Company's embedded derivative instruments is determined by the location of the related security.

### *Variable Interest Entities*

VIEs consolidated by the Company have entered into derivative instruments primarily consisting of interest rate swaps. Interest rate swaps are entered into to mitigate the risks associated with fluctuations in interest rates or fair values of certain contracts.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 8: Derivative Instruments (continued)***Asset/Liability Products*

The Company's asset/liability products business has entered into derivative instruments primarily consisting of interest rate swaps, and cross currency swaps. Interest rate swaps are entered into to hedge the risks associated with fluctuations in interest rates or fair values of certain contracts. Cross currency swaps are entered into to hedge the variability in cash flows resulting from fluctuations in foreign currency rates.

In certain instances, the Company's asset/liability products business purchased or issued securities that contain embedded derivatives. In accordance with the accounting guidance for derivative instruments and hedging activities, the balance sheet location of the Company's embedded derivative instruments is determined by the location of the related security.

Changes in the fair value of the Company's asset/liability products business derivatives are recorded on the Company's consolidated statements of operations within Net gains (losses) on financial instruments at fair value and foreign exchange.

*Credit Derivatives Sold*

The following tables present information about credit derivatives sold by the Company's insurance operations that were outstanding as of September 30, 2013 and December 31, 2012. Credit ratings represent the lower of underlying ratings assigned to the collateral by Moody's, S&P or MBIA.

\$ in millions		As of September 30, 2013						
		Notional Value						Fair Value Asset (Liability)
Credit Derivatives Sold	Weighted Average Remaining Expected Maturity	AAA	AA	A	BBB	Below Investment Grade	Total Notional	
Insured credit default swaps	2.7 Years	\$ 7,412	\$ 3,150	\$ 1,705	\$ 7,419	\$ 6,085	\$ 25,771	\$ (1,355)
Insured swaps	19.1 Years	-	77	3,694	1,592	-	5,363	(7)
All others	28.3 Years	-	-	-	-	36	36	(8)
Total notional		\$ 7,412	\$ 3,227	\$ 5,399	\$ 9,011	\$ 6,121	\$ 31,170	
Total fair value		\$ (3)	\$ -	\$ (6)	\$ (386)	\$ (975)		\$ (1,370)

\$ in millions		As of December 31, 2012						
		Notional Value						Fair Value Asset (Liability)
Credit Derivatives Sold	Weighted Average Remaining Expected	AAA	AA	A	BBB	Below Investment Grade	Total Notional	

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	<b>Maturity</b>							
Insured credit default swaps	5.1 Years	\$ 10,457	\$ 5,862	\$ 5,253	\$ 11,571	\$ 13,859	\$ 47,002	\$ (2,858)
Insured swaps	19.4 Years	-	103	3,661	1,982	71	5,817	(8)
All others	1.8 Years	-	-	-	-	195	195	(68)
Total notional		\$ 10,457	\$ 5,965	\$ 8,914	\$ 13,553	\$ 14,125	\$ 53,014	
Total fair value		\$ (7)	\$ (70)	\$ (72)	\$ (732)	\$ (2,053)		\$ (2,934)

Internal credit ratings assigned by MBIA on the underlying collateral are derived by the Company's surveillance group. In assigning an internal rating, current status reports from issuers and trustees, as well as publicly available transaction-specific information, are reviewed. Also, where appropriate, cash flow analyses and collateral valuations are considered. The maximum potential amount of future payments (undiscounted) on CDS contracts are estimated as the notional value plus any additional debt service costs, such as interest or other amounts owing on CDS contracts. The maximum amount of future payments that MBIA may be required to make under these guarantees as of September 30, 2013 is \$26.4 billion. This amount is net of \$67 million of insured derivatives ceded under reinsurance agreements in which MBIA economically hedges a portion of the credit and market risk associated with its insured derivatives and offsetting agreements with a counterparty. The maximum potential amount of future payments (undiscounted) on insured swaps are estimated as the notional value of such contracts.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 8: Derivative Instruments (continued)**

MBIA may hold recourse provisions with third parties in derivative instruments through both reinsurance and subrogation rights. MBIA's reinsurance arrangements provide that in the event MBIA pays a claim under a guarantee of a derivative contract, MBIA has the right to collect amounts from any reinsurers that have reinsured the guarantee on either a proportional or non-proportional basis, depending upon the underlying reinsurance agreement. MBIA may also have recourse through subrogation rights whereby if MBIA makes a claim payment, it is entitled to any rights of the insured counterparty, including the right to any assets held as collateral.

***Counterparty Credit Risk***

The Company manages counterparty credit risk on an individual counterparty basis through master netting agreements covering derivative instruments in the asset/liability products segment. There are no master netting agreements in the structured finance and international insurance or the U.S. public finance insurance segments. The master netting agreements in the asset/liability products segment allow the Company to contractually net amounts due from a counterparty with those amounts due to such counterparty when certain triggering events occur. The Company only executes swaps under master netting agreements, which typically contain mutual credit downgrade provisions that generally provide the ability to require assignment or termination in the event either MBIA or the counterparty is downgraded below a specified credit rating.

Under these arrangements, the Company may receive or provide U.S. Treasury and other highly rated securities or cash to secure counterparties exposure to the Company or its exposure to counterparties, respectively. Such collateral is available to the holder to pay for replacing the counterparty in the event that the counterparty defaults. As of September 30, 2013, the Company did not hold cash collateral to derivative counterparties but posted cash collateral to derivative counterparties of \$219 million. Of this amount, \$143 million is netted within Derivative liabilities, \$16 million is included within Other liabilities as cash collateral netted against accrued interest on derivative liabilities and an additional \$60 million is included in Other assets on the Company's consolidated balance sheets. As of December 31, 2012, the Company did not hold cash collateral to derivative counterparties but posted cash collateral to derivative counterparties of \$285 million. Of this amount, \$203 million is netted within Derivative liabilities, \$16 million is included within Other liabilities as cash collateral netted against accrued interest on derivative liabilities and an additional \$66 million is included in Other assets on the Company's consolidated balance sheets. As of September 30, 2013 and December 31, 2012, the Company did not post securities to derivative counterparties.

As of September 30, 2013 and December 31, 2012, the fair value on one Credit Support Annex (CSA) was \$4 million. This CSA governs collateral posting requirements between MBIA and its derivative counterparties. The Company did not receive collateral due to the Company's credit rating, which was below the CSA minimum credit ratings level for holding counterparty collateral. As of September 30, 2013 and December 31, 2012, the counterparty was rated A2 by Moody's and A by S&P.

***Financial Statement Presentation***

The fair value of amounts recognized for eligible derivative contracts executed with the same counterparty under a master netting agreement, including any cash collateral that may have been received or posted by the Company, is presented on a net basis in accordance with accounting guidance for the offsetting of fair value amounts related to derivative instruments. Insured CDSs and insured swaps are not subject to master netting agreements. VIE derivative assets and liabilities are not presented net of any master netting agreements.

As of September 30, 2013, the total fair value of the Company's derivative assets, after counterparty netting of \$53 million, was \$13 million, of which \$4 million was reported within Other assets on the Company's consolidated balance sheets. Embedded derivatives of \$9 million were reported within Medium-term notes on the Company's consolidated balance sheets.

As of September 30, 2013, the total fair value of the Company's derivative liabilities, after counterparty netting of \$53 million and cash collateral posted by the Company of \$143 million was \$1.4 billion, which was reported within Derivative liabilities and Derivative liabilities presented under Liabilities of consolidated variable interest entities on the Company's consolidated balance sheets. Embedded derivatives of \$16 million



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were reported within Medium-term notes on the Company's consolidated balance sheets.

Counterparty netting of derivative assets and liabilities offsets balances in Interest rate swaps and Currency swaps in the table below.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 8: Derivative Instruments (continued)**

The following table presents the total fair value of the Company's derivative assets and liabilities by instrument and balance sheet location, before counterparty netting and posting of cash collateral, as of September 30, 2013:

In millions	Derivative Assets <sup>(1)</sup>			Derivative Liabilities <sup>(1)</sup>	
	Notional Amount Outstanding	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivative Instruments					
Not designated as hedging instruments:					
Insured credit default swaps	\$ 25,771	Other assets	\$ -	Derivative liabilities	\$ (1,355)
Insured swaps	5,363	Other assets	-	Derivative liabilities	(7)
Interest rate swaps	1,575	Other assets	57	Derivative liabilities	(195)
Interest rate swaps-embedded	490	Medium-term notes	9	Medium-term notes	(16)
Currency swaps	20	Other assets	-	Derivative liabilities	(1)
Currency swaps-VIE	102	Other assets-VIE	-	Derivative liabilities-VIE	(15)
All other	36	Other assets	-	Derivative liabilities	(8)
All other-VIE	280	Other assets-VIE	-	Derivative liabilities-VIE	-
All other-embedded	10	Other investments	-	Other investments	-
Total non-designated derivatives	\$ 33,647		\$ 66		\$ (1,597)

(1) - In accordance with the accounting guidance for derivative instruments and hedging activities, the balance sheet location of the Company's embedded derivative instruments is determined by the location of the related host contract.

As of December 31, 2012, the total fair value of the Company's derivative assets, after counterparty netting of \$90 million, was \$12 million, of which \$4 million was reported within Other assets and Other assets presented under Assets of consolidated variable interest entities on the Company's consolidated balance sheets. Embedded derivatives of \$8 million were reported within Medium-term notes on the Company's consolidated balance sheets.

As of December 31, 2012, the total fair value of the Company's derivative liabilities, after counterparty netting of \$90 million and cash collateral posted by the Company of \$203 million, was \$3.1 billion which was reported within Derivative liabilities and Derivative liabilities presented under Liabilities of consolidated variable interest entities on the Company's consolidated balance sheets. Embedded derivatives of \$36 million were reported within Medium-term notes and Other investments on the Company's consolidated balance sheets.

Counterparty netting of derivative assets and liabilities offsets balances in Interest rate swaps and Currency swaps in the table below.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 8: Derivative Instruments (continued)**

The following table presents the total fair value of the Company's derivative assets and liabilities by instrument and balance sheet location, before counterparty netting and posting of cash collateral, as of December 31, 2012:

In millions	Notional Amount Outstanding	Derivative Assets <sup>(1)</sup>		Derivative Liabilities <sup>(1)</sup>	
		Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
<b>Derivative Instruments</b>					
Not designated as hedging instruments:					
Insured credit default swaps	\$ 47,320	Other assets	\$ -	Derivative liabilities	\$ (2,858)
Insured swaps	5,817	Other assets	-	Derivative liabilities	(8)
Non-insured credit default swaps	10	Other assets	-	Derivative liabilities	-
Interest rate swaps	1,637	Other assets	94	Derivative liabilities	(290)
Interest rate swaps-VIE	2,728	Other assets-VIE	-	Derivative liabilities-VIE	(141)
Interest rate swaps-embedded	483	Medium-term notes	8	Medium-term notes	(35)
Currency swaps	40	Other assets	-	Derivative liabilities	(3)
Currency swaps-VIE	110	Other assets-VIE	-	Derivative liabilities-VIE	(21)
All other	195	Other assets	-	Derivative liabilities	(68)
All other-VIE	280	Other assets-VIE	-	Derivative liabilities-VIE	-
All other-embedded	20	Other investments	-	Other investments	(1)
<b>Total non-designated derivatives</b>	<b>\$ 58,640</b>		<b>\$ 102</b>		<b>\$ (3,425)</b>

(1) - In accordance with the accounting guidance for derivative instruments and hedging activities, the balance sheet location of the Company's embedded derivative instruments is determined by the location of the related host contract.

The following table presents the effect of derivative instruments on the consolidated statements of operations for the three months ended September 30, 2013:

In millions		
Derivatives Not Designated as		Net Gain (Loss)
Hedging Instruments	Location of Gain (Loss) Recognized in Income on Derivative	Recognized in Income
Insured credit default swaps	Unrealized gains (losses) on insured derivatives	\$ 287
Insured credit default swaps	Realized gains (losses) and other settlements on insured derivatives	(28)
Interest rate swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	17
Interest rate swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	2
Currency swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	(1)
All other	Unrealized gains (losses) on insured derivatives	(2)

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Total	\$	275
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The following tables present the effect of derivative instruments on the consolidated statements of operations for the three months ended September 30, 2012:

**In millions**

	Location of Gain (Loss)	Gain (Loss)	Gain (Loss)	Net Gain (Loss)
Derivatives in Fair Value	Recognized in Income on	Recognized in	Recognized in	Recognized
Hedging Relationships	Derivative	Income on	Income on	in
		Derivative	Hedged	Income
			Item	
Interest rate swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	\$ (12)	\$ 12	\$ -
Total		\$ (12)	\$ 12	\$ -

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 8: Derivative Instruments (continued)****In millions**

<b>Derivatives Not Designated as</b>		<b>Net Gain (Loss)</b>
<b>Hedging Instruments</b>	<b>Location of Gain (Loss) Recognized in Income on Derivative</b>	<b>Recognized in Income</b>
Insured credit default swaps	Unrealized gains (losses) on insured derivatives	\$ (40)
Insured credit default swaps	Realized gains (losses) and other settlements on insured derivatives	12
Interest rate swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	(26)
Interest rate swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	8
Currency swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	1
Currency swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	(2)
All other	Unrealized gains (losses) on insured derivatives	7
Total		\$ (40)

The following table presents the effect of derivative instruments on the consolidated statements of operations for the nine months ended September 30, 2013:

**In millions**

<b>Derivatives Not Designated as</b>		<b>Net Gain (Loss)</b>
<b>Hedging Instruments</b>	<b>Location of Gain (Loss) Recognized in Income on Derivative</b>	<b>Recognized in Income</b>
Insured credit default swaps	Unrealized gains (losses) on insured derivatives	\$ 1,502
Insured credit default swaps	Realized gains (losses) and other settlements on insured derivatives	(1,548)
Interest rate swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	58
Interest rate swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	17
Currency swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	1
Currency swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	6
All other	Unrealized gains (losses) on insured derivatives	60
Total		\$ 96

The following tables present the effect of derivative instruments on the consolidated statements of operations for the nine months ended September 30, 2012:

**In millions**

<b>Derivatives in Fair Value</b>	<b>Location of Gain (Loss)</b>	<b>Gain (Loss)</b>	<b>Gain (Loss)</b>	<b>Net Gain (Loss)</b>
<b>Hedging Relationships</b>	<b>Recognized in Income on</b>	<b>Recognized in Income on</b>	<b>Recognized in Income on</b>	<b>Recognized in Income</b>

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	Derivative	Derivative	Hedged Item	
Interest rate swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	\$ 25	\$ (25)	\$ -
Interest rate swaps	Interest income (expense)	-	-	(3)
Total		\$ 25	\$ (25)	\$ (3)

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 8: Derivative Instruments (continued)**

In millions

Derivatives Not Designated as

Hedging Instruments	Location of Gain (Loss) Recognized in Income on Derivative	Net Gain(Loss) Recognized in Income
Insured credit default swaps	Unrealized gains (losses) on insured derivatives	\$ 1,463
Insured credit default swaps	Realized gains (losses) and other settlements on insured derivatives	(420)
Non-insured credit default swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	(1)
Non-insured credit default swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	(1)
Interest rate swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	(76)
Interest rate swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	39
Currency swaps	Net gains (losses) on financial instruments at fair value and foreign exchange	1
Currency swaps-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	(5)
All other	Unrealized gains (losses) on insured derivatives	10
All other	Net gains (losses) on financial instruments at fair value and foreign exchange	11
All other-VIE	Net gains (losses) on financial instruments at fair value and foreign exchange-VIE	(2)
Total		\$ 1,019

**Note 9: Debt**

The Company has disclosed its debt in Note 10: Debt in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012. The following debt discussion provides an update to the Company's Annual Report on Form 10-K.

**Long-Term Debt**

The Company's long-term debt consists of surplus notes and MBIA Inc. corporate debt. As of September 30, 2013, accrued interest on the Company's long-term debt was reported within Long-term debt on the Company's consolidated balance sheets. Prior to September 30, 2013, the accrued interest on long-term debt was included in Other liabilities on the Company's consolidated balance sheets. The accrued interest on long-term debt has been reclassified in the prior year's financial statements to conform to the current presentation. This reclassification had no impact on total revenues, expenses, assets, liabilities, shareholders' equity, operating cash flows, investing cash flows, or financing cash flows for all periods presented.

**Surplus Notes**

As of September 30, 2013 and December 31, 2012, there was \$940 million of principal outstanding related to surplus notes. As of September 30, 2013 and December 31, 2012, accrued interest related to these surplus notes was \$143 million and \$61 million, respectively.

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Interest and principal payments on the 14% Fixed to Floating Rate Surplus Notes due 2033 are subject to prior approval by the Superintendent of the NYSDFS. From the January 15, 2013 interest payment to the present, MBIA Insurance Corporation's requests for approval of the note interest payments have been denied by the NYSDFS. MBIA Insurance Corporation provided notice to the Fiscal Agent that it has not made a scheduled interest payment. The deferred interest payment will become due on the first business day on or after which MBIA Insurance Corporation obtains approval to make such payment. No interest will accrue on the deferred interest.

### *MBIA Inc. Corporate Debt*

As of September 30, 2013 and December 31, 2012, there was \$584 million and \$723 million, respectively, of principal outstanding related to MBIA Inc. corporate debt. As of September 30, 2013 and December 31, 2012, accrued interest related to MBIA Inc. corporate debt was \$10 million and \$9 million, respectively.

In connection with the BofA Settlement Agreement in May of 2013, MBIA Corp. received \$136 million principal amount of the 5.70% Senior Notes due 2034 as consideration for the settlement. These notes were subsequently transferred to National. On a consolidated basis, receipt of these notes by the Company reduced its outstanding debt.

### *Medium-Term Note Obligations*

During the nine months ended September 30, 2013, the Company redeemed \$486 million par value outstanding of MTNs issued by the Company's conduit segment at a cost of 100% of par value. The Company also repurchased approximately \$80 million par value outstanding of MBIA Global Funding, LLC ( GFL ) MTNs issued by the Company's asset/liability segment at a weighted average cost of approximately 92% of par value.



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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

### **Note 9: Debt (continued)**

#### ***Other Borrowing Arrangements***

##### **Blue Ridge Secured Loan**

In connection with the BofA Settlement Agreement in May of 2013, MBIA Insurance Corporation and Blue Ridge entered into the Blue Ridge Secured Loan, pursuant to which Blue Ridge agreed to make revolving loans to MBIA Insurance Corporation in an aggregate of up to \$500 million. The following is a summary of the material terms of the Loan Agreement, as amended by Amendment No. 1 entered into in June of 2013. This summary is not complete and is subject to the full text of the document described below.

During the third quarter of 2013, MBIA Insurance Corporation borrowed \$50 million under the Blue Ridge Secured Loan. MBIA Insurance Corporation elected the LIBOR Loans interest rate option and the average interest rate for the three months ended September 30, 2013 was 7.76%. Accrued interest expense for the Blue Ridge Secured Loan is included within Other liabilities on the Company's consolidated balance sheets.

##### ***Use of Proceeds***

The proceeds of the Blue Ridge Secured Loan can be used for general corporate purposes. Once the Blue Ridge Secured Loan amount outstanding exceeds \$50 million, the proceeds must be used for the purpose of meeting ordinary course liquidity requirements expected to arise during the 30 days following such borrowing.

##### ***Conditions to Borrowings***

Blue Ridge's obligation to make loans is subject to usual and customary conditions precedent, including that on the date of the borrowing (i) no default is continuing or would occur as a result of that borrowing and (ii) the representations and warranties specified in the Blue Ridge Secured Loan agreement are true and accurate in all material respects.

##### ***Security***

The Loans are secured by a pledge of collateral consisting of the following: (i) MBIA Insurance Corporation's right to receive put-back recoveries related to ineligible mortgage loans included in its insured RMBS transactions; (ii) MBIA Insurance Corporation's future recoveries on defaulted insured RMBS transactions resulting from expected excess spread generated by performing loans in such transactions; (iii) MBIA Insurance Corporation's future installment premiums; and (iv) 65% of the voting capital stock of MBIA Corp.'s equity interest in MBIA UK (Holdings) Limited (the collateral described in clauses (ii) and (iii) above, the ( Other Prepayment Collateral ). Under the Blue Ridge Secured Loan, the value of the collateral described in clauses (i) through (iii) above, must at all times be greater than \$1.0 billion. As of September 30, 2013, the value of the collateral was approximately \$2.5 billion.

##### ***Interest Rate and Fees***

Borrowings under the Blue Ridge Secured Loan have a variable interest rate, at MBIA Insurance Corporation's option based on either: (i) the adjusted LIBOR plus an applicable margin ( LIBOR Loans ), or (ii) the highest between (a) Bank of America's prime rate and (b) the sum of the federal funds effective rate plus 0.5% and (c) the adjusted LIBOR plus 1.00%, plus an applicable margin ( Base Rate Loans ). The applicable margin for the LIBOR Loans and the Base Rate Loans is 7.50% and 6.50%, respectively. With respect to any available but undrawn amounts under the Blue Ridge Secured Loan, MBIA Insurance Corporation is obligated to pay a commitment fee on such undrawn amounts of 2.00% per annum. The amount of the commitment fee and interest expense for the nine months ended September 30, 2013 was \$4 million.



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**MBIA Inc. and Subsidiaries**

**Notes to Consolidated Financial Statements (Unaudited)**

**Note 9: Debt (continued)**

*Scheduled Repayment*

The maturity date of the Blue Ridge Secured Loan is three years from the closing date, at which time any then outstanding loans will be due and payable.

*Mandatory Prepayments*

Loans are required to be prepaid (and Blue Ridge's commitments reduced) in an amount equal to the following: (i) 100% of the proceeds of any put-back recoveries and (ii) on and after the first anniversary of the closing date, from the proceeds of any Other Prepayment Collateral in an amount equal to (x) from the first anniversary of the closing date to the second anniversary of the closing date, 50% of such proceeds and (y) from the second anniversary of the closing date to the maturity date, 100% of such proceeds. In addition, loans must be prepaid (and Blue Ridge's commitments reduced) in an amount equal to 100% of the proceeds of certain disposals of assets to the extent exceeding \$1 million in aggregate for all such disposals. Finally, loans must be prepaid (but without any commitment reduction) to the extent the proceeds of any borrowing that is a liquidity borrowing are not in fact used for such purposes and have not otherwise been used to repay loans within the required 30-day period.

*Representations and Warranties*

The Blue Ridge Secured Loan contains certain customary representations and warranties for loan facilities of this type, which are given on the closing date and at each borrowing under the Blue Ridge Secured Loan agreement, including with respect to organization of MBIA Insurance Corporation, power of authority, enforceability of the loan documents, receipt of any necessary governmental approvals, financial condition and solvency, and compliance with laws.

*Covenants*

The Blue Ridge Secured Loan contains certain affirmative, negative and financial covenants, which are customary for loan facilities of this type in relation to, among other matters, delivery of financial statements, notice of material events, existence and conduct of business, payment of taxes and other obligations, maintenance of books and records, compliance with all material laws, and maintenance of insurance, and includes a requirement that MBIA Insurance Corporation maintain at least \$750 million of statutory capital (defined as policyholders' surplus plus contingency reserves).

In addition, MBIA Insurance Corporation may not, without Blue Ridge's consent, consummate any amendments, compromises or commutations with respect to insurance obligations and settlements of litigation to the extent (x) that payments made in respect of such remediation efforts subsequent to June 28, 2013 exceed \$260 million in the aggregate, (y) after giving effect thereto and to any borrowings of loans in connection therewith, the aggregate principal amount of loans outstanding would exceed \$200 million or (z) after giving effect thereto, all remediation efforts taken as a whole since the closing date, would, cumulatively, have reduced MBIA Insurance Corporation's statutory capital by \$100 million or more.

In addition, MBIA Insurance Corporation may not prepay, redeem, purchase, defease or otherwise satisfy prior to the scheduled maturity thereof in any manner, or make any payment of principal, interest or fees or any other payment on, any of its indebtedness (including the Surplus Notes), except for payments of the loans under the Blue Ridge Secured Loan agreement and except for certain refinancings and refundings of its indebtedness.

*Change of Control*

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MBIA Insurance Corporation may be required to prepay all amounts outstanding under the Blue Ridge Secured Loan agreement upon the occurrence of a change of control.

### *Events of Default*

The Blue Ridge Secured Loan agreement contains certain events of default which are customary for loan facilities of this type (and with customary cure periods), including failure to pay principal, interest or fees on the loans, misrepresentation, failure to observe covenants or conditions, failure to pay other material indebtedness, insolvency and bankruptcy matters, and unlawfulness or invalidity of the loan documents.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 10: Income Taxes**

The Company's income taxes and the related effective tax rates for the three and nine months ended September 30, 2013 and 2012 are as follows:

In millions	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Income (loss) before income taxes	\$ 171	\$ (57)	\$ 122	\$ 759
Provision (benefit) for income taxes	\$ 39	\$ (64)	\$ 4	\$ 161
Effective tax rate	22.8%	112.3%	3.3%	21.2%

For the nine months ended September 30, 2013, the Company's effective tax rate applied to its pre-tax income was lower than the U.S. statutory tax rate primarily as a result of the decrease in the valuation allowance against its deferred tax asset.

For the nine months ended September 30, 2012, the Company's effective tax rate applied to its pre-tax income was lower than the U.S. statutory tax rate as a result of the decrease in the valuation allowance, the release of a portion of the reserve for uncertain tax benefits and the benefit of tax-exempt interest income from investments.

For interim reporting purposes, the Company has calculated its effective tax rate for the full year of 2013 by adjusting annual forecasted pre-tax income for mark-to-market income, fair value adjustments, capital gains/losses, and other adjustments, when projecting its full year effective tax rate. The Company has accounted for these items at the federal applicable tax rate after applying the projected full year effective tax rate to actual nine-month results before discrete items.

***Deferred Tax Asset, Net of Valuation Allowance***

The Company establishes a valuation allowance against its deferred tax asset when it is more likely than not that all or a portion of the deferred tax asset will not be realized. All evidence, both positive and negative, needs to be identified and considered in making the determination. Future realization of the existing deferred tax asset ultimately depends, in part, on the existence of sufficient taxable income of appropriate character (for example, ordinary income versus capital gains) within the carryforward period available under the tax law.

As of September 30, 2013, the Company reported a net deferred tax asset of \$1.2 billion. The \$1.2 billion net deferred tax asset is net of a \$94 million valuation allowance. As of September 30, 2013, the Company had a valuation allowance against a portion of the deferred tax asset related to losses from asset impairments as these losses are considered capital losses, have a five-year carryforward period, once recognized, and can only offset capital gain income. The September 30, 2013 valuation allowance reflects a decrease of \$52 million from the December 31, 2012 valuation allowance of \$146 million. The decrease in the valuation allowance for the nine months ended September 30, 2013 was primarily due to the generation of capital gain income from the termination of certain contracts.

The Company has concluded that it is more likely than not that its net deferred tax asset will be realized. In its conclusion, the Company considered the following evidence (both positive and negative):

Due to the long-tail nature of the financial guarantee business, MBIA Inc.'s insurance subsidiaries, without regard to any new business, will have a steady stream of scheduled premium earnings with respect to the existing insured portfolio. Additionally, MBIA Corp.'s announcement in February 2008 of a suspension in writing new structured finance transactions and a permanent cessation with respect to insuring new CDS contracts, except in transactions related to the reduction of existing derivative exposure, would not have an impact on the expected earnings related to the existing insured portfolio.

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The Company performed taxable income projections over a twenty-year period to determine whether it will have sufficient income to offset its deferred tax asset that will generate future ordinary deductions. In this analysis, the Company concluded that premium earnings, including projected new business at National, combined with investment income, less deductible expenses, will be sufficient to recover its net deferred tax asset. The Company's taxable income projections used to assess the recoverability of its deferred tax asset include an estimate of future loss and LAE equal to the present value discount of loss reserves already recognized on the balance sheet and an estimate of LAE which is generally insignificant. The Company does not assume additional losses, with the exception of the accretion of its existing present value loss reserves, because the Company establishes case basis reserves on a present value basis based on an estimate of probable losses on specifically identified credits that have defaulted or are expected to default.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 10: Income Taxes (continued)**

While the lack of strong credit ratings assigned by the rating agencies have significantly adversely impacted the Company's ability to write new insurance business, these ratings did not have a material impact on earnings from the existing insured portfolio, which the Company believes will be sufficient to absorb losses in the event that the cumulative unrealized losses become fully impaired.

With respect to installment policies, the Company generally does not have an automatic cancellation provision solely in connection with ratings downgrades. With regard to upfront policies, to the extent that the issuer chooses to terminate a policy, any unearned premium reserve with respect to that policy will be accelerated into earnings (i.e. refundings).

After reviewing all of the evidence available, both positive and negative, the Company believes that it has appropriately valued the recoverability of its deferred tax assets, net of the valuation allowance, as of September 30, 2013. The Company continues to assess the adequacy of its valuation allowance as additional evidence becomes available. The Company's recent financial results have been volatile which has impacted management's ability to accurately project future taxable income. Continued volatility or losses beyond those projected may cause the Company to conclude that certain of the deferred tax assets within the total deferred tax assets of \$1.2 billion as of September 30, 2013 may not be realizable. The Company performs an analysis every quarter to review its conclusion as to the ability to realize the deferred tax asset.

***Accounting for Uncertainty in Income Taxes***

The Company's policy is to record and disclose any change in UTB and related interest and/or penalties to income tax in the consolidated statements of operations.

**In millions**

Unrecognized tax benefit as of December 31, 2012	\$ 47
The gross amount of the increase/(decrease) in the UTB as a result of tax positions taken:	
During a prior year	-
During the current year	11
The amounts of decreases in the UTB related to settlements with taxing authorities	-
The reduction in the UTB as a result of the applicable statute of limitations	-
Unrecognized tax benefit as of September 30, 2013	\$ 58

MBIA's major tax jurisdictions include the U.S. and the U.K. MBIA and its U.S. subsidiaries file a U.S. consolidated federal income tax return.

The U.K. tax authorities are currently auditing tax years 2005 through 2010. On June 5, 2013, the Company met with the HM Revenue & Customs (HMRC). During the third quarter of 2013, the Company sent HMRC additional information supporting its position. Currently, discussions with HMRC are ongoing and a resolution has not been reached. As of September 30, 2013, the Company has not established a reserve for this issue.

During the third quarter of 2013, the Company met with New York State Department of Taxation and Finance to discuss the Company's respective positions regarding certain issues related to the 2008 tax year. Currently, discussions are ongoing and a resolution has not been reached. As of September 30, 2013, the Company has not established a reserve for this issue.

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As of December 31, 2012, the Company's consolidated NOL carryforward was \$1.3 billion which will expire between tax years 2029 through 2032. As a result of commutation activity in the second quarter of 2013, the Company's NOL has significantly increased from December 31, 2012. As of September 30, 2013, the Company's NOL is approximately \$2.8 billion. As of December 31, 2012, the Company also had a capital loss carryforward of \$165 million which will expire between tax years 2013 through 2017. However, as of September 30, 2013, the Company has generated year-to-date capital gain income sufficient to fully utilize the 2012 capital loss carryforward.



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### **MBIA Inc. and Subsidiaries**

### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 11: Business Segments**

MBIA manages its activities through three principal business operations: U.S. public finance insurance, structured finance and international insurance, and advisory services. The Company's U.S. public finance insurance business is operated through National, its structured finance and international insurance business is operated through MBIA Corp., and its advisory services business is primarily operated through Cutwater. MBIA Inc. and certain of its subsidiaries also manage certain other business activities, the results of which are reported in its corporate, asset/liability products, and conduit segments. The corporate segment includes revenues and expenses that arise from general corporate activities. While the asset/liability products and conduit businesses represent separate business segments, they may be referred to collectively as wind-down operations as the funding programs managed through those businesses are in wind-down.

As defined by segment reporting, an operating segment is a component of a company (i) that engages in business activities from which it earns revenue and incurs expenses, (ii) whose operating results are regularly reviewed by the Chief Operating Decision Maker to assess the performance of the segment and to make decisions about the allocation of resources to the segment and, (iii) for which discrete financial information is available. The following sections provide a description of each of the Company's reportable operating segments.

#### *U.S. Public Finance Insurance*

The Company's U.S. public finance insurance segment is principally conducted through National. The financial guarantees issued by National provide unconditional and irrevocable guarantees of the payment of principal of, and interest or other amounts owing on, U.S. public finance insured obligations when due. The obligations are generally not subject to acceleration, except that National may have the right, at its discretion, to accelerate insured obligations upon default or otherwise. National issues financial guarantees for municipal bonds, including tax-exempt and taxable indebtedness of U.S. political subdivisions, as well as utility districts, airports, health care institutions, higher educational facilities, student loan issuers, housing authorities and other similar agencies and obligations issued by private entities that finance projects that serve a substantial public purpose. Municipal bonds and privately issued bonds used for the financing of public purpose projects are generally supported by taxes, assessments, fees or tariffs related to the use of these projects, lease payments or other similar types of revenue streams. National has not written any meaningful amount of business since its formation in 2009.

#### *Structured Finance and International Insurance*

The Company's structured finance and international insurance segment is principally conducted through MBIA Corp. The financial guarantees issued by MBIA Corp. generally provide unconditional and irrevocable guarantees of the payment of principal of, and interest or other amounts owing on, global structured finance and non-U.S. public finance insured obligations when due, or in the event MBIA Corp. has the right, at its discretion, to accelerate insured obligations upon default or otherwise, upon MBIA Corp.'s acceleration. Certain guaranteed investment contracts written by MBIA Inc. are insured by MBIA Corp., and if MBIA Inc. were to have insufficient assets to pay amounts due upon maturity or termination, MBIA Corp. would make such payments. MBIA Corp. also insures debt obligations of the following affiliates:

MBIA Inc.;

GFL;

Meridian Funding Company, LLC;

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LaCrosse Financial Products, LLC, a wholly-owned affiliate, in which MBIA Corp. has written insurance policies guaranteeing the obligations under CDS, including termination payments that may become due upon certain events including the insolvency or payment default of the financial guarantor or the CDS issuer.

MBIA Corp. s guarantees insure structured finance and asset-backed obligations, privately issued bonds used for the financing of public purpose projects, which are primarily located outside of the U.S. and that include toll roads, bridges, airports, public transportation facilities, utilities and other types of infrastructure projects serving a substantial public purpose, and obligations of sovereign-related and sub-sovereign issuers. Structured finance and ABS typically are securities repayable from expected cash flows generated by a specified pool of assets, such as residential and commercial mortgages, insurance policies, consumer loans, corporate loans and bonds, trade and export receivables, and leases for equipment, aircraft and real estate property. The Company is no longer insuring new credit derivative contracts except for transactions related to the reduction of existing derivative exposure. MBIA Corp. has not written any meaningful amount of business since 2008.

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### **MBIA Inc. and Subsidiaries**

#### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 11: Business Segments (continued)**

##### *Advisory Services*

The advisory services segment primarily consists of the operations of Cutwater Investor Services Corp. ( Cutwater-ISC ), Cutwater Asset Management Corp. ( Cutwater-AMC ), and Trifinium. Cutwater-ISC and Cutwater-AMC provide advisory services, including cash management, discretionary asset management and structured products on a fee-for-service basis. Cutwater offers these services to public, not-for-profit, corporate and financial services clients, including MBIA Inc. and its subsidiaries, as well as portfolio accounting and reporting services. Cutwater-ISC and Cutwater-AMC are Securities and Exchange Commission registered investment advisers. Cutwater-AMC is also a Financial Industry Regulatory Authority member firm. Trifinium provides certain advisory services primarily in the European Union and is regulated by the Financial Conduct Authority in the U.K.

##### *Corporate*

The Company's corporate segment is principally conducted through Optinuity Alliance Resources Corporation ( Optinuity ), which provides general support services to the corporate segment and other operating businesses. Optinuity is a reportable segment that includes revenues and expenses that arise from general corporate activities, such as fees, net investment income, net gains and losses, interest expense on MBIA Inc. debt and general corporate expenses. Employees of the service company provide various support services including management, legal, accounting, treasury, information technology, and insurance portfolio surveillance, among others, on a fee-for-service basis. The service company's revenues and expenses are included in the results of the corporate segment.

##### *Wind-down Operations*

The Company's wind-down operations consist of the asset/liability products and conduit segments. The asset/liability products segment principally consists of the activities of MBIA Inc., MBIA Investment Management Corp. ( IMC ) and GFL. IMC, along with MBIA Inc., provided customized investment agreements, guaranteed by MBIA Corp., for bond proceeds and other public funds for such purposes as construction, loan origination, escrow and debt service or other reserve fund requirements. It also provided customized products for funds that are invested as part of asset-backed or structured product transactions. GFL raised funds through the issuance of MTNs with varying maturities, which were, in turn, guaranteed by MBIA Corp. GFL lent the proceeds of these MTN issuances to MBIA Inc. ( GFL Loans ). MBIA Inc. invested the proceeds of investment agreements and GFL Loans in eligible investments, which consisted of investment grade securities rated investment grade at the time of purchase and maintained a minimum average double-A credit quality rating at the time of purchase. MBIA Inc. primarily purchases domestic securities, which are pledged to MBIA Corp. as security for its guarantees on investment agreements and MTNs.

The Company's conduit segment administers one conduit through MBIA Asset Finance, LLC. Assets financed by this conduit are currently funded by MTNs.

The ratings downgrades of MBIA Corp. have resulted in a substantial reduction of funding activities and the termination and collateralization of certain investment agreements, as well as winding down of existing asset/liability products and conduit obligations.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 11: Business Segments (continued)*****Segments Results***

The following tables provide the Company's segment results for the three months ended September 30, 2013 and 2012:

In millions	Three Months Ended September 30, 2013						Consolidated
	U.S. Public Finance Insurance	Structured Finance and International Insurance	Advisory Services	Corporate	Wind-down Operations	Eliminations	
Revenues <sup>(1)</sup>	\$ 93	\$ 39	\$ 3	\$ 10	\$ 6	\$ -	\$ 151
Net change in fair value of insured derivatives	-	257	-	-	-	-	257
Net gains (losses) on financial instruments at fair value and foreign exchange	-	(3)	-	37	(29)	-	5
Net gains (losses) on extinguishment of debt	-	-	-	-	7	(1)	6
Other net realized gains (losses)	(29)	-	-	-	-	-	(29)
Revenues of consolidated VIEs	-	30	-	(1)	1	-	30
Inter-segment revenues <sup>(2)</sup>	10	20	8	35	(3)	(70)	-
Total revenues	74	343	11	81	(18)	(71)	420
Losses and loss adjustment	35	63	-	-	-	-	98
Operating	13	22	16	29	-	-	80
Interest	-	27	-	13	19	-	59
Expenses of consolidated VIEs	-	12	-	-	-	-	12
Inter-segment expenses <sup>(2)</sup>	20	23	3	3	17	(66)	-
Total expenses	68	147	19	45	36	(66)	249
Income (loss) before income taxes	\$ 6	\$ 196	\$ (8)	\$ 36	\$ (54)	\$ (5)	\$ 171
Identifiable assets	\$ 6,509	\$ 12,096	\$ 47	\$ 910	\$ 1,785	\$ (3,714) <sup>(3)</sup>	\$ 17,633

(1) - Represents the sum of third-party financial guarantee net premiums earned, net investment income, insurance-related fees and reimbursements, investment management fees and other fees.

(2) - Represents intercompany premium income and expense, intercompany asset management fees and expenses, and intercompany interest income and expense pertaining to intercompany receivables and payables.

(3) - Consists of intercompany reinsurance balances, repurchase agreements and deferred income taxes.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 11: Business Segments (continued)**

In millions	Three Months Ended September 30, 2012						
	U.S. Public Finance Insurance	Structured Finance and International Insurance	Advisory Services	Corporate	Wind-down Operations	Eliminations	Consolidated
Revenues <sup>(1)</sup>	\$ 149	\$ 59	\$ 5	\$ 3	\$ 9	\$ -	\$ 225
Net change in fair value of insured derivatives	-	(21)	-	-	-	-	(21)
Net gains (losses) on financial instruments at fair value and foreign exchange	22	14	-	11	(40)	-	7
Net investment losses related to other-than-temporary impairments	-	(4)	-	(4)	-	-	(8)
Other net realized gains (losses)	-	-	-	1	-	-	1
Revenues of consolidated VIEs	-	57	-	-	20	-	77
Inter-segment revenues <sup>(2)</sup>	43	29	8	53	(1)	(132)	-
Total revenues	214	134	13	64	(12)	(132)	281
Losses and loss adjustment	4	167	-	-	-	-	171
Operating	14	29	12	24	1	-	80
Interest	-	33	-	14	22	-	69
Expenses of consolidated VIEs	-	15	-	-	3	-	18
Inter-segment expenses <sup>(2)</sup>	32	54	3	4	39	(132)	-
Total expenses	50	298	15	42	65	(132)	338
Income (loss) before income taxes	\$ 164	\$ (164)	\$ (2)	\$ 22	\$ (77)	\$ -	\$ (57)
Identifiable assets	\$ 7,134	\$ 17,399	\$ 53	\$ 843	\$ 2,861	\$ (6,158) <sup>(3)</sup>	\$ 22,132

(1) - Represents the sum of third-party financial guarantee net premiums earned, net investment income, insurance-related fees and reimbursements, investment management fees and other fees.

(2) - Represents intercompany premium income and expense, intercompany asset management fees and expenses, and intercompany interest income and expense pertaining to intercompany receivables and payables.

(3) - Consists of intercompany reinsurance balances, repurchase agreements and loans.



**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 11: Business Segments (continued)**

The following tables provide the Company's segment results for the nine months ended September 30, 2013 and 2012:

In millions	Nine Months Ended September 30, 2013						
	U.S. Public Finance Insurance	Structured Finance and International Insurance	Advisory Services	Corporate	Wind-down Operations	Eliminations	Consolidated
Revenues <sup>(1)</sup>	\$ 314	\$ 120	\$ 13	\$ 15	\$ 21	\$ -	\$ 483
Net change in fair value of insured derivatives	-	14	-	-	-	-	14
Net gains (losses) on financial instruments at fair value and foreign exchange	30	31	-	39	(38)	-	62
Net gains (losses) on extinguishment of debt	-	-	-	-	11	38 <sup>(3)</sup>	49
Other net realized gains (losses)	(29)	-	-	-	-	-	(29)
Revenues of consolidated VIEs	-	174	-	(10)	8	-	172
Inter-segment revenues <sup>(2)</sup>	81	52	20	56	(5)	(204)	-
Total revenues	396	391	33	100	(3)	(166)	751
Losses and loss adjustment	105	(13)	-	-	-	-	92
Operating	57	91	42	125	1	-	316
Interest	-	84	-	36	59	-	179
Expenses of consolidated VIEs	-	38	-	-	4	-	42
Inter-segment expenses <sup>(2)</sup>	72	115	6	8	32	(233)	-
Total expenses	234	315	48	169	96	(233)	629
Income (loss) before income taxes	\$ 162	\$ 76	\$ (15)	\$ (69)	\$ (99)	\$ 67	\$ 122
Identifiable assets	\$ 6,509	\$ 12,096	\$ 47	\$ 910	\$ 1,785	\$ (3,714) <sup>(4)</sup>	\$ 17,633

(1) - Represents the sum of third-party financial guarantee net premiums earned, net investment income, insurance-related fees and reimbursements, investment management fees and other fees.

(2) - Represents intercompany premium income and expense, intercompany asset management fees and expenses, intercompany interest income, expenses pertaining to intercompany receivables and payables and intercompany loans.



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- (3) - Represents the gain on the debt received as consideration in connection with the BofA Settlement Agreement.
- (4) - Consists of intercompany reinsurance balances, repurchase agreements and deferred income taxes.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 11: Business Segments (continued)**

In millions	Nine Months Ended September 30, 2012						Consolidated
	U.S. Public Finance Insurance	Structured Finance and International Insurance	Advisory Services	Corporate	Wind-down Operations	Eliminations	
Revenues <sup>(1)</sup>	\$ 419	\$ 194	\$ 16	\$ 10	\$ 44	\$ -	\$ 683
Net change in fair value of insured derivatives	-	1,053	-	-	-	-	1,053
Net gains (losses) on financial instruments at fair value and foreign exchange	43	80	-	19	(160)	-	(18)
Net investment losses related to other-than-temporary impairments	-	(45)	-	(4)	(56)	-	(105)
Other net realized gains (losses)	-	1	-	6	-	-	7
Revenues of consolidated VIEs	-	23	-	-	60	-	83
Inter-segment revenues <sup>(2)</sup>	123	10	26	132	(19)	(272)	-
Total revenues	585	1,316	42	163	(131)	(272)	1,703
Losses and loss adjustment	15	315	-	-	-	-	330
Operating	112	120	38	69	4	-	343
Interest	-	99	-	43	72	-	214
Expenses of consolidated VIEs	-	46	-	-	11	-	57
Inter-segment expenses <sup>(2)</sup>	91	154	10	10	87	(352)	-
Total expenses	218	734	48	122	174	(352)	944
Income (loss) before income taxes	\$ 367	\$ 582	\$ (6)	\$ 41	\$ (305)	\$ 80	\$ 759
Identifiable assets	\$ 7,134	\$ 17,399	\$ 53	\$ 843	\$ 2,861	\$ (6,158) <sup>(3)</sup>	\$ 22,132

(1) - Represents the sum of third-party financial guarantee net premiums earned, net investment income, insurance-related fees and reimbursements, investment management fees and other fees.

(2) - Represents intercompany premium income and expense, intercompany asset management fees and expenses, and intercompany interest income and expense pertaining to intercompany receivables and payables.

(3) - Consists of intercompany reinsurance balances, repurchase agreements and loans.

Premiums on financial guarantees and insured derivatives reported within the Company's insurance segments are generated within and outside the U.S. The following table summarizes premiums earned on financial guarantees and insured derivatives by geographic location of risk for the three and nine months ended September 30, 2013 and 2012:

In millions	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Total premiums earned:				
United States	\$ 82	\$ 141	\$ 297	\$ 402
United Kingdom	9	9	26	27
Europe (excluding United Kingdom)	3	3	9	12
Internationally diversified	2	3	8	13
Central and South America	13	8	28	40
Asia	1	2	3	4
Other	2	2	6	8
Total	\$ 112	\$ 168	\$ 377	\$ 506

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 11: Business Segments (continued)**

The following tables provide the results of the segments within the wind-down operations for the three months ended September 30, 2013 and 2012:

In millions	Three Months Ended September 30, 2013			
	Asset / Liability Products	Conduits	Eliminations	Total Wind- down Operations
Revenues <sup>(1)</sup>	\$ 6	\$ -	\$ -	\$ 6
Net gains (losses) on financial instruments at fair value and foreign exchange	(29)	-	-	(29)
Net gains (losses) on extinguishment of debt	7	-	-	7
Revenues of consolidated VIEs	-	1	-	1
Inter-segment revenues <sup>(2)</sup>	(1)	(2)	-	(3)
Total revenues	(17)	(1)	-	(18)
Interest	19	-	-	19
Inter-segment expenses <sup>(2)</sup>	2	15	-	17
Total expenses	21	15	-	36
Income (loss) before income taxes	\$ (38)	\$ (16)	\$ -	\$ (54)
Identifiable assets	\$ 1,586	\$ 198	\$ 1	\$ 1,785

(1) - Represents the sum of third-party interest income, investment management services fees and other fees.

(2) - Represents intercompany asset management fees and expenses plus intercompany interest income and expense pertaining to intercompany debt.

In millions	Three Months Ended September 30, 2012			
	Asset / Liability Products	Conduits	Eliminations	Total Wind- down Operations
Revenues <sup>(1)</sup>	\$ 9	\$ -	\$ -	\$ 9
Net gains (losses) on financial instruments at fair value and foreign exchange	(40)	-	-	(40)
Revenues of consolidated VIEs	-	20	-	20
Inter-segment revenues <sup>(2)</sup>	(1)	-	-	(1)
Total revenues	(32)	20	-	(12)

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Operating	1	-	-	1
Interest	22	-	-	22
Expenses of consolidated VIEs	-	3	-	3
Inter-segment expenses <sup>(2)</sup>	3	36	-	39
Total expenses	26	39	-	65
Income (loss) before income taxes	\$ (58)	\$ (19)	\$ -	\$ (77)
Identifiable assets	\$ 2,219	\$ 693	\$ (51)	\$ 2,861

(1) - Represents the sum of third-party interest income, investment management services fees and other fees.

(2) - Represents intercompany asset management fees and expenses plus intercompany interest income and expense pertaining to intercompany debt.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 11: Business Segments (continued)**

The following tables provide the results of the segments within the wind-down operations for the nine months ended September 30, 2013 and 2012:

In millions	Nine Months Ended September 30, 2013			
	Asset / Liability Products	Conduits	Eliminations	Total Wind- down Operations
Revenues <sup>(1)</sup>	\$ 21	\$ -	\$ -	\$ 21
Net gains (losses) on financial instruments at fair value and foreign exchange	(38)	-	-	(38)
Net gains (losses) on extinguishment of debt	11	-	-	11
Revenues of consolidated VIEs	-	8	-	8
Inter-segment revenues <sup>(2)</sup>	(3)	(8)	6	(5)
Total revenues	(9)	-	6	(3)
Operating	1	-	-	1
Interest	59	-	-	59
Expenses of consolidated VIEs	-	4	-	4
Inter-segment expenses <sup>(2)</sup>	6	26	-	32
Total expenses	66	30	-	96
Income (loss) before income taxes	\$ (75)	\$ (30)	\$ 6	\$ (99)
Identifiable assets	\$ 1,586	\$ 198	\$ 1	\$ 1,785

(1) - Represents the sum of third-party interest income, investment management services fees and other fees.

(2) - Represents intercompany asset management fees and expenses plus intercompany interest income and expense pertaining to intercompany debt.

In millions	Nine Months Ended September 30, 2012			
	Asset / Liability Products	Conduits	Eliminations	Total Wind- down Operations
Revenues <sup>(1)</sup>	\$ 44	\$ -	\$ -	\$ 44
Net gains (losses) on financial instruments at fair value and foreign exchange	(160)	-	-	(160)
Net investment losses related to other-than-temporary impairments	(56)	-	-	(56)
Revenues of consolidated VIEs	-	60	-	60

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Inter-segment revenues <sup>(2)</sup>	(15)	(2)	(2)	(19)
Total revenues	(187)	58	(2)	(131)
Operating	4	-	-	4
Interest	72	-	-	72
Expenses of consolidated VIEs	-	11	-	11
Inter-segment expenses <sup>(2)</sup>	16	71	-	87
Total expenses	92	82	-	174
Income (loss) before income taxes	\$ (279)	\$ (24)	\$ (2)	\$ (305)
Identifiable assets	\$ 2,219	\$ 693	\$ (51)	\$ 2,861

(1) - Represents the sum of third-party interest income, investment management services fees and other fees.

(2) - Represents intercompany asset management fees and expenses plus intercompany interest income and expense pertaining to intercompany debt.

**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 12: Earnings Per Share**

Basic earnings per share excludes dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects the dilutive effect of all stock options, warrants and other items outstanding during the period that could potentially result in the issuance of common stock. For the three months ended September 30, 2013 and 2012, there were 26,988,764 and 28,732,318, respectively, of stock options and warrants outstanding that were not included in the diluted earnings per share calculation because they were antidilutive. For the nine months ended September 30, 2013 and 2012, there were 27,369,789 and 28,785,415, respectively, of stock options and warrants outstanding that were not included in the diluted earnings per share calculation because they were antidilutive.

The following table presents the computation of basic and diluted earnings per share for the three and nine months ended September 30, 2013 and 2012:

\$ in millions except share and per share amounts	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net income (loss)	\$ 132	\$ 7	\$ 118	\$ 598
Basic weighted average shares <sup>(1)</sup>	192,711,608	193,879,994	193,440,078	193,760,654
Effect of common stock equivalents:				
Stock options and warrants	4,035,163	1,097,648	4,322,410	1,074,883
Diluted weighted average shares	196,746,771	194,977,642	197,762,488	194,835,537
Net income (loss) per common share:				
Basic	\$ 0.68	\$ 0.04	\$ 0.61	\$ 3.09
Diluted	\$ 0.67	\$ 0.04	\$ 0.60	\$ 3.07

(1) - Includes 4,349,481 and 5,524,396 of unvested restricted stock and units that receive nonforfeitable dividends or dividend equivalents for the three months ended September 30, 2013 and 2012, respectively. Includes 4,981,970 and 5,442,143 of unvested restricted stock and units that receive nonforfeitable dividends or dividend equivalents for the nine months ended September 30, 2013 and 2012, respectively.

**Note 13: Accumulated Other Comprehensive Income**

The following table presents the changes in the components of AOCI for the nine months ended September 30, 2013:

In millions	Unrealized Gains (Losses) on AFS Securities, Net		Foreign Currency Translation, Net		Total
Balance, January 1, 2013	\$	43	\$	13	\$ 56
Other comprehensive income before reclassifications		(91)		(8)	(99)



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Amounts reclassified from AOCI	(7)	-	(7)
Net current period other comprehensive income (loss)	(98)	(8)	(106)
Balance, September 30, 2013	\$ (55)	\$ 5	\$ (50)

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**Table of Contents****MBIA Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****Note 13: Accumulated Other Comprehensive Income (continued)**

The following table presents the details of the reclassifications from AOCI for the nine months ended September 30, 2013:

In millions

Details about AOCI Components	Amounts Reclassified from AOCI	Affected Line Item on the Consolidated Statements of Operations
Unrealized gains (losses) on AFS securities:		
Realized gain on sale of securities	\$ 15	Net gains (losses) on financial instruments at fair value and foreign exchange
Amortization on securities	(4)	Net investment income
	11	Income (loss) before income taxes
	4	Provision (benefit) for income taxes
Total reclassifications for the period	\$ 7	Net income (loss)

**Note 14: Commitments and Contingencies**

The following commitments and contingencies provide an update of those discussed in Note 20: Commitments and Contingencies in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012, and should be read in conjunction with the complete descriptions provided in the aforementioned Form 10-K.

***Recovery Litigation***

*MBIA Insurance Corp. v. Countrywide Home Loans, Inc., et al.*; Index No. 602825/08 (N.Y. Sup. Ct., N.Y. County)

In May of 2013, the parties reached an agreement to resolve MBIA's claims in this action. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the comprehensive settlement agreement.

*MBIA Insurance Corp. v. Bank of America Corp.; Countrywide Home Loans, Inc., Countrywide Securities Corp., and Countrywide Financial Corp. et al.*; Case No. BC417572 (Ca. Super. Ct., County of Los Angeles)

In May of 2013, the parties reached an agreement to resolve MBIA's claims in this action. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the comprehensive settlement agreement.

*MBIA Insurance Corp. v. Federal Deposit Insurance Corporation (in its corporate capacity and as conservator and receiver for IndyMac Federal Bank, F.S.B.)*; Civil Action No. 09-01011 (ABJ) (D.D.C.)

On March 8, 2013, the United States Court of Appeals for the D.C. Circuit affirmed the district court's ruling dismissing MBIA Corp.'s amended complaint.

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*MBIA Insurance Corp. v. Credit Suisse Securities (USA) LLC, et al.*; Index No. 603751/2009 (N.Y. Sup. Ct., N.Y. County)

On March 8, 2013, the defendants filed their answer to the amended complaint. On April 19, 2013, the court issued an order scheduling fact discovery to close by June 30, 2014.

*MBIA Insurance Corp. v. J.P. Morgan Securities LLC (f/k/a Bear, Stearns & Co. Inc.)*; Index No. 64676/2012 (N.Y. Sup. Ct., County of Westchester)

On October 9, 2013, J.P. Morgan Securities LLC filed its motion for summary judgment.

*MBIA Insurance Corp. v. Ally Financial Inc. (f/k/a GMAC, LLC) et al.*; 12-cv-02563 SRN/TNL (D. Minn.)

This case is currently stayed.

*MBIA Insurance Corp. v. Flagstar ABS, LLC, et al.*; 13-cv-0262 (JSR) (S.D.N.Y.)

The parties filed a Stipulation of Discontinuance and Order of Dismissal with Prejudice of this action on May 2, 2013. Under the terms of the settlement, MBIA Corp. dismissed the lawsuit against Flagstar Bank in exchange for \$110 million in cash and other consideration.

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### **MBIA Inc. and Subsidiaries**

#### **Notes to Consolidated Financial Statements (Unaudited)**

#### **Note 14: Commitments and Contingencies (continued)**

##### ***Transformation Litigation***

*ABN AMRO Bank N.V. et al. v. Eric Dinallo et al.*; Index no. 601846/09 (N.Y. Sup. Ct., N.Y. County)

On March 4, 2013, the court issued a decision dismissing the Article 78 proceeding. On April 2, 2013, the remaining plaintiffs filed a Notice of Appeal to the Appellate Division, First Department. In May of 2013, following the Bank of America and Societe Generale settlements, all plaintiffs in this matter dismissed their claims. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the settlement agreements.

*ABN AMRO Bank N.V. et al. v. MBIA Inc. et al.*; Index No. 601475/2009 (N.Y. Sup. Ct., N.Y. County)

In May of 2013, following the Bank of America and Societe Generale settlements, all plaintiffs in this matter dismissed their claims. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the settlement agreements.

*Barclays Bank PLC., et al. v. Wrynn et al.*; Index No. 651811/2010 (N.Y. Sup. Ct., N.Y. County)

In May of 2013, following the Bank of America and Societe Generale settlements, all plaintiffs in this matter dismissed their claims. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the settlement agreements.

*CQS ABS Master Fund Ltd., CQS Select ABS Master Fund Ltd., and CQS ABS Alpha Master Fund Ltd. v. MBIA Inc. et al.*; Civil Action No. 12-cv-6840 (R.S.) (S.D.N.Y.)

On October 23, 2013, the plaintiffs filed a motion for a preliminary injunction seeking to prospectively enjoin National from issuing dividends during the pendency of the litigation. Although the motion referenced the dividend that the Company previously had disclosed that National intended to pay in the fourth quarter of 2013, that dividend was paid prior to the filing of the motion and therefore is not subject to the relief requested by the motion. Refer to Note 1: Business Developments and Risks and Uncertainties for information regarding this dividend. National filed its reply to the motion on November 1, 2013, and believes it is not meritorious and should be denied. The court has adjourned oral argument on the motion to November 14, 2013. The court entered a revised Management Plan and Scheduling Order setting a fact discovery deadline of April 4, 2014.

*Broadbill Partners LP, et al. v. MBIA Inc., et al.*; Index No. 653865/2012 (N.Y. Sup. Ct., N.Y. County)

On June 6, 2013, the plaintiffs voluntarily dismissed the litigation without prejudice. A Stipulation of Discontinuance was filed on June 7, 2013.

##### ***Corporate Litigation***

*Bank of America v. MBIA Inc. and The Bank of New York Mellon, as Indenture Trustee*; Index No. 70444/2012 (N.Y. Sup. Ct., Westchester County)

In May of 2013, the parties reached an agreement to resolve their respective claims in this action. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the comprehensive settlement agreement.

*MBIA Inc. v. Bank of America Corp. and Blue Ridge Investments, L.L.C.*; Index No. 51664/2013 (N.Y. Sup. Ct., Westchester County)

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In May of 2013, the parties reached an agreement to resolve their respective claims in this action. Refer to Note 1: Business Developments and Risks and Uncertainties included herein for a description of the comprehensive settlement agreement.

*Mary Crescente v. Joseph Brown, et al.*; Index No. 17595/2008 (N.Y. Sup. Ct., Westchester County)

On March 25, 2013, a Stipulation of Discontinuance was filed with the court resolving the litigation.

*Ambac Bond Insurance Coverage Cases*, Coordinated Proceeding Case No. JCCP 4555 (Super. Ct. of Cal., County of San Francisco)

The plaintiffs filed a notice of appeal of the March 22, 2013 decision that granted the Bond Insurer defendants' motion to strike pursuant to California's Anti-SLAPP statute dismissing the plaintiffs' claims under California's Cartwright Act. On October 1, 2013, the Bond Insurer defendants filed a notice of cross-appeal.

*Tri-City Healthcare District v. Citibank, et al.*; Case No. 30-2010-00359692 (Super. Ct. of Cal., County of Orange)

The parties reached an agreement to resolve Tri-City Healthcare District's claims in this matter.

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**MBIA Inc. and Subsidiaries**

**Notes to Consolidated Financial Statements (Unaudited)**

**Note 14: Commitments and Contingencies (continued)**

*City of Phoenix v. AMBAC et al.*, Case No. 2:10-cv-00555-TMB (D. Ariz.)

On June 4, 2013, the parties reached an agreement to resolve the City of Phoenix's claims in this matter.

*National Public Finance Guarantee Corp. et al. v City of Detroit, Michigan et al.*; Adv. Pro. No 13-05309-swr (Bkcy. E.D. MI)

On November 8, 2013, National (together with Assured Guaranty Municipal Corp.) commenced an adversary proceeding against the City of Detroit and certain individuals employees/managers in the Chapter 9 bankruptcy case titled In re: City of Detroit, Michigan; Case No. 13-53846, pending in the United States Bankruptcy Court for the Eastern District of Michigan. The complaint seeks, among other things, a declaration that the City of Detroit and its employees/managers must comply with Michigan state law in the collection, segregation and use of restricted *ad valorem* tax proceeds levied and pledged to repay the principal and interest on several series of Detroit's unlimited tax general obligation bonds.

The Company is defending against the aforementioned actions in which it is a defendant and expects ultimately to prevail on the merits. There is no assurance, however, that the Company will prevail in these actions. Adverse rulings in these actions could have a material adverse effect on the Company's ability to implement its strategy and on its business, results of operations, cash flows and financial condition. At this stage of the litigation, there has not been a determination as to the amount, if any, of damages. Accordingly, the Company is not able to estimate any amount of loss or range of loss.

There are no other material lawsuits pending or, to the knowledge of the Company, threatened, to which the Company or any of its subsidiaries is a party.

**Note 15: Subsequent Events**

Refer to Note 14: Commitments and Contingencies for information about legal proceedings that occurred after September 30, 2013.

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### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

#### **FORWARD-LOOKING AND CAUTIONARY STATEMENTS**

This quarterly report of MBIA Inc. ( "MBIA", the "Company", we, us or our ) includes statements that are not historical or current facts and are forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The words believe, anticipate, project, plan, expect, estimate, intend, will likely result, looking forward, or will continue and similar expressions are used to identify forward-looking statements. These statements are subject to certain risks and uncertainties that could cause actual results to differ materially from historical earnings and those presently anticipated or projected. MBIA cautions readers not to place undue reliance on any such forward-looking statements, which speak only to their respective dates. We undertake no obligation to publicly correct or update any forward-looking statement if the Company later becomes aware that such result is not likely to be achieved.

The following are some of the factors that could affect financial performance or could cause actual results to differ materially from estimates contained in or underlying the Company's forward-looking statements:

the possibility that the Company will experience severe losses or liquidity needs due to increased deterioration in its insurance portfolios and in particular, due to the performance of insured credit default swaps ( "CDS" ) that are backed by or reference commercial mortgage-backed securities ( "CMBS" ) pools and commercial real estate ( "CRE" ) collateralized debt obligations ( "CDOs" ), insured residential mortgage-backed securities ( "RMBS" ) transactions, and insured asset-backed security ( "ABS" ) CDOs;

uncertainty regarding whether the Company will realize, or will be delayed in realizing, insurance loss recoveries expected in disputes with sellers/servicers of RMBS transactions and excess spread at the levels recorded in its consolidated financial statements;

failure to implement our risk reduction and liquidity strategies because of an inability to draw on expected liquidity sources or obtain regulatory approvals;

the possibility that loss reserve estimates are not adequate to cover potential claims;

our ability to access capital and our exposure to significant fluctuations in liquidity and asset values within the global credit markets, in particular within our asset/liability products segment;

our ability to fully implement our strategic plan, including our ability to achieve high stable ratings for National Public Finance Guarantee Corporation (together with its subsidiaries, "National") or any of our other insurance companies and our ability to commute certain of our insured exposures, including as a result of limited available liquidity;

the possibility of deterioration in the economic environment and financial markets in the United States ( "U.S." ) or abroad, and adverse developments in European sovereign credit performance, real estate market performance, credit spreads, interest rates and foreign currency levels;

the possibility that severe fiscal stress will result in credit losses or impairments on obligations of state and local governments that we insure;

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the possibility of impairment of general obligation bonds that we insure as a result of municipal issuers that are experiencing severe financial stress filing for protection under Chapter 9 of the United States Bankruptcy Code and the unpredictable outcome of bankruptcy proceedings;

changes in the Company's or its insurance subsidiaries' credit ratings;

competitive conditions for bond insurance, including potential entry into the public finance market of additional insurers of municipal bonds, and changes in the demand for financial guarantee insurance;

the effects of governmental regulation, including insurance laws, securities laws, tax laws, legal precedents and accounting rules; and

uncertainties that have not been identified at this time.

The above factors provide a summary of and are qualified in their entirety by the risk factors discussed under "Risk Factors" in Part II, Item 1A of this Form 10-Q. In addition, refer to "Note 1: Business Developments and Risks and Uncertainties" in the Notes to Consolidated Financial Statements for a discussion of certain risks and uncertainties related to our financial statements.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****EXECUTIVE OVERVIEW**

MBIA operates one of the largest financial guarantee insurance businesses in the industry and is a provider of asset management and advisory services. These activities are managed through three business segments: U.S. public finance insurance; structured finance and international insurance; and advisory services. Our U.S. public finance insurance business is primarily operated through National, our structured finance and international insurance business is primarily operated through MBIA Insurance Corporation and its subsidiaries ( MBIA Corp. ), and our asset management and advisory services business is primarily operated through Cutwater Holdings, LLC and its subsidiaries ( Cutwater ). We also manage certain business activities through our corporate, asset/liability products, and conduit segments. Our corporate segment includes revenues and expenses that arise from general corporate activities. Funding programs managed through our asset/liability products and conduit segments are in wind-down.

***Recent Developments******Operating Cost Reductions***

In order to better position the Company for future business opportunities, in the third quarter of 2013, we initiated cost reduction measures focused on our legal, consulting, staffing and head office occupancy costs. As a result, expenses for net compensation costs related to staff reductions totaled \$18 million and were recorded primarily during the third quarter of 2013. These expenses are included in Operating expenses on our consolidated statements of operations. These staff reductions reduced our worldwide June 30, 2013 headcount by approximately 21%. We estimate that our staff reductions will result in annualized future savings of approximately \$24 million, which will be offset by any future staff increases and increases in compensation. In addition, as a result of the potential sale of the office used in our operations, we recorded an impairment charge of \$29 million on our Armonk, New York facility. The carrying value of the facility was adjusted to its fair market value, which was determined based on an independent third-party appraisal of the facility. This impairment charge is reflected in the results of our U.S. public finance insurance segment and is included in Other net realized gains (losses) on our consolidated statements of operations.

In addition, during the three and nine months ended September 30, 2013, operating expenses included \$2 million and \$89 million, respectively, related to settlement, consulting and legal expenses associated with the resolution of litigation matters with Bank of America, Societe Generale, and Flagstar Bank.

***Bank of America Settlement Agreement***

In May of 2013, MBIA Inc., together with its subsidiaries MBIA Corp. and National, entered into a comprehensive settlement agreement and related agreements (the BofA Settlement Agreement ) with Bank of America Corporation and certain of its subsidiaries (collectively, Bank of America ). Refer to Note 1: Business Developments and Risks and Uncertainties in the Notes to Consolidated Financial Statements for a discussion of the BofA Settlement Agreement. As a result of the BofA Settlement Agreement, the repayment of the remaining balance and accrued interest on MBIA Corp.'s secured loan from National (the National Secured Loan ) and recent credit ratings upgrades, the Company is currently evaluating strategies for re-entry into the U.S. public finance market.

***Societe Generale Settlement***

In May of 2013, the Company entered into an agreement with Societe Generale pursuant to which MBIA commuted \$4.2 billion of gross insured exposure comprising ABS CDOs, structured CMBS pools and CRE CDOs. Refer to Note 1: Business Developments and Risks and Uncertainties in the Notes to Consolidated Financial Statements for a description of the settlement.

***Residential Capital LLC Agreement***

In May of 2013, the Company, the Consenting Claimants, Residential Capital LLC ( ResCap ) and Ally Financial Inc. ( Ally ), agreed to the terms of a comprehensive plan agreement to support ResCap's Chapter 11 plan. The confirmation of ResCap's Chapter 11 plan would resolve MBIA Corp.'s claims against the Residential Funding Company, LLC, GMAC Mortgage LLC and ResCap estates, and Ally. In June of 2013, the bankruptcy court issued a Memorandum Opinion approving the Plan Support Agreement (the Plan ). The Plan is now subject to voting by creditors as well as a confirmation hearing by the bankruptcy court. All creditor ballots were due back by October 21, 2013 and as of the date of this report, the results had not been tallied. There can be no assurance that the Plan will be confirmed. Refer to Note 5: Loss and Loss

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Adjustment Expense Reserves in the Notes to Consolidated Financial Statements for a description of the agreement.

### *Transformation Litigation*

Subsequent to the BofA Settlement Agreement and the Societe Generale settlement, all litigation brought originally by the group of eighteen domestic and international financial institutions, relating to the establishment of National, has been resolved. Refer to Note 14: Commitments and Contingencies in the Notes to Consolidated Financial Statements for a description of this litigation.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****EXECUTIVE OVERVIEW (continued)***National*

As a result of the BofA Settlement Agreement and the Societe Generale settlement, Standard & Poor's Financial Services LLC (S&P) upgraded National's rating to A with a stable outlook. Also, Moody's Investors Service, Inc. (Moody's) upgraded National's rating to Baa1 with a positive outlook. The absence of higher ratings from S&P and Moody's has adversely impacted our ability to write new insurance business and our ability to write new premiums. The Company is seeking rating upgrades from the rating agencies and believes the current ratings of National do not fully represent the financial strength of National when compared with other companies in its industry. We expect to achieve high stable ratings for National that would be necessary to support writing new business, but there is no assurance that we will be able to achieve such ratings and the timing of such rating upgrades is uncertain. We are also considering obtaining ratings for National from additional rating agencies.

We expect National will gain market acceptance and become a competitive financial guarantor once its ratings are upgraded. We expect that the majority of its new business will be in the general obligation, tax-backed and revenue bond sectors. The Company also believes there are significant amounts of insurable bonds that have been issued on an unwrapped basis in recent years, which the Company believes meet its underwriting criteria and present attractive secondary market opportunities. In addition, we believe the increase in interest rates during 2013 and the continued issuance of new municipal debt will present attractive risk-adjusted business opportunities for National. National maintains underwriting criteria for most municipal risk types and expects opportunities for new business across the spectrum of municipal sectors. National's underwriting criteria does not limit it to particular sectors.

While there are currently two other bond insurers actively engaged in the market, one of which was recently established, we have observed other new competitors indicating an interest in entering the bond insurance market and continue to consider strategies for launch. We will continue to monitor the impact that new and existing market participants may have on our ability to compete in the U.S. public finance insurance market in the future.

In August of 2013, the novation agreement between Financial Guaranty Insurance Corporation (FGIC) and National, whereby FGIC transferred, by novation, to National all the rights and liabilities under each of the policies covered under a reinsurance agreement with FGIC, became effective. This novation agreement included covered policies that previously benefited from the reinsurance agreement and second-to-pay policies entered into by MBIA Insurance Corporation in 2008 that were subsequently assigned to and reinsured by National in 2009. As a result of this novation, National is now the primary insurer under these policies.

While our U.S. public finance insured portfolio in National continued to perform satisfactorily on the whole, we did experience increased stress in this portfolio in the nine months ended September 30, 2013, as a portion of the obligations that we insure were issued by some of the state and local governments that remain under extreme financial and budgetary stress. In addition, several of these local governments have filed for protection under the United States Bankruptcy Code or have entered into state statutory proceedings established to assist municipalities in managing through periods of severe fiscal stress. This could lead to an increase in defaults by such entities on the payment of their obligations and losses or impairments on a greater number of our insured transactions. We continue to monitor and analyze these situations very closely, and the overall extent and duration of this stress is uncertain. National has exposure to the Commonwealth of Puerto Rico (the Commonwealth) and certain governmental issuers in the territory. The Commonwealth is experiencing fiscal stress, however it has taken pro-active actions to address its significant economic challenges. We are continuing to monitor the situation closely, but do not expect a default by the Commonwealth. In addition, during the third quarter of 2013, National participated in the restructuring of a gaming revenue transaction, in which National received marketable securities where the fair value of these securities was less than the salvage receivable recorded at the time of the transaction. We expect to recover the full value of the original salvage receivable over time. Refer to the following Results of Operations - U.S. Public Finance Insurance Loss and Loss Adjustment Expenses section for additional information about this remedial credit transaction.

*MBIA Corp.*

As a result of the BofA Settlement Agreement, MBIA Corp.'s liquidity and capital risk profile has substantially improved. MBIA Corp. still has significant risk within its insured portfolio and the amount and timing of potential claims from its second-lien RMBS and remaining insured CMBS pools are uncertain. MBIA Corp.'s strategy for managing its CMBS pool and ABS CDO exposures has been evaluating opportunities to

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commute exposures and successfully executing such commutations. MBIA Corp.'s ability to commute insured transactions is limited by available liquidity. MBIA Corp. believes that it continues to have sufficient capital and liquidity to meet all of its expected obligations. Refer to Note 1: Business Developments and Risks and Uncertainties in the Notes to Consolidated Financial Statements for a discussion of significant risks and uncertainties that could affect amounts reported in the Company's financial statements in future periods. MBIA Corp.'s business and financial results have been significantly influenced by a number of factors including, but not limited to, the matters described below:

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****EXECUTIVE OVERVIEW (continued)**

Our expected liquidity and capital forecasts for MBIA Corp., which include expected availability of draws under a \$500 million three-year secured revolving credit agreement with Blue Ridge Investments, L.L.C. ( "Blue Ridge" ), an affiliate of Bank of America (the "Blue Ridge Secured Loan" ), expected recoveries from the ResCap agreement, and projected collections of excess spread and the remaining put-back recoverables, reflect more than adequate resources to pay expected claims. However, there are risks to these forecasts, as the amount and timing of potential claims from our second-lien RMBS and remaining insured CMBS pools are potentially volatile, as are the projected collections of excess spread and the remaining put-back recoverables. Further, the remaining insured portfolio, aside from these exposures, could deteriorate and result in loss reserves and claim payments. While we believe MBIA Corp. will have adequate resources to pay expected claims, if MBIA Corp. experiences higher than expected claim payments or is unable to commute the remaining exposures that represent substantial risk to the Company, MBIA Corp. may ultimately have insufficient resources to continue to pay claims, which could cause the New York State Department of Financial Services ( "NYSDFS" ) to put MBIA Insurance Corporation into a rehabilitation or liquidation proceeding. In addition, if MBIA Corp.'s statutory capital falls below \$750 million as a result of an increase in loss reserves, claims payments or for other reasons, Blue Ridge may in its sole discretion terminate its obligations to make loans under the Blue Ridge Secured Loan, or declare all borrowings to be due and immediately payable.

For the three and nine months ended September 30, 2013, we estimated additional aggregate losses and loss adjustment expense ( "LAE" ) of \$98 million and \$459 million, respectively, related to our insured CMBS exposure. We have recorded additional impairments on our insured CMBS portfolio every quarter since the beginning of 2010 reflecting that actual deterioration has been more than expected. It is possible that we will experience severe losses or near-term liquidity needs due to increased deterioration in our insured CMBS portfolio.

During the nine months ended September 30, 2013, MBIA Corp. commuted \$19.9 billion of gross insured exposure, primarily comprising structured CMBS pools, investment grade CDOs, ABS CDOs, first-lien subprime RMBS, high yield corporate CDOs, CRE CDOs, structured insurance securities and first-lien alternative A-paper RMBS. In consideration for the commutation of insured transactions, the Company has made and may in the future make payments to the counterparties, the amounts of which, if any, may be less than or greater than any statutory loss reserves established for the respective transactions. The Company enters into commutations in the ordinary course of its business and generally does not intend to make contemporaneous disclosures regarding any such transactions regardless of the amounts paid to effect such commutations in relation to the statutory loss reserves established for the respective transactions. The Company's ability to commute insured transactions is limited by available liquidity, including the availability of the Blue Ridge Secured Loan, other available financing structures and expected put-back recoveries, and commutations may be subject to regulatory approval by the NYSDFS and/or the United Kingdom's ( "U.K." ) Prudential Regulation Authority. There can be no assurance that the Company will be able to fund further commutations by borrowing or otherwise or that it will be able to obtain required regulatory approvals.

***Economic and Financial Market Trends***

We believe the first nine months of 2013 continued to show modest improvements in the U.S. economy. For the three months ended September 30, 2013, the U.S. economy expanded slightly aided by stabilization in the housing market and rising home prices. The unemployment rate dropped in the third quarter of 2013 to its lowest levels in over four years. While this continued improvement in the labor market should help to increase personal incomes, the ultimate outcomes on the debt ceiling, the federal budget and the Affordable Care Act will add uncertainty to the business and consumer segments of our economy. In addition, the recent speculation that the Federal Reserve might taper their quantitative easing programs caused concerns over the level of interest rates. Information concerning our interest rate sensitivity appears in Part I, Item 3, "Quantitative and Qualitative Disclosures about Market Risk". While Europe begins to display signs of recovering from its recession, such signs remain inconclusive and there continues to be high unemployment rates. Prolonged debt and budget issues and related austerity programs suggest that it may be some time before Europe shows sustained growth and a robust recovery. While we believe confidence in the U.S. economy should continue for the remainder of 2013, sustained job growth and resolution of fiscal policies in Washington are paramount to a complete recovery. MBIA's business outlook should be viewed against this backdrop since these are some of the key economic conditions which, together with the volatility of gains and losses on our insured credit derivatives, significantly impact our financial results.



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### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

#### **EXECUTIVE OVERVIEW (continued)**

##### ***Financial Highlights***

Our financial results, prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ), have been extremely volatile since the fourth quarter of 2007 primarily as a result of unrealized gains and losses from fair valuing our insured credit derivatives. We do not believe that the volatility caused by these unrealized gains and losses on our insured derivatives reflects the underlying economics of our business. We expect that our reported financial results will remain volatile and uncertain during the remainder of 2013 as a result of actual and perceived future performance of our insured credit derivatives and the perception of MBIA's credit risk. Our economic performance may also be volatile depending on changes in our loss estimates based on changes in macroeconomic conditions in the U.S. and abroad and deviations in collateral performance from our expectations.

For the three months ended September 30, 2013, we recorded consolidated net income of \$132 million or \$0.67 per diluted share compared with consolidated net income of \$7 million, or \$0.04 per diluted share for the same period of 2012.

For the nine months ended September 30, 2013, we recorded consolidated net income of \$118 million or \$0.60 per diluted share compared with consolidated net income of \$598 million or \$3.07 per diluted share, for the same period of 2012.

We also use adjusted pre-tax income (loss), a non-GAAP measure, to supplement our analysis of our periodic results. We consider adjusted pre-tax income (loss) a fundamental measure of periodic financial performance, which we believe is useful for an understanding of our results. Adjusted pre-tax income (loss) adjusts GAAP pre-tax income (loss) to remove the effects of consolidating insured variable interest entities ( VIEs ) and gains and losses related to insured credit derivatives, which we believe will reverse over time, as well as to add in changes in the present value of insurance claims we expect to pay on insured credit derivatives based on our ongoing insurance loss monitoring. Adjusted pre-tax income (loss) is not a substitute for and should not be viewed in isolation of GAAP pre-tax income (loss), and our definition of adjusted pre-tax income (loss) may differ from that used by other companies. Refer to the following Results of Operations section for a reconciliation of adjusted pre-tax income (loss) to GAAP pre-tax income (loss).

For the three months ended September 30, 2013, consolidated adjusted pre-tax loss was \$188 million compared with an adjusted pre-tax loss of \$118 million for the same period of 2012.

For the nine months ended September 30, 2013, consolidated adjusted pre-tax loss was \$368 million compared with an adjusted pre-tax loss of \$818 million for the same period of 2012.

Our consolidated shareholders' equity was \$3.2 billion as of September 30, 2013 and December 31, 2012. Our consolidated book value per share as of September 30, 2013 was \$16.54 compared with \$16.22 as of December 31, 2012.

In addition to book value per share, we also analyze adjusted book value ( ABV ) per share, a non-GAAP measure. We consider ABV a measure of fundamental value of the Company and the change in ABV an important measure of financial performance. ABV adjusts GAAP book value to remove the impact of certain items which the Company believes will reverse from GAAP book value over time through the GAAP statements of operations and GAAP statements of comprehensive income, as well as to add in the impact of certain items which the Company believes will be realized in GAAP book value in future periods. The Company has limited such adjustments to those items that it deems to be important to fundamental value and performance and which the likelihood and amount can be reasonably estimated. ABV assumes no new business activity. We have presented ABV to allow investors and analysts to evaluate the Company using the same measure that MBIA's management regularly uses to measure financial performance and value. ABV is not a substitute for and should not be viewed in isolation of GAAP book value, and our definition of ABV may differ from that used by other companies. Refer to the following Results of Operations section for a further discussion of ABV and a reconciliation of GAAP book value per share to ABV per share.

As of September 30, 2013, ABV per share was \$28.68, down from \$30.68 as of December 31, 2012.

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A detailed discussion of our financial results is presented within the Results of Operations section included herein. Refer to the Capital Resources Insurance Statutory Capital section for a discussion of National's and MBIA Corp.'s capital positions under statutory accounting principles ( U.S. STAT ).

### CRITICAL ACCOUNTING ESTIMATES

We prepare our financial statements in accordance with GAAP, which requires the use of estimates and assumptions. Management has discussed and reviewed the development, selection, and disclosure of critical accounting estimates with the Company's Audit Committee. Management believes that the most critical accounting estimates, since these estimates require significant judgment, are loss and LAE reserves, valuation of financial instruments, and deferred income taxes. Financial results could be materially different if other methodologies were used or if management modified its assumptions.



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**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

**CRITICAL ACCOUNTING ESTIMATES (continued)**

For a discussion of the Company's critical accounting estimates, see "Critical Accounting Estimates" in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012. In addition, refer to "Note 5: Loss and Loss Adjustment Expense Reserves" in the Notes to Consolidated Financial Statements for a current description of estimates used in our insurance loss reserving process.

**RECENT ACCOUNTING PRONOUNCEMENTS**

Refer to "Note 3: Recent Accounting Pronouncements" in the Notes to Consolidated Financial Statements for a discussion of accounting guidance recently adopted by the Company.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS***Summary of Consolidated Results*

The following table presents a summary of our consolidated financial results for the three and nine months ended September 30, 2013 and 2012:

In millions except for per share amounts	Three Months Ended		Nine Months Ended	
	September 30, 2013	September 30, 2012	September 30, 2013	September 30, 2012
Total revenues	\$ 420	\$ 281	\$ 751	\$ 1,703
Total expenses	249	338	629	944
Pre-tax income (loss)	171	(57)	122	759
Provision (benefit) for income taxes	39	(64)	4	161
Net income (loss)	\$ 132	\$ 7	\$ 118	\$ 598
Net income (loss) per common share:				
Basic	\$ 0.68	\$ 0.04	\$ 0.61	\$ 3.09
Diluted	\$ 0.67	\$ 0.04	\$ 0.60	\$ 3.07

For the three months ended September 30, 2013, we recorded consolidated net income of \$132 million, or \$0.67 per diluted common share, compared with consolidated net income of \$7 million, or \$0.04 per diluted common share, for the same period of 2012. Weighted average diluted common shares outstanding totaled 197 million and 195 million for the three months ended September 30, 2013 and 2012, respectively. Consolidated total revenues for the three months ended September 30, 2013 included \$257 million of net gains on insured derivatives compared with \$21 million of net losses for the same period of 2012. The net gains on insured derivatives in 2013 were principally the result of the effects of unfavorable changes in the market perception of MBIA Corp.'s nonperformance risk on its derivative liabilities and changes in spreads and pricing of underlying collateral and the weighted average life on transactions. The net losses on insured derivatives in 2012 were principally due to changes in spreads and pricing of underlying collateral and collateral erosion, partially offset by the effects of unfavorable changes in the market perception of MBIA Corp.'s nonperformance risk on its derivative liabilities. Consolidated total expenses for the three months ended September 30, 2013 included \$98 million of net insurance loss and LAE compared with \$171 million for the same period of 2012. The decrease in net insurance loss and LAE in 2013 when compared to 2012 was principally the result of lower increases in expected payments related to CMBS and first-lien RMBS transactions, partially offset by an increase in losses related to a gaming revenue transaction.

For the nine months ended September 30, 2013, we recorded consolidated net income of \$118 million, or \$0.60 per diluted common share, compared with consolidated net income of \$598 million, or \$3.07 per diluted common share, for the same period of 2012. Weighted average diluted common shares outstanding totaled 198 million and 195 million for the nine months ended September 30, 2013 and 2012, respectively. Consolidated total revenues for the nine months ended September 30, 2013 included \$14 million of net gains on insured derivatives compared with \$1.1 billion of net gains for the same period of 2012. The net gains on insured derivatives in 2013 were principally the result of commuting derivative liabilities at prices below their fair values and changes in the weighted average life on transactions, partially offset by the effects of favorable changes in the market perception of MBIA Corp.'s nonperformance risk on its derivative liabilities. The net gains on insured derivatives in 2012 were principally the result of commuting derivative liabilities at prices below their fair values and the effects of unfavorable changes in the market perception of MBIA Corp.'s nonperformance risk on its derivative liabilities. Consolidated total expenses for the nine months ended September 30, 2013 included \$92 million of net insurance loss and LAE compared with \$330 million for the same period of 2012. The decrease in net insurance loss and LAE in 2013 when compared to 2012 was principally related to decreases in actual and expected payments related to insured second-lien RMBS and first-lien RMBS transactions, partially offset by an increase in losses related to an international road transaction and certain U.S. public finance transactions. In addition, consolidated total expenses for the nine months ended September 30, 2013 included operating expenses of approximately \$89 million related to settlement, consulting and legal expenses associated with the resolution of litigation matters with Bank of America, Societe Generale and Flagstar Bank.

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Included in our consolidated net income for the three months ended September 30, 2013 and 2012 was \$18 million and \$59 million, respectively, of income before income taxes related to consolidated VIEs, after the elimination of intercompany revenues and expenses. Included in our consolidated net income for the nine months ended September 30, 2013 and 2012 was \$130 million and \$26 million, respectively, of income before income taxes related to consolidated VIEs, after the elimination of intercompany revenues and expenses. The net effect of consolidated VIEs on our financial results will vary over time as VIEs are consolidated or deconsolidated by the Company, and as the values of consolidated VIE assets and liabilities change.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

**RESULTS OF OPERATIONS (continued)**

***European Sovereign Debt Exposure***

Uncertainties regarding the European sovereign debt crisis have affected the global economy. Outside the U.S., financial guarantee insurance has been used by issuers of sovereign-related and sub-sovereign bonds, structured finance securities, utility debt and financing for public purpose projects, among others. MBIA does not insure any direct European sovereign debt. However, we do insure both structured finance and public finance obligations in select international markets. MBIA's indirect European sovereign insured debt exposure totaled \$8.0 billion as of September 30, 2013 and included obligations of sovereign-related and sub-sovereign issuers, such as regions, departments, and sovereign-owned entities that are supported by a sovereign state, region or department. Of the \$8.0 billion of insured gross par outstanding, \$817 million, \$491 million, and \$258 million related to Spain, Portugal, and Ireland, respectively. The remaining \$6.4 billion related to the U.K. We closely monitor our existing insured European portfolios on an ongoing basis. We consider country risk, including economic and political factors, the type and quality of local regulatory oversight, the strength of the legal framework in each country and the stability of the local institutional framework. We also monitor local accounting, regulatory and legal requirements, local financial market developments, the impact of exchange rates and local demand dynamics. The Company has an immaterial amount of direct and indirect European sovereign debt holdings included in its investment portfolios. A default by one or more sovereign issuers could have an adverse effect on our insured debt exposures.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)*****Adjusted Pre-Tax Income***

In addition to the above results, we also analyze the operating performance of the Company using adjusted pre-tax income (loss), a non-GAAP measure. We believe adjusted pre-tax income (loss), as used by management, is useful for an understanding of the results of operations of the Company. Adjusted pre-tax income (loss) is not a substitute for pre-tax income (loss) determined in accordance with GAAP, and our definition of adjusted pre-tax income (loss) may differ from that used by other companies.

For the three months ended September 30, 2013, our consolidated adjusted pre-tax loss increased when compared with the same period of 2012 primarily as a result of decreases in premiums earned and net investment income, an increase in impairments on insured credit derivatives, losses and LAE related to a gaming revenue transaction, and an impairment charge related to our Armonk, New York facility. This increase was partially offset by decreases in other insurance losses and LAE as a result of a lower increase in the expected payments related to CMBS and first-lien RMBS transactions.

For the nine months ended September 30, 2013, our consolidated adjusted pre-tax loss decreased when compared with the same period of 2012 primarily as a result of a decrease in insurance losses and LAE, the absence of net investment losses related to other-than-temporary impairments, net gains from the sale of investments and a decrease in interest expense. These changes were partially offset by lower premiums earned and lower net investment income. In addition, our consolidated adjusted pre-tax loss for the nine months ended September 30, 2013 included operating expenses of approximately \$89 million related to settlement, consulting and legal expenses associated with the resolution of litigation matters with Bank of America, Societe Generale and Flagstar Bank.

The following table presents our consolidated adjusted pre-tax income (loss) (a non-GAAP measure) and provides a reconciliation of adjusted pre-tax income (loss) to GAAP pre-tax income (loss) for the three and nine months ended September 30, 2013 and 2012:

In millions	Three Months Ended		Nine Months Ended	
	September 30, 2013	September 30, 2012	September 30, 2013	September 30, 2012
Adjusted pre-tax income (loss)	\$ (188)	\$ (118)	\$ (368)	\$ (818)
Additions to adjusted pre-tax income (loss):				
Impact of consolidating certain VIEs	20	29	18	62
Mark-to-market gains (losses) on insured credit derivatives	285	(33)	1,562	1,473
Subtractions from adjusted pre-tax income (loss):				
Impairments on insured credit derivatives	(54)	(65)	1,090	(42)
Pre-tax income (loss)	\$ 171	\$ (57)	\$ 122	\$ 759

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)*****Adjusted Book Value***

As of September 30, 2013, ABV per share (a non-GAAP measure) was \$28.68, down from \$30.68 as of December 31, 2012. The decrease in ABV per share was primarily driven by insurance losses and credit impairments, a decline in future installment premiums related to insured credit derivatives that were commuted during the period and an increase in operating expenses.

The following table provides a reconciliation of consolidated book value per share to consolidated ABV per share:

<b>In millions except share and per share amounts</b>	<b>As of September 30, 2013</b>	<b>As of December 31, 2012</b>
Total shareholders' equity of MBIA Inc.	\$ 3,180	\$ 3,173
Common shares outstanding	192,252,644	195,671,509
Book value per share	\$ 16.54	\$ 16.22
Adjustments for items included in book value per share (after-tax):		
Cumulative net loss from consolidating certain VIEs <sup>(1)</sup>	0.59	0.59
Cumulative unrealized loss on insured credit derivatives	4.59	9.70
Net unrealized (gains) losses included in other comprehensive income	0.12	(0.47)
Adjustments for items not included in book value per share (after-tax):		
Net unearned premium revenue <sup>(2)(3)</sup>	8.74	9.92
Present value of insured derivative installment revenue <sup>(4)</sup>	0.25	0.60
Cumulative impairments on insured credit derivatives <sup>(4)</sup>	(1.22)	(4.85)
Deferred acquisition costs	(0.93)	(1.03)
<b>Total adjustments per share</b>	<b>12.14</b>	<b>14.46</b>
<b>Adjusted book value per share</b>	<b>\$ 28.68</b>	<b>\$ 30.68</b>

(1) - Represents the impact on book value per share of consolidated VIEs that are not considered a business enterprise of the Company.

(2) - Consists of financial guarantee premiums and fees.

(3) - The discount rate on financial guarantee installment premiums was the risk-free rate as defined by the accounting principles for financial guarantee insurance contracts.

(4) - The discount rate on insured derivative installment revenue and impairments was 5% as of September 30, 2013 and December 31, 2012.

Our Net unearned premium revenue adjustment to book value per share consists of unearned premium revenue net of prepaid reinsurance premiums related to financial guarantee insurance contracts, the unamortized portion of installment premiums collected on insured derivative contracts, and the unamortized portion of insurance-related deferred fee revenue. Our Present value of insured derivative installment revenue adjustment to book value per share consists of the present value of premiums not yet collected from insured derivative contracts, which are not

recorded on our balance sheet in accordance with accounting principles for financial guarantee insurance contracts but which are contractually due to the Company.

***U.S. Public Finance Insurance***

Our U.S. public finance insurance business is primarily conducted through National. The financial guarantees issued by National provide unconditional and irrevocable guarantees of the payment of the principal of, and interest or other amounts owing on, insured obligations when due or, in the event National has exercised, at its discretion, the right to accelerate the payment under its policies upon the acceleration of the underlying insured obligations due to default or otherwise. National's guarantees insure municipal bonds, including tax-exempt and taxable indebtedness of U.S. political subdivisions, as well as utility districts, airports, healthcare institutions, higher educational facilities, student loan issuers, housing authorities and other similar agencies and obligations issued by private entities that finance projects that serve a substantial public purpose. Municipal bonds and privately issued bonds used for the financing of public purpose projects are generally supported by taxes, assessments, user fees or tariffs related to the use of these projects, lease payments or other similar types of revenue streams.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

The following table presents our U.S. public finance insurance segment results for the three and nine months ended September 30, 2013 and 2012:

In millions	Three Months Ended September 30,		Percent Change	Nine Months Ended September 30,		Percent Change
	2013	2012		2013	2012	
Net premiums earned	\$ 75	\$ 134	-44%	\$ 280	\$ 370	-24%
Net investment income	26	56	-54%	110	167	-34%
Fees and reimbursements	2	2	-%	5	5	-%
Net gains (losses) on financial instruments at fair value and foreign exchange	-	22	-100%	30	43	-30%
Other net realized gains (losses)	(29)	-	n/m	(29)	-	n/m
Total revenues	74	214	-65%	396	585	-32%
Losses and loss adjustment	35	4	n/m	105	15	n/m
Amortization of deferred acquisition costs	16	26	-38%	59	75	-21%
Operating	17	20	-15%	70	128	-45%
Total expenses	68	50	36%	234	218	7%
Pre-tax income	\$ 6	\$ 164	-96%	\$ 162	\$ 367	-56%

n/m - Percent change not meaningful.

For the three and nine months ended September 30, 2013 and 2012, we did not write a meaningful amount of U.S. public finance insurance. The lack of insurance writings in our U.S. public finance segment reflects the insurance financial strength credit ratings assigned to National by major rating agencies and the impact of litigation over the formation of National in 2009. Subsequent to the BofA Settlement Agreement and the Societe Generale settlement, all litigation brought originally by the group of eighteen domestic and international financial institutions relating to the establishment of National has been resolved. In addition, during 2013, the National Secured Loan was repaid in full, S&P upgraded National's rating twice to the current rating of A with a stable outlook, and Moody's upgraded National's rating to Baa1 from Baa2 with a positive outlook. We are seeking ratings upgrades from the rating agencies as we believe the current ratings of National do not fully represent the financial strength of National compared with other companies in its industry. We do not expect to write a material amount of new business prior to an upgrade of our insurance financial strength ratings. The timing of any rating upgrade is uncertain and will depend on a variety of quantitative and qualitative factors used by the rating agencies in their evaluation. National maintains underwriting criteria for most municipal risk types and expects opportunities for new business across the spectrum of municipal sectors.

**NET PREMIUMS EARNED** Net premiums earned on non-derivative financial guarantees represent gross premiums earned net of premiums ceded to reinsurers, and include scheduled premium earnings and premium earnings from refunded issues. For the three months ended September 30, 2013, U.S. public finance net premiums earned were \$75 million compared with \$134 million for the same period of 2012. The decrease in 2013 resulted from a decrease in refunded premiums earned of \$56 million and a decrease of \$3 million in scheduled premiums earned. For the nine months ended September 30, 2013, U.S. public finance net premiums earned were \$280 million compared with \$370 million for the same period of 2012. The decrease in 2013 resulted from a decrease in refunded premiums earned of \$79 million and a decrease



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in scheduled premiums earned of \$11 million. Scheduled premium earnings declined due to the maturity of insured issues within our U.S. public finance portfolio with no material new insurance writings. Refundings have experienced a decline when compared to the prior periods due to an overall decrease in municipal market issuance. Refunding activity over the past several years has accelerated premium earnings in prior periods and reduced the amount of premiums that would have been earned in the current period.

**NET INVESTMENT INCOME** The decrease in net investment income for the three and nine months ended September 30, 2013 compared with the same periods of 2012 was primarily due to a higher balance in lower yielding short-term assets generated from the repayment of the National Secured Loan in May of 2013. The interest income on the National Secured Loan for the nine months ended September 30, 2013 totaled \$41 million compared with \$74 million for the same period of 2012. In connection with the BofA Settlement Agreement, MBIA Corp. repaid the remaining outstanding balance and accrued interest on the National Secured Loan in May of 2013. Refer to the Liquidity section included herein for additional information about the National Secured Loan.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

Investment asset balances at amortized cost as of September 30, 2013 and December 31, 2012 are presented in the following table:

In millions	September 30, 2013		December 31, 2012	
	Investments at Amortized Cost	Pre-tax Yield <sup>(1)</sup>	Investments at Amortized Cost	Pre-tax Yield <sup>(1)</sup>
Fixed-income securities:				
Tax-exempt	\$ 342	3.87%	\$ 417	3.98%
Taxable	3,258	3.43%	2,378	2.98%
Short-term	1,002	0.24%	204	1.17%
Total fixed-income	4,602	2.76%	2,999	2.99%
Secured loan to an affiliate	-		1,652	
Other	11		16	
Total	\$ 4,613		\$ 4,667	

(1) - Estimated yield-to-maturity.

**NET GAINS (LOSSES) ON FINANCIAL INSTRUMENTS AT FAIR VALUE AND FOREIGN EXCHANGE** The decrease in net gains (losses) on financial instruments at fair value and foreign exchange for the three months ended September 30, 2013 compared with the same period of 2012 was principally due to a decrease in net realized gains from the sales of securities from the ongoing management of our U.S. public finance insurance investment portfolio. The decrease in net gains (losses) on financial instruments at fair value and foreign exchange for the nine months ended September 30, 2013 compared with the same period of 2012 was primarily driven by losses from fair valuing financial instruments.

**OTHER NET REALIZED GAINS (LOSSES)** Other net realized gains (losses) for the three and nine months ended September 30, 2013 included an impairment charge of \$29 million related to our Armonk, New York facility.

**LOSS AND LOSS ADJUSTMENT EXPENSES** National's portfolio surveillance group is responsible for monitoring our U.S. public finance segment's insured obligations. The level and frequency of monitoring of any insured obligation depends on the type, size, rating and performance of the insured issue. Refer to Note 5: Loss and Loss Adjustment Expense Reserves in the Notes to Consolidated Financial Statements for a description of the Company's loss reserving policy and additional information related to its loss reserves.

The following table presents information about our U.S. public finance insurance loss and LAE expenses for the three and nine months ended September 30, 2013 and 2012:

In millions	Three Months Ended		Percent Change	Nine Months Ended		Percent Change
	September 30, 2013	September 30, 2012		September 30, 2013	September 30, 2012	

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Loss and LAE related to actual and expected payments	\$ (24)	\$ (10)	140%	\$ 86	\$ 57	51%
Recoveries of actual and expected payments	59	14	n/m	20	(42)	-148%
Gross losses incurred	35	4	n/m	106	15	n/m
Reinsurance	-	-	-%	(1)	-	n/m
Losses and loss adjustment expenses	\$ 35	\$ 4	n/m	\$ 105	\$ 15	n/m

n/m - Percent change not meaningful.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

Losses and LAE for the three and nine months ended September 30, 2013, included the loss related to the difference in the value of the salvage receivable recorded and the fair market value of the marketable securities received in connection with the restructuring of a gaming revenue transaction. We expect to recover the full value of the original salvage receivable in the future with the securities received as a result of this transaction. Under U.S. STAT, this salvage receivable continues to be reflected as a component of National's loss reserves. U.S. STAT differs from GAAP in certain respects. Refer to Note 11: Statutory Accounting Practices in the Notes to Consolidated Financial Statements of National within exhibit 99.1 of MBIA Inc.'s Annual Report on Form 10-K for the year ended December 31, 2012 for an explanation of the differences between U.S. STAT and GAAP. Losses and LAE related to actual and expected payments for the three months ended September 30, 2013 and 2012 are driven by lower expected future payments based on National's remediation efforts. In addition, losses and LAE for the nine months ended September 30, 2013, included losses primarily related to certain general obligation bonds. For the three and nine months ended September 30, 2012, losses and LAE primarily related to certain general obligation bonds.

Certain local governments remain under extreme financial and budgetary stress and several have filed for protection under the United States Bankruptcy Code, or have entered into state statutory proceedings established to assist municipalities in managing through periods of severe fiscal stress. This could lead to an increase in defaults by such entities on the payment of their obligations and losses or impairments on a greater number of our insured transactions. We continue to monitor and analyze these situations very closely, however the overall extent and duration of these events is uncertain.

The following tables present information about our U.S. public finance insurance loss and LAE reserves and recoverables as of September 30, 2013 and December 31, 2012:

In millions	September 30, 2013	December 31, 2012	Percent Change
Gross loss and LAE reserves	\$ 212	\$ 267	-21%
Expected recoveries on unpaid losses	(118)	(108)	9%
Loss and LAE reserves	\$ 94	\$ 159	-41%
Insurance loss recoverable	\$ 17	\$ 256	-93%
Insurance loss recoverable-ceded <sup>(1)</sup>	\$ -	\$ 7	-100%
Reinsurance recoverable on paid and unpaid losses <sup>(2)</sup>	\$ 1	\$ 8	-88%

(1) - Reported within Other liabilities on our consolidated balance sheets.

(2) - Reported within Other assets on our consolidated balance sheets.

Loss and LAE reserves as of September 30, 2013 decreased when compared with December 31, 2012 primarily related to the Allegheny Health, Education and Research Foundation transaction discussed below, partially offset by increases in certain general obligation bonds reserves.

Insurance loss recoverable as of September 30, 2013 decreased when compared with December 31, 2012 primarily related to the receipt of salvage in connection with the restructuring of a gaming revenue transaction.

Included in our U.S. public finance loss and LAE reserves are both reserves for insured obligations for which a payment default has occurred and National has already paid a claim and also for which a payment default has not yet occurred but a claim is expected in the future. As of

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September 30, 2013 and 2012, loss and LAE reserves comprised the following:

\$ in millions	Number of Issues <sup>(1)</sup>		Loss and LAE Reserve		Par Outstanding	
	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
Gross of reinsurance:						
Issues with defaults	7	9	\$ 81	\$ 141	\$ 732	\$ 749
Issues without defaults	8	9	13	18	102	113
Total gross of reinsurance	15	18	\$ 94	\$ 159	\$ 834	\$ 862

(1) - An issue represents the aggregate of financial guarantee policies that share the same revenue source for purposes of making debt service payments. On July 9, 2013, the Company and the Pennsylvania Higher Educational Facilities Authority gave direction to the trustee under each of the indentures for the three Allegheny Health, Education and Research Foundation Bond series to exercise the right of optional redemption at par plus accrued interest. These bonds were redeemed during the third quarter of 2013, the insurance policies were returned to National and \$118 million of gross insured par was eliminated.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

POLICY ACQUISITION COSTS AND OPERATING EXPENSES U.S. public finance insurance segment expenses for the three and nine months ended September 30, 2013 and 2012 are presented in the following table:

In millions	Three Months Ended September 30,		Percent Change	Nine Months Ended September 30,		Percent Change
	2013	2012		2013	2012	
Gross expenses	\$ 17	\$ 20	-15%	\$ 70	\$ 128	-45%
Amortization of deferred acquisition costs	\$ 16	\$ 26	-38%	\$ 59	\$ 75	-21%
Operating	17	20	-15%	70	128	-45%
Total insurance operating expenses	\$ 33	\$ 46	-28%	\$ 129	\$ 203	-36%

Gross expenses represent total insurance expenses before the deferral of any policy acquisition costs. Gross expenses decreased for the three months ended September 30, 2013 compared with the same period of 2012 primarily due to decreases in legal and litigation related costs. Gross expenses decreased for the nine months ended September 30, 2013 compared with the same period of 2012 as a result of decreases in legal and litigation related costs partially offset by an increase in consulting fees. We did not defer a material amount of policy acquisition costs during 2013 or 2012.

**INSURED PORTFOLIO EXPOSURE** Financial guarantee insurance companies use a variety of approaches to assess the underlying credit risk profile of their insured portfolios. MBIA uses both an internally developed credit rating system as well as third-party rating sources in the analysis of credit quality measures of its insured portfolio. In evaluating credit risk, we obtain, when available, the underlying rating of the insured obligation before the benefit of its insurance policy from nationally recognized rating agencies, Moody's and S&P. Other companies within the financial guarantee industry may report credit quality information based upon internal ratings that would not be comparable to our presentation.

The following table presents the credit quality distribution of MBIA's U.S. public finance outstanding gross par insured as of September 30, 2013 and December 31, 2012. Capital appreciation bonds are reported at the par amount at the time of issuance of the insurance policy. All ratings are as of the period presented and represent S&P ratings. If transactions are not rated by S&P, a Moody's equivalent rating is used. If transactions are not rated by either S&P or Moody's, an internal equivalent rating is used.

In millions	Gross Par Outstanding			
	September 30, 2013		December 31, 2012	
Rating	Amount	%	Amount	%
AAA	\$ 15,813	5.4%	\$ 18,518	5.5%
AA	140,279	48.1%	162,504	48.2%
A	105,966	36.4%	122,743	36.4%
BBB	24,737	8.5%	30,496	9.0%
Below investment grade	4,643	1.6%	2,853	0.9%
Total	\$ 291,438	100.0%	\$ 337,114	100.0%

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The credit quality distribution of our U.S. public finance insurance exposure as of September 30, 2013 remained relatively consistent with December 31, 2012. Total U.S. public finance insurance gross par outstanding rated A or above, before giving effect to National's guarantee, was approximately 90% and gross par outstanding rated below investment grade, before giving effect to National's guarantee, was less than 2% as of September 30, 2013 and less than 1% as of December 31, 2012.

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**Table of Contents**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

**RESULTS OF OPERATIONS (continued)**

***Structured Finance and International Insurance***

Our structured finance and international insurance business is principally conducted through MBIA Corp. The financial guarantees issued by MBIA Corp. generally provide unconditional and irrevocable guarantees of the payment of the principal of, and interest or other amounts owing on, insured obligations when due or, in the event MBIA Corp. has the right, at its discretion, to accelerate the payment under its policies upon the acceleration of the underlying insured obligations due to default or otherwise. Certain guaranteed investment contracts written by MBIA Inc. or its subsidiaries are insured by MBIA Corp. If MBIA Inc. or such subsidiaries were to have insufficient assets to pay amounts due upon maturity or termination, MBIA Corp. would make such payments under its insurance policies. MBIA Corp. also insured debt obligations of other affiliates, including MBIA Global Funding, LLC ( "GFL" ) and Meridian Funding Company, LLC ( "Meridian" ). MBIA Corp. has also written insurance policies guaranteeing the obligations under CDS contracts of an affiliate, LaCrosse Financial Products, LLC, including termination payments that may become due upon certain events including the insolvency or payment default of the financial guarantor or the CDS issuer. MBIA Insurance Corporation also provides reinsurance to its insurance subsidiaries.

MBIA Corp.'s guarantees insure structured finance and asset-backed obligations, privately issued bonds used for the financing of public purpose projects that are primarily located outside of the U.S. which include toll roads, bridges, airports, public transportation facilities, utilities and other types of infrastructure projects serving a substantial public purpose, and obligations of sovereign-related and sub-sovereign issuers. Structured finance and ABS typically are securities repayable from expected cash flows generated by a specified pool of assets, such as residential and commercial mortgage loans, insurance policies, consumer loans, corporate loans and bonds, trade and export receivables, and leases and loans for equipment, aircraft and real property.

In certain cases, we may be required to consolidate entities established by issuers of insured obligations as part of securitizations when we insure the assets or liabilities of those entities and in connection with remediations under our insurance policies. These entities typically meet the definition of a VIE under accounting principles for the consolidation of VIEs. We do not believe there is any difference in the risks and profitability of financial guarantees provided to VIEs compared with other financial guarantees written by us.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

The following table presents our structured finance and international insurance segment results for the three and nine months ended September 30, 2013 and 2012:

In millions	Three Months Ended September 30,		Percent	Nine Months Ended September 30,		Percent
	2013	2012	Change	2013	2012	Change
Net premiums earned	\$ 40	\$ 38	5%	\$ 111	\$ 143	-22%
Net investment income	3	8	-63%	12	22	-45%
Fees and reimbursements	18	43	-58%	65	109	-40%
Change in fair value of insured derivatives:						
Realized gains (losses) and other settlements on insured derivatives	(28)	12	n/m	(1,548)	(420)	n/m
Unrealized gains (losses) on insured derivatives	285	(33)	n/m	1,562	1,473	6%
Net change in fair value of insured derivatives	257	(21)	n/m	14	1,053	-99%
Net gains (losses) on financial instruments at fair value and foreign exchange	(3)	14	-121%	31	18	72%
Net investment losses related to other-than-temporary impairments	-	(4)	-100%	-	(45)	-100%
Other net realized gains (losses)	-	1	-100%	-	1	-100%
Revenues of consolidated VIEs:						
Net investment income	13	13	-%	38	40	-5%
Net gains (losses) on financial instruments at fair value and foreign exchange	15	42	-64%	119	(25)	n/m
Other net realized gains (losses)	-	-	-%	1	-	n/m
Total revenues	343	134	n/m	391	1,316	-70%
Losses and loss adjustment	63	167	-62%	(13)	315	-104%
Amortization of deferred acquisition costs	19	24	-21%	76	81	-6%
Operating	22	30	-27%	83	115	-28%
Interest	30	62	-52%	129	175	-26%
Expenses of consolidated VIEs:						
Operating	3	5	-40%	10	16	-38%
Interest	10	10	-%	30	32	-6%
Total expenses	147	298	-51%	315	734	-57%
Pre-tax income (loss)	\$ 196	\$ (164)	n/m	\$ 76	\$ 582	-87%

n/m - Percent change not meaningful.

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For the three and nine months ended September 30, 2013 and 2012, we did not write a meaningful amount of structured finance and international insurance. As of September 30, 2013, MBIA Corp.'s total insured gross par outstanding was \$83.9 billion. Since December 31 2007, our total gross par outstanding has decreased approximately 75% from \$331.2 billion. The lack of insurance writings in our structured finance and international insurance segment reflects the insurance financial strength credit ratings assigned to MBIA Corp. by the major rating agencies. The Company does not expect to write a material amount of new business prior to an upgrade of the insurance financial strength ratings of MBIA Corp. and market acceptance that such ratings will be stable in the future. The timing of any future upgrades is uncertain and will depend on a variety of quantitative and qualitative factors used by the rating agencies in their evaluation. Pre-tax income (loss) in each of the periods included in the preceding table was primarily driven by changes in the fair value of our insured credit derivatives, which reflects changes in the market perception of MBIA Corp.'s credit risk.

**ADJUSTED PRE-TAX INCOME (LOSS)** In addition to the above results, we also analyze the operating performance of our structured finance and international insurance segment using adjusted pre-tax income (loss), a non-GAAP measure. We believe adjusted pre-tax income (loss), as used by management, is useful for an understanding of the results of operations of our structured finance and international insurance segment. Adjusted pre-tax income (loss) is not a substitute for pre-tax income (loss) determined in accordance with GAAP, and our definition of adjusted pre-tax income (loss) may differ from that used by other companies.

Adjusted pre-tax loss for the three months ended September 30, 2013 decreased when compared with the same period of 2012 principally due to decreases in financial guarantee insurance losses and interest expense from the National Secured Loan, which was repaid in full in May of 2013. These changes were partially offset by an increase in impairments on insured credit derivatives.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

Adjusted pre-tax loss for the nine months ended September 30, 2013 decreased when compared with the same period of 2012 principally due to a decrease in financial guarantee insurance losses, an increase in gains on sales of investments, a decrease in interest expense from the National Secured Loan and the absence of net investment losses related to other-than-temporary impairments.

The following table presents the adjusted pre-tax income (loss) of our structured finance and international insurance segment and a reconciliation of adjusted pre-tax income (loss) to GAAP pre-tax income (loss) for the three and nine months ended September 30, 2013 and 2012:

<b>In millions</b>	<b>Three Months Ended September 30,</b>			<b>Nine Months Ended September 30,</b>		
	<b>2013</b>	<b>2012</b>	<b>Percent Change</b>	<b>2013</b>	<b>2012</b>	<b>Percent Change</b>
Adjusted pre-tax income (loss)	\$ (167)	\$ (224)	-25%	\$ (357)	\$ (970)	-63%
Additions to adjusted pre-tax income (loss):						
Impact of consolidating certain VIEs	24	28	-14%	(39)	37	n/m
Mark-to-market gain (loss) on insured credit derivatives	285	(33)	n/m	1,562	1,473	6%
Subtractions from adjusted pre-tax income (loss):						
Impairments on insured credit derivatives	(54)	(65)	-17%	1,090	(42)	n/m
Pre-tax income (loss)	\$ 196	\$ (164)	n/m	\$ 76	\$ 582	-87%

n/m - Percent change not meaningful.

**NET PREMIUMS EARNED** Our structured finance and international insurance segment generates net premiums from insurance policies accounted for as financial guarantee contracts and insured derivative contracts, and certain of those premiums may be eliminated in our consolidated financial statements as a result of the Company consolidating VIEs. The following table provides net premiums earned by type of insurance contract for the three and nine months ended September 30, 2013 and 2012:

<b>In millions</b>	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Net premiums earned:				
Financial guarantee contracts	\$ 40	\$ 38	\$ 111	\$ 143
Insured derivative contracts <sup>(1)</sup>	6	12	28	42
VIEs (eliminated in consolidation)	4	4	11	11
Total net premiums earned	\$ 50	\$ 54	\$ 150	\$ 196

(1) -

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Premiums related to insured derivatives are included in Realized gains (losses) and other settlements on insured derivatives on our consolidated statements of operations.

Net premiums earned on non-derivative financial guarantee contracts for the three and nine months ended September 30, 2013 and 2012 are presented in the following table. Net premiums earned represent gross premiums earned net of premiums ceded to reinsurers, and include scheduled premium earnings and premium earnings from refunded issues.

In millions	Three Months Ended September 30,		Percent Change	Nine Months Ended September 30,		Percent Change
	2013	2012		2013	2012	
Net premiums earned:						
U.S.	\$ 12	\$ 14	-14%	\$ 37	\$ 50	-26%
Non-U.S.	28	24	17%	74	93	-20%
Total net premiums earned	\$ 40	\$ 38	5%	\$ 111	\$ 143	-22%

Structured finance and international net premiums earned decreased for the nine months ended September 30, 2013 when compared with the same period of 2012 primarily due to the maturity and early settlement of insured transactions with no material writings of new insurance policies.

**NET INVESTMENT INCOME** The decrease in net investment income for the three and nine months ended September 30, 2013 compared with the same periods of 2012 was primarily due to declining average asset balances in 2013 due to sales of investments to fund claim and commutation payments.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

Investment asset balances at amortized cost as of September 30, 2013 and December 31, 2012 are presented in the following table:

In millions	September 30, 2013		December 31, 2012	
	Investments		Investments	
	at	Pre-tax	at	Pre-tax
	Amortized Cost	Yield <sup>(1)</sup>	Amortized Cost	Yield <sup>(1)</sup>
Fixed-income securities:				
Taxable	\$ 316	2.10%	\$ 725	1.60%
Short-term	206	1.16%	160	1.38%
Total fixed-income	522	1.73%	885	1.56%
Other	2		1	
Total	\$ 524		\$ 886	

(1) - Estimated yield-to-maturity.

**FEES AND REIMBURSEMENTS** The decrease in fees and reimbursements for the three and nine months ended September 30, 2013 compared with the same periods of 2012 was primarily due to a decrease in waiver and consent fees related to the ongoing management of our structured finance and international insurance business.

**NET CHANGE IN FAIR VALUE OF INSURED DERIVATIVES** The following table presents the net premiums and fees earned related to derivatives and the components of the net change in fair value of insured derivatives for the three and nine months ended September 30, 2013 and 2012:

In millions	Three Months Ended			Nine Months Ended		
	September 30, 2013	September 30, 2012	Percent Change	September 30, 2013	September 30, 2012	Percent Change
Net premiums and fees earned on insured derivatives	\$ 6	\$ 12	-50%	\$ 29	\$ 43	-33%
Realized gains (losses) on insured derivatives	(34)	-	n/m	(1,577)	(463)	n/m
Realized gains (losses) and other settlements on insured derivatives	(28)	12	n/m	(1,548)	(420)	n/m
Unrealized gains (losses) on insured derivatives	285	(33)	n/m	1,562	1,473	6%
Net change in fair value of insured derivatives	\$ 257	\$ (21)	n/m	\$ 14	\$ 1,053	-99%

n/m - Percent change not meaningful.

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The Company no longer insures new credit derivative contracts except in transactions related to the restructuring or reduction of existing derivative exposure. Premiums earned related to insured credit derivatives will decrease over time as a result of settlements prior to maturity and scheduled amortizations. For the three months ended September 30, 2013, realized losses on insured derivatives resulted primarily from claim payments on CMBS transactions. For the nine months ended September 30, 2013 and 2012, realized losses on insured derivatives resulted primarily from settlements and claim payments on CMBS and ABS transactions.

For the three months ended September 30, 2013, unrealized gains on insured derivatives were principally associated with the effects of MBIA Corp.'s nonperformance risk on its derivative liabilities, favorable changes in spreads and pricing on the underlying collateral and a decline in the weighted average life on transactions. For the three months ended September 30, 2012, unrealized losses on insured derivatives were principally associated with unfavorable changes in spreads and pricing on the underlying collateral and collateral erosion of transactions, partially offset by a widening of MBIA Corp.'s credit spreads and a reduction in MBIA Corp.'s recovery rate.

For the nine months ended September 30, 2013, unrealized gains on insured derivatives were principally associated with the reversal of unrealized losses from commutations, a decline in the weighted average life on transactions and favorable changes in spread/prices on the underlying collateral, partially offset by the effects of MBIA Corp.'s nonperformance risk on its derivative liabilities and collateral erosion of transactions. For the nine months ended September 30, 2012, unrealized gains on insured derivatives were principally associated with the reversal of unrealized losses from commutations, the effects of MBIA Corp.'s nonperformance risk on its derivative liabilities and the result of favorable movements in spreads and pricing on collateral within transactions, partially offset by collateral erosion.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

As of September 30, 2013, MBIA Corp.'s five year CDS cost was 16.38% upfront plus 5% per annum compared with 35.88% upfront plus 5% per annum as of September 30, 2012. Our mark-to-market on insured credit derivatives uses the most appropriate of the one to ten year CDS cost for each transaction, and those costs ranged from 4.13% upfront plus 5% per annum to 20.63% upfront plus 5% per annum as of September 30, 2013. As of September 30, 2012, those costs ranged from 17.75% upfront plus 5% per annum to 38.25% upfront plus 5% per annum.

As of September 30, 2013, we had \$25.8 billion of gross par outstanding on insured credit derivatives compared with \$26.9 billion and \$47.5 billion as of June 30, 2013 and December 31, 2012, respectively. The decrease in gross par outstanding was primarily due to contractual terminations, amortizations and maturities. During the three months ended September 30, 2013, three insured issues, representing \$1.2 billion in gross par outstanding, either matured or were contractually settled. During the nine months ended September 30, 2013, 36 insured issues, representing \$21.3 billion in gross par outstanding, either matured, contractually settled or were agreed to be contractually settled prior to maturity.

Since our insured credit derivatives have similar terms, conditions, risks, and economic profiles as our financial guarantee insurance policies, we evaluate them for impairment periodically in the same way that we estimate loss and LAE for our financial guarantee policies. Credit impairments on insured derivatives represent actual payments plus the present values of our estimates of expected future claim payments, net of expected future recoveries. MBIA Insurance Corporation's expected future claim payments were discounted using a rate of 5.72%, the same rate used to calculate its statutory loss reserves as of September 30, 2013. We estimated that additional credit impairments on insured derivatives (excluding LAE) for the nine months ended September 30, 2013 were \$483 million across 12 insured CDO issues. Beginning with the fourth quarter of 2007 through September 30, 2013, total credit impairments on insured derivatives were estimated at \$6.1 billion across 74 insured CDO issues, inclusive of 71 insured issues for which we made settlement and claim payments of \$5.8 billion, net of reinsurance and collections. Accordingly, we expect to realize additional net losses of \$337 million. Refer to the following "Loss and Loss Adjustment Expenses" section for additional information about credit impairments on insured derivatives.

Our estimate of credit impairments, a non-GAAP measure, may differ from the fair values recorded in our consolidated financial statements. The Company believes its disclosure of credit impairments on insured derivatives provides additional meaningful information about potential realized losses on these contracts. The fair value of an insured derivative contract will be influenced by a variety of market and transaction-specific factors that may be unrelated to potential future claim payments. In the absence of credit impairments or the termination of derivatives at losses, the cumulative unrealized losses recorded from fair valuing insured derivatives should reverse before or at the maturity of the contracts. Contracts also may be settled prior to maturity at amounts that may be more or less than their recorded fair values. Those settlements can result in realized gains or losses, and will result in the reversal of unrealized gains or losses. The Company is not required to post collateral to counterparties of these contracts. Refer to "Risk Factors" in Part II, Item 1A of this Quarterly Report on Form 10-Q for the quarterly period year ended September 30, 2013 for information on legislative changes that could require collateral posting by MBIA Corp. notwithstanding the contract terms.

**NET GAINS (LOSSES) ON FINANCIAL INSTRUMENTS AT FAIR VALUE AND FOREIGN EXCHANGE** The decrease in net gains (losses) on financial instruments at fair value and foreign exchange for the three months ended September 30, 2013 when compared with the same period of 2012 was primarily due to an increase in losses from foreign exchange. The increase in net gains (losses) on financial instruments at fair value and foreign exchange for the nine months ended September 30, 2013 when compared with the same period of 2012 was primarily due to net realized gains from the sales of securities.

**NET INVESTMENT LOSSES RELATED TO OTHER-THAN-TEMPORARY IMPAIRMENTS** Net investment losses related to other-than-temporary impairments for the three and nine months ended September 30, 2012 were primarily related to one impaired security that was written down to its fair value as it was our intent to sell the security before an expected recovery of fair value to its amortized cost. Refer to the "Liquidity" section included herein for additional information about impaired investments.

**REVENUES OF CONSOLIDATED VIEs** For the three months ended September 30, 2013, total revenues of consolidated VIEs were \$28 million compared with total revenues of \$55 million for the same period of 2012. The decrease in revenues of consolidated VIEs for the three

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months ended September 30, 2013 when compared to the same period of 2012 was primarily related to a decrease in net gains from second-lien RMBS put-back claims on ineligible mortgage loans and a decrease in net gains due to the movements of MBIA Corp. s nonperformance risk. For the nine months ended September 30, 2013, total revenues of consolidated VIEs were \$158 million compared with total revenues of \$15 million for the same period of 2012. The increase in revenues of consolidated VIEs for the nine months ended September 30, 2013 when compared to the same period of 2012 was primarily related to an increase in net gains from second-lien RMBS put-back claims on ineligible mortgage loans partially offset by a decrease in net gains due to the movements of MBIA Corp. s nonperformance risk.



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**Table of Contents**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

**RESULTS OF OPERATIONS (continued)**

LOSS AND LOSS ADJUSTMENT EXPENSES MBIA's insured portfolio management group within its structured finance and international insurance business is responsible for monitoring structured finance and international insured obligations. The level and frequency of monitoring of any insured issue depends on the type, size, rating and performance of the insured issue. If we identify concerns with respect to the performance of an insured issue we may designate such insured issue as Caution List-Low, Caution List-Medium, Caution List-High, or Classified depending on the likelihood of a loss. We establish case basis reserves in connection with insured issues designated as Classified credits.

The Company faces significant risks and uncertainties related to potential or actual losses from its CMBS and CRE CDO insured exposure, its second-lien RMBS insured exposure (due to the unpredictable performance of ineligible mortgage loans included in the transactions we insured) backed by home equity lines of credit ( HELOC ) or closed-end second mortgages ( CES ), its first-lien RMBS insured exposure and its ABS CDO insured exposure. Continued significant adverse developments and higher than expected payments on these exposures and/or lower than expected recoveries on the RMBS exposures, could result in a decline in the Company's liquidity and statutory capital position.

The impact of insured exposures on the Company's liquidity position is best understood by assessing the ultimate amount of payments that the Company will be required to make with respect to these exposures. In this regard, the Company discloses the discounted expected future net cash flows to be made under all insurance contracts, irrespective of the legal form of the guarantee (i.e., financial guarantee insurance policy or insured derivative contract) or the GAAP accounting basis.

All amounts presented in the following aggregate losses and LAE tables are calculated in accordance with GAAP, with the exception of those related to insured credit derivative impairments. The amounts reported for insured credit derivative impairments are calculated in accordance with U.S. STAT because GAAP does not contain a comparable measurement basis for these contracts. All losses and recoverables reported in the following tables are measured using discounted probability-weighted cash flows. Losses and recoverables on VIEs that are eliminated in consolidation are included because the consolidation of these VIEs does not impact whether or not we will be required to make payments under our insurance contracts. As a result of the different accounting bases of amounts included in the following tables, the total provided in each table represents a non-GAAP measure.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

The following tables present the aggregate loss and LAE reserves and insurance loss recoverables as of September 30, 2013 and December 31, 2012, and the aggregate change in the discounted values of net payments expected to be made on all insurance contracts for the three and nine months ended September 30, 2013 and 2012:

**Aggregate Losses and LAE Roll Forward**

<b>In millions</b>	<b>Financial Guarantee Insurance<sup>(1)</sup></b>	<b>Financial Guarantee Insurance Related to VIEs<sup>(2)</sup></b>	<b>Insurance Credit Derivative Impairments and LAE<sup>(3)</sup></b>	<b>Reinsurance<sup>(4)</sup></b>	<b>Total<sup>(5)</sup></b>
Gross loss and LAE reserves as of December 31, 2012	\$ 694	\$ 293	\$ 1,458	\$ (7)	\$ 2,438
Gross insurance loss recoverable as of December 31, 2012	(3,392)	(1,338)	(31)	6	(4,755)
Total reserves (recoverable) as of December 31, 2012	(2,698)	(1,045)	1,427	(1)	(2,317)
Ceded reserves	(1)	-	-	1	-
Net reserves as of December 31, 2012	(2,699)	(1,045)	1,427	-	(2,317)
Total aggregate losses and LAE incurred	(13)	(83)	483	-	387
(Payments) collections and other	2,580	53	(1,571)	-	1,062
Net reserves as of September 30, 2013	(132)	(1,075)	339	-	(868)
Ceded reserves	1	-	(1)	-	-
Total reserves (recoverable) as of September 30, 2013	\$ (131)	\$ (1,075)	\$ 338	\$ -	\$ (868)
Gross loss and LAE reserves as of September 30, 2013	\$ 594	\$ 240	\$ 368	\$ (6)	\$ 1,196
Gross insurance loss recoverable as of September 30, 2013	(725)	(1,315)	(30)	6	(2,064)
Total reserves (recoverable) as of September 30, 2013	\$ (131)	\$ (1,075)	\$ 338	\$ -	\$ (868)

(1) - Included in Losses and loss adjustment, Loss and loss adjustment expense reserves, and Insurance loss recoverable on the Company's consolidated financial statements.

(2) - Represents loss expense, reserves and insurance loss recoverable eliminated upon the consolidation of insured VIEs.

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(3) - Represents statutory losses and LAE and recoveries for insurance contracts accounted for as derivatives. Realized and unrealized gains and losses on these contracts under GAAP are recorded in Net change in fair value of insured derivatives on the Company's consolidated statements of operations and the fair value of these contracts are recorded in Derivative liabilities on the Company's consolidated balance sheets.

(4) - Represents Losses and loss adjustment, Loss and loss adjustment expense reserves and Insurance loss recoverable on the Company's consolidated financial statements and are ceded to third-party reinsurers under insurance contracts. As of December 31, 2012, there was a \$1 million receivable related to insured credit derivative impairments and LAE reinsurance.

(5) - Represents totals after ceding to third-party reinsurers under insurance contracts.

### Aggregate Losses and LAE (change in discounted values of net payments)

For the Three Months Ended September 30, 2013						
In millions	Second-lien RMBS (1)	First-lien RMBS	ABS CDO	CMBS	Other (2)	Total
Change in actual and expected payments	\$ (8)	\$ 14	\$ (10)	\$ 90	\$ 7	\$ 93
Change in actual and expected salvage	61	(6)	(2)	8	9	70
Total aggregate losses and LAE	\$ 53	\$ 8	\$ (12)	\$ 98	\$ 16	\$ 163

(1) - Includes HELOC loans and CES.

(2) - Primarily represents an international road transaction.

For the Three Months Ended September 30, 2012						
In millions	Second-lien RMBS (1)	First-lien RMBS	ABS CDO	CMBS	Other	Total
Change in actual and expected payments	\$ 60	\$ 46	\$ 21	\$ 131	\$ 3	\$ 261
Change in actual and expected salvage	(2)	1	5	(8)	(5)	(9)
Total aggregate losses and LAE	\$ 58	\$ 47	\$ 26	\$ 123	\$ (2)	\$ 252

(1) - Includes HELOC loans and CES.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)****Aggregate Losses and LAE (change in discounted values of net payments)**

In millions	For the Nine Months Ended September 30, 2013					Total
	Second-lien RMBS <sup>(1)</sup>	First-lien RMBS	ABS CDO	CMBS	Other <sup>(2)</sup>	
Change in actual and expected payments	\$ 126	\$ 12	\$ (90)	\$ 472	\$ 98	\$ 618
Change in actual and expected salvage	(262)	(11)	-	(13)	55	(231)
Total aggregate losses and LAE	\$ (136)	\$ 1	\$ (90)	\$ 459	\$ 153	\$ 387

(1) - Includes HELOC loans and CES.

(2) - Primarily represents an international road transaction and high yield corporate CDOs.

In millions	For the Nine Months Ended September 30, 2012					Total
	Second-lien RMBS <sup>(1)</sup>	First-lien RMBS	ABS CDO	CMBS	Other	
Change in actual and expected payments	\$ 266	\$ 101	\$ (22)	\$ 602	\$ 10	\$ 957
Change in actual and expected salvage	(7)	4	18	(13)	1	3
Total aggregate losses and LAE	\$ 259	\$ 105	\$ (4)	\$ 589	\$ 11	\$ 960

(1) - Includes HELOC loans and CES.

The decrease in total aggregate losses and LAE for the three months ended September 30, 2013 compared with the same period of 2012 was primarily due to lower increases in expected future payments on second-lien RMBS, CMBS, first-lien RMBS and ABS CDO exposures. Partially offsetting these decreases were changes in actual and expected salvage primarily related to lower recoveries resulting from ineligible mortgage loans included in insured second-lien RMBS exposures that are subject to contractual obligations by sellers/servicers to repurchase or replace such mortgage loans.

The decrease in total aggregate losses and LAE for the nine months ended September 30, 2013 compared with the same period of 2012 was primarily due to lower increases in expected future payments on second-lien RMBS, CMBS, first-lien RMBS and ABS CDO exposures. The Company also recorded increases in actual and expected salvage due to the resolution of the Company's claims as reflected in a disclosure statement filed in August of 2013. The disclosure statement indicated a revised expected recovery for the Company of approximately \$828 million which is an increase over the previously identified recovery amount of \$796 million reflected in the Plan. The increased recovery amount is primarily due to the favorable disposition of assets and settlements of claims. Additionally, the Company also increased the amount of recoveries subject to contractual obligations by Credit Suisse to repurchase such ineligible mortgage loans. Partially offsetting this was a decrease in excess spread (the difference between interest inflows on mortgage loan collateral and interest outflows on insured beneficial

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interests) within the RMBS securitizations, reversal of recoveries related to high yield corporate CDOs and deterioration in an international road transaction.

In addition to the information presented above, the following tables present aggregate losses and LAE for the three and nine months ended September 30, 2013 and 2012 by insurance type:

### Aggregate Losses and LAE by Insurance Type (change in discounted values of net payments)

In millions	For the Three Months Ended September 30, 2013					
	Second-lien RMBS (1)	First-lien RMBS	ABS CDO	CMBS	Other (2)	Total
Financial guarantee insurance (3)	\$ 28	\$ 8	\$ 1	\$ 10	\$ 16	\$ 63
Financial guarantee insurance related to consolidated VIEs (eliminated in consolidation) (4)	25	-	(13)	-	-	12
Insured credit derivatives (statutory basis) (5)	-	-	-	88	-	88
Total aggregate losses and LAE	\$ 53	\$ 8	\$ (12)	\$ 98	\$ 16	\$ 163

(1) - Includes HELOC loans and CES.

(2) - Primarily represents an international road transaction.

(3) - Included in Losses and loss adjustment as reported on the Company's consolidated statements of operations.

(4) - Represents losses eliminated upon the consolidation of insured VIEs.

(5) - Represents statutory losses and LAE for insurance contracts accounted for as derivatives. Realized and unrealized gains and losses on these contracts under GAAP are recorded in Net change in fair value of insured derivatives on the Company's consolidated statements of operations.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

In millions	For the Three Months Ended September 30, 2012					
	Second-lien RMBS (1)	First-lien RMBS	ABS CDO	CMBS	Other	Total
Financial guarantee insurance <sup>(2)</sup>	\$ 38	\$ 47	\$ 9	\$ 75	\$ (2)	\$ 167
Financial guarantee insurance related to consolidated VIEs (eliminated in consolidation) <sup>(3)</sup>	20	-	(2)	-	-	18
Insured credit derivatives (statutory basis) <sup>(4)</sup>	-	-	19	48	-	67
Total aggregate losses and LAE	\$ 58	\$ 47	\$ 26	\$ 123	\$ (2)	\$ 252

(1) - Includes HELOC loans and CES.

(2) - Included in Losses and loss adjustment as reported on the Company's consolidated statements of operations.

(3) - Represents losses eliminated upon the consolidation of insured VIEs.

(4) - Represents statutory losses and LAE for insurance contracts accounted for as derivatives. Realized and unrealized gains and losses on these contracts under GAAP are recorded in Net change in fair value of insured derivatives on the Company's consolidated statements of operations.

**Aggregate Losses and LAE by Insurance Type (change in discounted values of net payments)**

In millions	For the Nine Months Ended September 30, 2013					
	Second-lien RMBS (1)	First-lien RMBS	ABS CDO	CMBS	Other <sup>(2)</sup>	Total
Financial guarantee insurance <sup>(3)</sup>	\$ (92)	\$ 1	\$ (47)	\$ (28)	\$ 153	\$ (13)
Financial guarantee insurance related to consolidated VIEs (eliminated in consolidation) <sup>(4)</sup>	(44)	-	(39)	-	-	(83)
Insured credit derivatives (statutory basis) <sup>(5)</sup>	-	-	(4)	487	-	483
Total aggregate losses and LAE	\$ (136)	\$ 1	\$ (90)	\$ 459	\$ 153	\$ 387

(1) - Includes HELOC loans and CES.

(2) - Primarily represents an international road transaction.

(3) - Included in Losses and loss adjustment as reported on the Company's consolidated statements of operations.

(4) - Represents losses eliminated upon the consolidation of insured VIEs.

(5) - Represents statutory losses and LAE for insurance contracts accounted for as derivatives. Realized and unrealized gains and losses on these contracts under GAAP are recorded in Net change in fair value of insured derivatives on the Company's consolidated statements of operations.

In millions	For the Nine Months Ended September 30, 2012					
	Second-lien RMBS (1)	First-lien RMBS	ABS CDO	CMBS	Other	Total
Financial guarantee insurance <sup>(2)</sup>	\$ 106	\$ 105	\$ 6	\$ 87	\$ 11	\$ 315
Financial guarantee insurance related to consolidated VIEs (eliminated in consolidation) <sup>(3)</sup>	153	-	(18)	-	-	135
Insured credit derivatives (statutory basis) <sup>(4)</sup>	-	-	8	502	-	510
Total aggregate losses and LAE	\$ 259	\$ 105	\$ (4)	\$ 589	\$ 11	\$ 960

(1) - Includes HELOC loans and CES.

(2) - Included in Losses and loss adjustment as reported on the Company's consolidated statements of operations.

(3) - Represents losses eliminated upon the consolidation of insured VIEs.

(4) - Represents statutory losses and LAE for insurance contracts accounted for as derivatives. Realized and unrealized gains and losses on these contracts under GAAP are recorded in Net change in fair value of insured derivatives on the Company's consolidated statements of operations.

#### **Summary of Financial Guarantee Insurance Losses and LAE**

The following information relates to financial guarantee insurance losses and LAE recorded in accordance with GAAP. Refer to Note 5: Loss and Loss Adjustment Expense Reserves in the Notes to Consolidated Financial Statements for a description of the Company's loss and LAE reserving policy and additional information related to its loss reserves.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

The following table presents information about our loss and LAE incurred for the three and nine months ended September 30, 2013 and 2012:

In millions	Three Months Ended		Percent Change	Nine Months Ended		Percent Change
	September 30, 2013	September 30, 2012		September 30, 2013	September 30, 2012	
Loss and LAE related to actual and expected payments	\$ 18	\$ 185	-90%	\$ 119	\$ 396	-70%
Recoveries of actual and expected payments	45	(18)	n/m	(132)	(81)	63%
Gross losses incurred	63	167	-62%	(13)	315	-104%
Reinsurance	-	-	-%	-	-	-%
Losses and loss adjustment expenses	\$ 63	\$ 167	-62%	\$ (13)	\$ 315	-104%

n/m - Percent change not meaningful.

Losses and LAE incurred in our structured finance and international insurance segment totaled \$63 million for the three months ended September 30, 2013. Included in the \$63 million were decreases in gross recoveries of actual and expected payments of \$45 million and gross losses related to actual and expected future payments of \$18 million. The \$45 million decrease in recoveries of actual and expected payments includes \$42 million of recoveries related to insured second-lien RMBS transactions, primarily driven by a reduction in excess spread within the securitizations. The \$18 million of actual and expected payments includes \$14 million related to insured first-lien RMBS exposures and \$18 million of other loss activity, primarily related to CMBS and an international road transaction, partially offset by a \$14 million decrease in actual and expected payments related to insured second-lien RMBS transactions.

Losses and LAE incurred in our structured finance and international insurance segment totaled \$167 million for the three months ended September 30, 2012. Included in the \$167 million were gross losses related to actual and expected future payments of \$185 million, of which \$140 million primarily related to CMBS and insured first-lien RMBS transactions and \$45 million related to insured second-lien RMBS transactions. Partially offsetting these losses were recoveries of actual and expected payments of \$18 million, including \$7 million related to insured second-lien RMBS transactions. The \$7 million of recoveries related to second-lien RMBS transactions included \$44 million of recoveries resulting from ineligible mortgage loans included in insured exposures that are subject to contractual obligations by sellers/servicers to repurchase or replace such mortgage loans, partially offset by a \$37 million reduction in excess spread within the securitizations.

Losses and LAE incurred in our structured finance and international insurance segment was a benefit of \$13 million for the nine months ended September 30, 2013. Included in the \$13 million benefit were increases in recoveries of actual and expected payments of \$132 million, of which \$177 million related to insured second-lien RMBS transactions, partially offset by \$45 million of other activity. The \$177 million of recoveries related to insured second-lien RMBS transactions included \$316 million of recoveries primarily resulting from ineligible mortgage loans included in insured exposures that are subject to contractual obligations by sellers/servicers to repurchase or replace such mortgage loans, partially offset by a \$139 million reduction in excess spread within the securitizations. The \$45 million of other activity was primarily the result of a reversal of recoveries related to high yield corporate CDOs, partially offset by an increase in recoveries related to an international road transaction. These recoveries were partially offset by gross losses related to actual and expected future payments of \$119 million, of which \$85 million related to insured second-lien RMBS transactions and \$12 million related to first-lien RMBS transactions.



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Losses and LAE incurred in our structured finance and international insurance segment totaled \$315 million for the nine months ended September 30, 2012. Included in the \$315 million were gross losses related to actual and expected future payments of \$396 million, of which \$216 million primarily related to insured first-lien RMBS transactions and CMBS transactions and \$180 million related to insured second-lien RMBS transactions. Partially offsetting these losses were recoveries of actual and expected payments of \$81 million, including \$74 million related to insured second-lien RMBS transactions. The \$74 million of recoveries related to insured second-lien RMBS transactions included \$154 million of recoveries resulting from ineligible mortgage loans included in insured exposures that are subject to contractual obligations by sellers/servicers to repurchase or replace such mortgage loans, partially offset by an \$80 million reduction in excess spread within the securitizations.

For the three and nine months ended September 30, 2013, losses and LAE incurred included the elimination of a \$12 million expense and an \$83 million benefit, respectively, as a result of the consolidation of VIEs. The \$12 million expense elimination included recoveries of actual and expected payments of \$18 million, partially offset by gross losses related to actual and expected future payments of \$6 million. The \$83 million benefit elimination included gross recoveries of actual and expected payments of \$85 million, partially offset by gross losses related to actual and expected future payments of \$2 million.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

For the three and nine months ended September 30, 2012, losses and LAE incurred included the elimination of \$18 million and \$135 million of expense, respectively, as a result of the consolidation of VIEs. The \$18 million elimination included gross losses related to actual and expected future payments of \$11 million and a decrease in recoveries of actual and expected payments of \$7 million. The \$135 million elimination included gross losses related to actual and expected future payments of \$68 million and a decrease in recoveries of actual and expected payments of \$67 million.

The following table presents information about our insurance reserves and recoverable as of September 30, 2013 and December 31, 2012. The Company's insurance loss recoverable represents expected potential recoveries of paid claims based on probability-weighted net cash inflows discounted at applicable risk-free rates as of the measurement date. Our insurance loss recoverable includes expected recoveries related to put-backs of ineligible mortgage loans within second-lien RMBS transactions and other amounts due to MBIA under the terms and conditions of the respective transactional documents (inclusive of subrogation rights).

In millions	September 30, 2013	December 31, 2012	Percent Change
Gross loss and LAE reserves	\$ 802	\$ 918	-13%
Expected recoveries on unpaid losses	(208)	(224)	-7%
Loss and LAE reserves	\$ 594	\$ 694	-14%
Insurance loss recoverable	\$ 725	\$ 3,392	-79%
Insurance loss recoverable-ceded <sup>(1)</sup>	\$ 5	\$ 6	-17%
Reinsurance recoverable on paid and unpaid losses <sup>(2)</sup>	\$ 6	\$ 7	-14%

(1) - Reported within Other liabilities on our consolidated balance sheets.

(2) - Reported within Other assets on our consolidated balance sheets.

Included in the Company's loss and LAE reserves are both reserves for insured obligations for which a payment default has occurred and MBIA Corp. has already paid a claim and also for which a payment default has not yet occurred but a claim is expected in the future. The following table includes LAE reserves as of September 30, 2013 and December 31, 2012 for four issues that had no expected future claim payments or par outstanding, but for which the Company was obligated to pay LAE incurred in prior periods. As of September 30, 2013 and December 31, 2012, loss and LAE reserves comprised the following:

\$ in millions	Number of Issues <sup>(1)</sup>		Loss and LAE Reserve		Par Outstanding	
	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
Gross of reinsurance:						
Issues with defaults	105	97	\$ 403	\$ 448	\$ 6,494	\$ 7,194
Issues without defaults	19	25	191	246	1,004	1,402

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Total gross of reinsurance	124	122	\$ 594	\$ 694	\$ 7,498	\$ 8,596
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(1) - An issue represents the aggregate of financial guarantee policies that share the same revenue source for purposes of making debt service payments. MBIA reports expected potential recoveries of certain paid claims within Insurance loss recoverable and the corresponding estimated recovery amounts due to reinsurers within Other liabilities on the Company's consolidated balance sheets. As of September 30, 2013 and December 31, 2012, our insurance loss recoverable in our structured finance and international insurance segment was \$725 million and \$3.4 billion, respectively. The decrease in our insurance loss recoverable primarily resulted from the collections of previously established recoveries related to the BofA Settlement Agreement related to insured second-lien RMBS securitizations. As of September 30, 2013 and December 31, 2012, our insurance loss recoverable also included estimated recoveries of approximately \$669 million and \$780 million, respectively, primarily from excess spread within insured second-lien RMBS securitizations. Insurance loss recoverables due to reinsurers totaled \$5 million and \$6 million as of September 30, 2013 and December 31, 2012, respectively. Insurance loss recoverables are only paid to reinsurers upon receipt of such amounts by MBIA.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)*****Residential Mortgage Exposure***

MBIA Corp. insures mortgage-backed securities ( MBS ) backed by residential mortgage loans, including second-lien RMBS transactions (revolving HELOC loans and CES). For the three months ended September 30, 2013, we recorded losses and LAE of \$28 million related to insured second-lien RMBS transactions. The \$28 million consolidated losses and LAE was due to a decrease in gross recoveries of actual and expected payments of \$42 million, partially offset by a decrease in gross losses and LAE related to actual and expected payments of \$14 million. For the nine months ended September 30, 2013, we recorded a \$92 million benefit related to insured second-lien RMBS transactions. The \$92 million benefit was due to gross recoveries of actual and expected payments of \$177 million, partially offset by gross losses and LAE related to actual and expected payments of \$85 million.

MBIA Corp. also insures MBS backed by first-lien subprime mortgage loans directly through RMBS securitizations. There has been considerable stress and continued deterioration in the subprime mortgage market since 2008 reflected by increased delinquencies and losses, particularly related to subprime mortgage loans originated during 2005, 2006 and 2007. As of September 30, 2013 and December 31, 2012, the Company had \$1.1 billion and \$2.2 billion, respectively, of gross par outstanding from direct exposure to subprime mortgage loans. While subprime transactions directly guaranteed by MBIA Corp. include collateral comprising mortgage loans that originated during 2005, 2006, and 2007, we currently do not expect ultimate material losses on these transactions given the amount of subordination below MBIA Corp.'s insured portion of such transactions available to absorb losses from collateral defaults. As of September 30, 2013, the Company had \$59 million of gross par outstanding in two insured direct subprime mortgage transactions with 2005 or 2006 subprime mortgage collateral appearing on the Company's Classified or Caution Lists.

The following table presents the gross par outstanding by vintage year of MBIA Corp.'s total direct RMBS insured exposure as of September 30, 2013. Amounts include the gross par outstanding related to transactions that the Company consolidates under accounting guidance for VIEs.

In millions	Gross Par Outstanding					Total
	Prime First- lien	Alternative A-paper First-lien	Subprime First-lien	HELOC Second- lien	CES Second- lien	
2005 - 2007	\$ 15	\$ 1,733	\$ 360	\$ 2,263	\$ 2,684	\$ 7,055
2004 and prior	175	761	763	528	52	2,279
Total gross par	\$ 190	\$ 2,494 <sup>(1)</sup>	\$ 1,123 <sup>(2)</sup>	\$ 2,791	\$ 2,736	\$ 9,334

(1) - Includes international exposure of \$662 million.

(2) - Includes international exposure of \$9 million.

During the nine months ended September 30, 2013, we collected approximately \$2.7 billion, net of reinsurance and \$243 million in payments, on insured second-lien RMBS transactions, or \$2.6 billion after eliminating \$130 million of collections and \$75 million of payments made on behalf of consolidated VIEs. Through September 30, 2013, we paid a cumulative total of \$3.9 billion, net of reinsurance and collections, or \$1.7 billion after eliminating \$2.2 billion of net payments on insured second-lien RMBS transactions that are currently consolidated as VIEs. As of September 30, 2013, we had loss and LAE reserves related to our remaining insured second-lien RMBS exposure of \$124 million before eliminating \$44 million of loss and LAE reserves related to our consolidated VIEs. The loss and LAE reserves represent the present value of the

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difference between cash payments we expect to make on the insured transactions and the cash receipts we expect from the performing mortgage loans in the securitizations. As payments are made, a portion of those expected future receipts is recorded within Insurance loss recoverable in our consolidated balance sheets. The payments that we make virtually all go to reduce the principal balances of the securitizations.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

The following table provides information about insured second-lien RMBS transactions included in MBIA Corp.'s insured portfolio. Classified List as of September 30, 2013. The total payments of consolidated VIEs are not reflected as insurance losses in our consolidated financial statements.

**Second-Lien RMBS Transactions with Claim Payments**

<b>\$ in millions</b>	<b>Number of Issues</b>	<b>Original Par Insured</b>	<b>Gross Par Outstanding</b>	<b>Claim Payments and LAE Net of Collections Since Inception</b>
<b>Non-Consolidated VIEs:</b>				
HELOC	14	\$ 16,253	\$ 1,830	\$ 762
CES	9	8,198	1,760	956
Total	23	\$ 24,451	\$ 3,590	\$ 1,718
Total net of reinsurance				\$ 1,609
<b>Consolidated VIEs:</b>				
HELOC	6	\$ 3,657	\$ 842	\$ 701
CES	6	4,683	956	1,591
Total	12	\$ 8,340	\$ 1,798	\$ 2,292
Total net of reinsurance				\$ 2,220

The preceding table excludes gross and net claim and LAE payments of \$35 million for one issue that has been removed from our Classified List and has no outstanding exposure.

*Non-Consolidated VIEs*

The gross par outstanding on insured second-lien RMBS transactions decreased from \$4.0 billion as of December 31, 2012 to \$3.6 billion as of September 30, 2013. As of September 30, 2013, we expect to pay an additional \$167 million (on a present value basis) on these transactions and expect to receive a total of \$756 million (on a present value basis) in reimbursement of past and future expected claims through excess spread in these transactions. Of our expected reimbursement from excess spread, \$669 million is included in Insurance loss recoverable and \$87 million is included in Loss and loss adjustment expense reserves. In addition, we expect to receive \$18 million (on a present value basis) with respect to amounts contemplated in the ResCap disclosure statement filed in August of 2013, which is included in Insurance loss recoverable.

*Consolidated VIEs*

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The gross par outstanding on insured second-lien RMBS transactions decreased from \$2.2 billion as of December 31, 2012 to \$1.8 billion as of September 30, 2013. The total payments before reinsurance, includes \$751 million that was eliminated subsequent to consolidation. As of September 30, 2013, we expect to pay an additional \$60 million (on a present value basis) on these transactions and expect to receive a total of \$216 million (on a present value basis) in reimbursement of past and future expected claims through excess spread in these transactions. In addition, we expect to receive \$1.1 billion (on a present value basis) as of September 30, 2013 with respect to amounts contemplated in the ResCap disclosure statement filed in August of 2013 as well as Credit Suisse's obligation to repurchase ineligible mortgage loans, which is reported in Loan repurchase commitments under Assets of consolidated variable interest entities on the consolidated balance sheets.

Refer to Note 5: Loss and Loss Adjustment Expense Reserves in the Notes to Consolidated Financial Statements for additional information about assumptions used to estimate recoveries on our RMBS exposure.

### *Other*

We may seek to purchase, from time to time, directly or indirectly, obligations guaranteed by MBIA or seek to commute policies. The amount of insurance exposure reduced, if any, and the nature of any such actions will depend on market conditions, pricing levels from time to time, and other considerations. In some cases, these activities may result in a reduction of expected loss reserves, but in all cases they are intended to limit our ultimate losses and reduce the future volatility in loss development on the related policies. Our ability to purchase guaranteed obligations and to commute policies will depend on management's assessment of available liquidity.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

**POLICY ACQUISITION COSTS AND OPERATING EXPENSES** Structured finance and international insurance segment expenses for the three and nine months ended September 30, 2013 and 2012 are presented in the following table:

In millions	Three Months Ended September 30,		Percent Change	Nine Months Ended September 30,		Percent Change
	2013	2012		2013	2012	
Gross expenses	\$ 23	\$ 30	-23%	\$ 88	\$ 118	-25%
Amortization of deferred acquisition costs	\$ 19	\$ 24	-21%	\$ 76	\$ 81	-6%
Operating	22	30	-27%	83	115	-28%
Total insurance operating expenses	\$ 41	\$ 54	-24%	\$ 159	\$ 196	-19%

Gross expenses represent total insurance expenses before the deferral of any policy acquisition costs. Gross expenses decreased for the three months ended September 30, 2013 compared with the same period of 2012 primarily due to decreases in legal and litigation related costs and compensation expenses. The decrease in the amortization of deferred acquisition costs for the three months ended September 30, 2013 compared with the same period of 2012 principally reflects the acceleration of deferred costs into earnings in prior periods as policies were terminated. Gross expenses decreased for the nine months ended September 30, 2013 compared with the same period of 2012 as a result of decreases in legal and litigation related costs and compensation expenses partially offset by an increase in consulting fees.

Operating expenses decreased for the three and nine months ended September 30, 2013 compared with the same periods of 2012 due to decreases in gross expenses. We did not defer a material amount of policy acquisition costs during 2013 or 2012. Policy acquisition costs in these periods were primarily related to ceding commission income and premium taxes on installment policies written in prior periods.

**INTEREST EXPENSE** Interest expense incurred by our structured finance and international insurance segment decreased for the three and nine months ended September 30, 2013 when compared to the same periods of 2012 primarily due to the repayment of the National Secured Loan in May of 2013. In addition, during 2013, the interest rate on MBIA Corp.'s surplus notes decreased as a result of the conversion to a floating rate.

**INSURED PORTFOLIO EXPOSURE** The credit quality of our structured finance and international insured portfolio is assessed in the same manner as our U.S. public finance insured portfolio. As of September 30, 2013 and December 31, 2012, 23% and 26%, respectively, of our structured finance and international insured portfolio, was rated below investment grade, before giving effect to MBIA's guarantees, based on MBIA's internal ratings, which are more current than the underlying ratings provided by S&P and Moody's for this subset of our insured portfolio.

***Structured Finance and International Insurance Selected Portfolio Exposures***

The following is a summary of selected significant exposures within the insured portfolio of our structured finance and international insurance segment. The Company has large exposures to many of these sectors. Moreover, many of these sectors are and have been considered volatile over the past several years. As described below, considerable incurred losses and future expected payments are attributable to many of these sectors.

***Collateralized Debt Obligations and Related Instruments***

As part of our structured finance and international insurance activities, MBIA Corp. typically provided guarantees on senior and, in a limited number of cases, mezzanine tranches of CDOs, as well as protection on structured CMBS pools and corporate securities, and CDS referencing



such securities. The following discussion, including reported amounts and percentages, includes insured CDO transactions consolidated by the Company as VIEs.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

As of September 30, 2013, MBIA Corp.'s \$31.0 billion CDO portfolio represented 37% of its total insured gross par outstanding of \$83.9 billion. As of December 31, 2012, MBIA Corp.'s \$51.8 billion CDO portfolio represented 46% of its total insured gross par outstanding of \$112.4 billion. The distribution of the Company's insured CDO and related instruments portfolio by collateral type is presented in the following table:

In billions Collateral Type	Gross Par Outstanding as of		
	September 30, 2013	December 31, 2012	Percent Change
Multi-sector CDOs	\$ 1.6	\$ 4.3	-63%
Investment grade CDOs and structured corporate credit pools	16.6	24.1	-31%
High yield corporate CDOs	4.3	5.7	-25%
Commercial real estate pools and CRE CDOs	8.5	17.7	-52%
<b>Total</b>	<b>\$ 31.0</b>	<b>\$ 51.8</b>	<b>-40%</b>

*Multi-Sector CDOs*

The multi-sector CDO portfolio is comprised of 12 transactions insured in the primary market between 2002 and 2006 and 21 transactions insured in the secondary market between 2000 and 2004. The underlying collateral in MBIA Corp.'s insured multi-sector CDO transactions is comprised of RMBS, other multi-sector CDOs, corporate CDOs, collateralized loan obligations, ABS (e.g., securitizations of auto receivables, credit cards, etc.), CRE CDOs, CMBS and corporate credits. Our remaining insured multi-sector CDO transactions primarily rely on underlying collateral originally rated triple-B.

Generally, we are subject to a claim on a multi-sector CDO when the insured tranche incurs an interest or principal shortfall. Such shortfalls result once the underlying collateral supporting the transaction no longer generates enough cash flow to support the insured notes. MBIA Corp.'s payment obligation after a default insures current interest and ultimate principal. Original subordination levels for transactions insured in the primary market ranged from 10% to 31%. Current subordinations range from 0% to 81%.

The significant erosion of subordination in our multi-sector CDO transactions principally resulted from the underperformance of RMBS and CDO collateral. As discussed above, the erosion of subordination in these transactions increases the likelihood that MBIA Corp. will pay claims. As of September 30, 2013, there were credit impairment estimates for 21 classified multi-sector CDO transactions for which MBIA Corp. expects to incur actual net claims in the future (14 of which are insured in the secondary market), representing 64% of all MBIA Corp.-insured multi-sector CDO transactions (including both CDS and non-CDS contracts). Of the remaining transactions, 15% are on our Caution List and 21% continue to perform at or close to our original expectations. In the event of further performance deterioration of the collateral referenced or held in our multi-sector CDO transactions, the amount of credit impairments could increase materially.

Total gross par exposure in our multi-sector CDO portfolio was \$37.3 billion as of December 31, 2007. Since the end of 2007 through September 30, 2013, our multi-sector CDO gross par exposure has decreased by approximately \$35.7 billion primarily from negotiated commutations of \$23.6 billion and contractual terminations without any payment from MBIA Corp. of \$5.4 billion. The remaining reduction in gross par was due to the amortization and maturity of transactions. As of September 30, 2013, our gross par exposure to multi-sector CDOs of \$1.6 billion represented 5% of MBIA Corp.'s CDO exposure and 2% of MBIA Corp.'s total gross par insured.

*Investment Grade Corporate CDOs*

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Our 12 investment grade corporate CDO exposures insured in 2006 and 2007 reference pools of predominantly investment grade corporate credits. Three of these pools include limited exposure to other asset classes, including structured finance securities (such as RMBS and CDOs). Our investment grade corporate CDO policies guarantee coverage of losses on collateral assets once a deductible has been eroded, and are highly customized structures. Our gross par exposure to investment grade corporate CDOs of \$16.6 billion represents 54% of MBIA Corp. s CDO exposure and 20% of MBIA Corp. s total gross par insured. The Company s insured investment grade corporate CDOs have experienced erosion of subordination due to the default of underlying referenced corporate and structured finance securities, but we currently do not expect losses on MBIA Corp. s insured tranches. As of September 30, 2013, the collateral amount in the portfolio exceeds the gross par outstanding as a result of credit enhancement. Original subordination levels for nine of the investment grade corporate CDO policies ranged from 15% to 30%. Current subordination levels for these nine policies are between 11% and 28%.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

Our gross par of insured investment grade corporate CDOs includes \$7.1 billion across three transactions that were structured to include buckets (typically 30% to 35% of the overall CDO) of references to specific tranches of other investment grade corporate CDOs (monotranches). In such transactions, MBIA Corp.'s insured investment grade corporate CDOs include, among direct corporate or structured credit reference risks, and monotranches or single layer credit risk referencing a diverse pool of corporate assets or obligors with a specific attachment and a specific detachment point. The referenced monotranches in such CDOs were typically rated double-A and sized to approximately 3% of the overall reference risk pool. The inner referenced monotranches are not subject to acceleration and do not give control rights to a senior investor. The inner referenced monotranches have also experienced erosion of subordination due to defaults in their referenced corporate assets. These transactions had original subordination of 25% and current subordination ranges from 15% to 18%.

*High Yield Corporate CDOs*

Our high yield corporate CDO portfolio, totaling \$4.3 billion of gross par exposure, largely comprises middle-market/special- opportunity corporate loan transactions. Our gross par exposure to high yield corporate CDOs represents 14% of MBIA Corp.'s CDO exposure and 5% of MBIA Corp.'s total gross par insured as of September 30, 2013. Original subordination for our high yield corporate portfolio ranged from 22% to 33%. Current subordination is between 10% and 30%. Declines in subordination levels result from defaults in underlying collateral, as well as sales of underlying collateral at discounted prices. Subordination within CDOs may decline further over time as a result of additional collateral deterioration. We do not expect insured losses on our high yield corporate CDO portfolio. Accordingly, as of September 30, 2013, there is no loss reserve established for this portfolio. However, there can be no assurance that the Company will not incur losses as a result of further deterioration in subordination.

*Commercial Real Estate Pools and CRE CDOs*

As of September 30, 2013, we had \$8.5 billion of gross par exposure to the CRE sector through insured structured transactions primarily comprising CRE collateral. In addition, MBIA Corp. insures approximately \$1.5 billion in CRE loan pools, primarily comprising European assets. These CRE loans are not included in the following Structured CMBS Pools and CRE CDOs sections. During the nine months ended September 30, 2013, the Company commuted \$8.9 billion of gross par exposure related to CRE exposure. Refer to Note 5: Loss and Loss Adjustment Expense Reserves in the Notes to Consolidated Financial Statements for a discussion of credit impairments on our CRE pools and CDO exposure, including the methodology used to calculate these impairments.

**Structured CMBS Pools**

As of September 30, 2013, our gross par exposure to structured CMBS pools totaled \$7.2 billion and represented approximately 9% of MBIA Corp.'s total gross par insured. Since the end of 2007 through September 30, 2013, our structured CMBS pools gross par exposure has decreased by approximately \$33.5 billion, primarily from negotiated commutations and early settlements. Our structured CMBS pool insured transactions are pools of CMBS bonds, Real Estate Investment Trust (REIT) debt and other CRE CDOs structured with first loss deductibles such that MBIA Corp.'s obligation attached at a minimum of a triple-A level when the policies were issued. The deductible sizing was a function of the underlying collateral ratings and certain structural attributes. MBIA Corp.'s guarantees for most structured CMBS pool transactions cover losses on collateral assets once the deductibles have been eroded. These deductibles provide credit enhancement and subordination to MBIA's insured position.

The collateral in the pools are generally CMBS bonds or CDSs referencing CMBS bonds (collectively, CMBS bonds). MBIA Corp.'s guarantee generally is in the form of a CDS referencing the static pooled transactions. MBIA Corp. would have a payment obligation if the volume of CMBS bond defaults exceeds the deductible level in the transaction. Each pool comprising CMBS bonds is ultimately backed by the commercial mortgage loans securitized within each CMBS trust. The same CMBS bonds may be referenced in multiple pools. The Company's structured CMBS pools are static, meaning that the collateral pool of securitizations cannot be and has not been changed since the origination of the policy. Most transactions comprised similarly rated underlying tranches at inception. The deductible for each transaction varies according to the ratings of the underlying collateral. For example, a transaction which comprised originally BBB rated underlying CMBS bonds would typically include a 30-35% deductible to MBIA Corp.'s position whereas a transaction comprising all originally AAA rated underlying CMBS bonds would

typically have required a 5-10% deductible.

Original deductibles for our structured CMBS pools ranged from 5.0% to 82.3%. As of September 30, 2013, the deductibles for these transactions ranged from 0% to 81.7%. Deductibles are eroded as bonds experience realized losses which are ultimately due to liquidations of underlying loan collateral. During the second and third quarters of 2013, we paid claims on a CMBS pool transaction which experienced deterioration such that all of the remaining deductible was eliminated. We expect to experience additional claims on this transaction.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

As of September 30, 2013, we have significantly reduced our exposure to pools comprised of 2006 and 2007 vintage CMBS collateral originally rated BBB. As of September 30, 2013, we had exposure to four static CMBS pools, having \$800 million of gross par outstanding, that were originally insured in 2006 and 2007, and in which substantially all of the underlying collateral comprised CMBS tranches originally rated BBB and lower. Additionally, we insure two static CMBS pools, totaling \$3.0 billion of gross par outstanding as of September 30, 2013, that were originally insured in 2007, and are comprised of CMBS collateral which was originally rated A. Ultimate loss rates remain uncertain. If the economy does not continue to improve, it is possible that we will experience severe losses, particularly if the underlying loans are unable to pay off at their expected maturity dates. Although we believe MBIA Corp. will have adequate resources to pay expected claims, there can be no assurance that this will be the case. The remaining insured CMBS portfolio primarily consists of transactions backed by collateral originally rated AAA and originated in 2004, 2005, 2006 or 2007.

Delinquencies increased markedly in the CRE market during and immediately after the economic crisis, however they have stabilized over the last twelve months. As of September 30, 2013, 30-day and over delinquencies in the fixed-rate conduit CMBS market were 7.8%, and in MBIA Corp.'s insured static pooled CMBS portfolio were 11.2%. The higher delinquency rate in MBIA Corp.'s portfolio was primarily due to a concentration in the 2006 and early 2007 vintages. Additionally, the market includes newer vintage transactions from 2010 to 2012, which have virtually no material delinquencies. Although we have also seen stabilization in the delinquency rate over the past several months, some of the moderation is attributable to increased liquidations, and loan modifications and extensions granted by the special servicers. The special servicers are responsible for managing loans that have defaulted and for conducting the remediation and foreclosure process with the objective of maximizing proceeds for all bondholders by avoiding or minimizing loan level losses.

Actual losses will be a function of the proportion of loans in the pools that are foreclosed and liquidated and the loss severities associated with those liquidations. If the deductibles in the Company's insured transactions and underlying referenced CMBS transactions are fully eroded, additional property level losses upon foreclosures and liquidations could result in substantial losses for MBIA. Ultimate loss rates remain uncertain and it is possible that we will experience severe losses or liquidity needs due to increased deterioration in our insured CMBS portfolio or our failure to commute the policies, in particular if macroeconomic stress escalates, there is a new recession, increased delinquencies, higher levels of liquidations of delinquent loans, and/or higher severities of loss upon liquidation. Although we still believe the likelihood of a new recession is low, we do consider the possibility in our estimates for future claims.

**CRE CDOs**

As of September 30, 2013, our gross par exposure to CRE CDOs totaled \$1.3 billion and represented approximately 2% of MBIA Corp.'s total gross par insured. CRE CDOs are managed pools of CMBS, CRE whole loans, B-Notes, mezzanine loans, REIT debt, and other securities (including, in some instances, buckets for RMBS and CRE CDOs) that allow for reinvestment during a defined time period. These transactions benefit from typical CDO structural features such as cash diversion triggers, collateral quality tests, and manager replacement provisions. MBIA Corp. guarantees timely interest and ultimate principal of these CDOs. As with our other insured CDOs, these transactions were structured with credit protection originally rated triple-A, or a multiple of triple-A, below our guarantee. As of September 30, 2013, our CRE CDO insured portfolio did not contain any CDOs of ABS exposures. Some of the CRE CDO transactions do contain some RMBS collateral, but overall this comprises less than 1% of the collateral in the CRE CDO portfolio. To the extent losses do occur on these transactions, the payments are due at the maturity date, which range from the years 2036 through 2056. Current subordination levels are between 0% and 42%.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)*****U.S. Public Finance and Structured Finance and International Reinsurance***

Reinsurance enables the Company to cede exposure for purposes of syndicating risk and increasing its capacity to write new business while complying with its single risk and credit guidelines. When a reinsurer is downgraded by one or more of the rating agencies, less capital credit is given to MBIA under rating agency models and the overall value of the reinsurance to MBIA is reduced. The Company generally retains the right to reassume the business ceded to reinsurers under certain circumstances, including a reinsurer's rating downgrade below specified thresholds. The following table presents information about our reinsurance agreements as of September 30, 2013 for our U.S. public finance and structured finance and international insurance operations:

In millions	Standard & Poor's Rating	Moody's Rating	Ceded Par Outstanding	Letters of Credit/Trust Accounts	Reinsurance Recoverable <sup>(1)</sup>
Reinsurers	(Status)	(Status)			
Assured Guaranty Re Ltd.	AA- (Stable Outlook)	Baa1 (Stable Outlook)	\$ 4,009	\$ 5	\$ 7
Assured Guaranty Corp.	AA- (Stable Outlook)	A3 (Stable Outlook)	2,773	-	-
Overseas Private Investment Corporation	AA+ (Stable Outlook)	Aaa (Stable Outlook)	337	-	-
Others	A+ or above	A2 or above	132	2	-
<b>Total</b>			<b>\$ 7,251</b>	<b>\$ 7</b>	<b>\$ 7</b>

(1) - Total reinsurance recoverable of \$7 million is primarily recoverables on unpaid losses.

MBIA requires certain unauthorized reinsurers to maintain bank letters of credit or establish trust accounts to cover liabilities ceded to such reinsurers under reinsurance contracts. As of September 30, 2013, the total amount available under these letters of credit and trust accounts was \$7 million. The Company remains liable on a primary basis for all reinsured risk, and although MBIA believes that its reinsurers remain capable of meeting their obligations, there can be no assurance of such in the future.

As of September 30, 2013, the aggregate amount of insured par outstanding ceded by MBIA to reinsurers under reinsurance agreements was \$7.3 billion compared with \$3.4 billion as of December 31, 2012. Of the \$7.3 billion of ceded par outstanding as of September 30, 2013, \$5.8 billion was ceded from our U.S. public finance insurance segment and \$1.5 billion was ceded from our structured finance and international insurance segment. Under National's reinsurance agreement with MBIA Corp., if a reinsurer of MBIA Corp. is unable to pay claims ceded by MBIA Corp. on U.S. public finance exposure, National will assume liability for such ceded claim payments. As of September 30, 2013, the total amount for which National would be liable in the event that the reinsurers of MBIA Corp. were unable to meet their obligations is \$1.6 billion.

In August of 2013, the novation agreement between FGIC and National, whereby FGIC transfers, by novation, to National all the rights and liabilities under each of the policies covered under a reinsurance agreement with FGIC, became effective. This novation agreement includes covered policies that previously benefited from the reinsurance agreement and second-to-pay policies entered into by MBIA Insurance Corporation in 2008 that were subsequently assigned to and reinsured by National in 2009. As a result of this novation, National is now the

primary insurer under these policies. The amount of third-party reinsurance available to National via the novation agreement totals \$4.2 billion.

***Advisory Services***

Our asset management and advisory business is primarily conducted through Cutwater and Trifinium Advisors (UK) Limited ( Trifinium ). Cutwater provides advisory services, including cash management, discretionary asset management and structured products on a fee-for-service basis. Cutwater offers these services to public, not-for-profit, corporate and financial services clients, including MBIA Inc. and its other subsidiaries. Trifinium provides certain advisory services primarily in the European Union.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

The following table summarizes the results and assets under management of our advisory services segment for the three and nine months ended September 30, 2013 and 2012. These results include revenues and expenses from transactions with the Company's insurance, corporate, and wind-down operations.

In millions	Three Months Ended September 30, 2013		2012		Percent Change	Nine Months Ended September 30, 2013		2012		Percent Change
Fees	\$	11	\$	13	-15%	\$	33	\$	42	-21%
Operating expenses		19		15	27%		48		48	-%
Pre-tax income (loss)	\$	(8)	\$	(2)	n/m	\$	(15)	\$	(6)	150%
Ending assets under management:										
Third-party	\$	15,010	\$	17,624	-15%	\$	15,010	\$	17,624	-15%
Insurance and corporate		6,807		7,530	-10%		6,807		7,530	-10%
Asset/liability products and conduits		4,040		5,061	-20%		4,040		5,061	-20%
Total ending assets under management	\$	25,857	\$	30,215	-14%	\$	25,857	\$	30,215	-14%

n/m - Percent change not meaningful.

For the three and nine months ended September 30, 2013, the unfavorable changes in pre-tax income (loss) compared with the same periods of 2012 were primarily driven by decreases in fees due to declines in asset balances managed for our other segments and for third parties. Operating expenses for the three months ended September 30, 2013 increased compared with the same period of 2012 due to increases in legal costs, compensation expense related to severance and consulting fees.

Average third-party assets under management for the nine months ended September 30, 2013 and 2012 were \$16.9 billion and \$19.7 billion, respectively. This decrease was principally due to declines in our pool products and CDO management business.

**Corporate**

General corporate activities are conducted through our corporate segment. Our corporate operations primarily consist of holding company activities, including our service company, Optinuity Alliance Resources Corporation ( Optinuity ). Revenues and expenses for Optinuity are included in the results of our corporate segment. Optinuity provides support services such as management, legal, accounting, treasury, information technology, and insurance portfolio surveillance, among others, to our corporate segment and other operating businesses on a fee-for-service basis.

The following table summarizes the consolidated results of our corporate segment for the three and nine months ended September 30, 2013 and 2012. The results include revenues and expenses that arise from general corporate activities and from providing support to our other segments.

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In millions	Three Months Ended September 30,			Percent Change	Nine Months Ended September 30,			Percent Change
	2013	2012			2013	2012		
Net investment income	\$ 6	\$ 3		100%	\$ 15	\$ 10		50%
Fees	32	54		-41%	76	133		-43%
Net gains (losses) on financial instruments at fair value and foreign exchange	43	11		n/m	19	19		-%
Net investment losses related to other-than-temporary impairments	-	(4)		-100%	-	(4)		-100%
Other net realized gains (losses)	-	-		-%	-	5		-100%
Revenues of consolidated VIEs:								
Other net realized gains (losses)	-	-		-%	(10)	-		n/m
Total revenues	81	64		27%	100	163		-39%
Operating	32	27		19%	133	79		68%
Interest	13	15		-13%	36	43		-16%
Total expenses	45	42		7%	169	122		39%
Pre-tax income (loss)	\$ 36	\$ 22		64%	\$ (69)	\$ 41		n/m

n/m - Percent change not meaningful.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

**FEES** Fees are generated from support services provided to business units within the Company on a fee-for-service basis. Fees for the three and nine months ended September 30, 2013 decreased compared with the same periods of 2012 primarily due to decreases in fees paid by our conduit segment for administrative and other services. Such fees may vary significantly from period to period.

**NET GAINS (LOSSES) ON FINANCIAL INSTRUMENTS AT FAIR VALUE AND FOREIGN EXCHANGE** The increase in net gains (losses) on financial instruments at fair value and foreign exchange for the three months ended September 30, 2013 compared with the same period of 2012 was primarily due to the changes in the fair value of outstanding warrants issued on MBIA Inc. common stock. These changes were attributable to fluctuations in MBIA Inc.'s stock price and volatility, which are used in the valuation of the warrants. Under the terms of the BofA Settlement Agreement, Blue Ridge received a five-year warrant to purchase 9.94 million shares of MBIA common stock in May of 2013. Under the terms of the Investment Agreement with Warburg Pincus Private Equity X, L.P. and certain of its affiliates (Warburg Pincus), the Company issued Warburg Pincus a five-year warrant to purchase 1.91 million shares of MBIA common stock in August of 2013.

**OTHER NET REALIZED GAINS (LOSSES)** Other net realized gains and losses for the nine months ended September 30, 2012, consisted of insurance recoveries received from our directors' and officers' insurance policy. These insurance recoveries reimbursed the Company for a portion of the expenses incurred by the Company related to private securities litigation.

**REVENUES OF CONSOLIDATED VIEs** For the nine months ended September 30, 2013, total revenues of consolidated VIEs related to net losses as a result of the deconsolidation of VIEs.

**OPERATING EXPENSES** Operating expenses for the three months ended September 30, 2013 increased compared with the same period of 2012 due to an increase in compensation expense related to severance. Operating expenses for the nine months ended September 30, 2013 increased compared with the same period of 2012 due to expenses related to the BofA Settlement Agreement.

**Wind-down Operations**

We operate an asset/liability products business in which we historically issued debt and investment agreements insured by MBIA Corp. to capital markets and municipal investors. The proceeds of the debt and investment agreements were used initially to purchase assets that largely matched the duration of those liabilities. We also operate a conduit business in which we historically funded transactions by issuing debt insured by MBIA Corp. The rating downgrades of MBIA Corp. resulted in the termination and collateralization of certain derivatives and investment agreements and, together with the rising cost and declining availability of funding and liquidity within many of the asset classes in which proceeds were invested, caused the Company to begin winding down its asset/liability products and conduit businesses in 2008. Since the downgrades of MBIA Corp., we have not issued debt in connection with either business and, as a result, the outstanding liability balances and corresponding asset balances will continue to decline over time as liabilities mature, terminate or are redeemed or repurchased by us.

**Asset/Liability Products**

The following table presents the results of our asset/liability products segment for the three and nine months ended September 30, 2013 and 2012. These results include revenues and expenses from transactions with the Company's other segments.

In millions	Three Months Ended September 30,		Percent	Nine Months Ended September 30,		Percent
	2013	2012	Change	2013	2012	Change
Net investment income	\$ 5	\$ 7	-29%	\$ 18	\$ 37	-51%
Net gains (losses) on financial instruments at fair value and foreign exchange	(29)	(39)	-26%	(38)	(168)	-77%

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Net investment losses related to other-than-temporary impairments	-	-	-%	-	(56)	-100%
Net gains (losses) on extinguishment of debt	7	-	n/m	11	-	n/m
Total revenues	(17)	(32)	-47%	(9)	(187)	-95%
Operating	2	4	-50%	7	12	-42%
Interest expense	19	22	-14%	59	80	-26%
Total expenses	21	26	-19%	66	92	-28%
Pre-tax income (loss)	\$ (38)	\$ (58)	-34%	\$ (75)	\$ (279)	-73%

n/m - Percent change not meaningful.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)**

**NET INVESTMENT INCOME** The decrease in net investment income for the three and nine months ended September 30, 2013 compared with the same periods of 2012 was primarily due to lower average asset balances as investments were sold to generate liquidity and repay liabilities.

**NET GAINS (LOSSES) ON FINANCIAL INSTRUMENTS AT FAIR VALUE AND FOREIGN EXCHANGE** The favorable change in net gains (losses) on financial instruments at fair value and foreign exchange for the three months ended September 30, 2013 compared with the same period of 2012 was primarily the result of derivative gains in 2013 compared with losses in 2012 partially offset by a decline in gains related to the sale of investments. The favorable change in net gains (losses) on financial instruments at fair value and foreign exchange for the nine months ended September 30, 2013 compared to the same period of 2012 was primarily the result of derivative gains in 2013 compared with losses in 2012 and a decline in losses related to the sale of investments, partially offset by higher losses on medium-term notes ( MTNs ) carried at fair value.

**NET INVESTMENT LOSSES RELATED TO OTHER-THAN-TEMPORARY IMPAIRMENTS** The Company has an ongoing review process for all securities to assess whether a decline in value is related to a credit loss. The Company utilizes cash flow modeling for purposes of assessing other-than-temporary impairments. Net investment losses related to other-than-temporary impairments for the nine months ended September 30, 2012 related to impairing certain securities to their fair values, as it was our intent to sell these securities before a recovery of their fair values to amortized cost. Refer to the Liquidity section included herein for additional information about impaired investments.

**NET GAINS (LOSSES) ON EXTINGUISHMENT OF DEBT** For the three and nine months ended September 30, 2013, net gains (losses) on extinguishment of debt was primarily due to gains from terminations of MTNs and investment agreements issued by the Company.

**INTEREST EXPENSE** The decrease in interest expense for the three and nine months ended September 30, 2013 compared with the same periods of 2012 was primarily due to the continued maturity and repurchases of liabilities by the Company.

*Conduits*

The following table presents the results of our conduit segment for the three and nine months ended September 30, 2013 and 2012. These results include revenues and expenses from transactions with the Company's other segments.

In millions	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Percent Change	2013	2012	Percent Change
<b>Revenues of consolidated VIEs:</b>						
Net investment income	\$ (1)	\$ 4	-125%	\$ 3	\$ 9	-67%
Net gains (losses) on financial instruments at fair value and foreign exchange	-	-	-%	(3)	-	n/m
Net gains (losses) on extinguishment of debt	-	16	-100%	-	49	-100%
<b>Total revenues</b>	<b>(1)</b>	<b>20</b>	<b>-105%</b>	<b>-</b>	<b>58</b>	<b>-100%</b>
<b>Expenses of consolidated VIEs:</b>						
Operating	15	37	-59%	26	72	-64%
Interest	-	2	-100%	4	10	-60%
<b>Total expenses</b>	<b>15</b>	<b>39</b>	<b>-62%</b>	<b>30</b>	<b>82</b>	<b>-63%</b>

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Pre-tax income (loss)	\$	(16)	\$	(19)	-16%	\$	(30)	\$	(24)	25%
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n/m- Percent change not meaningful.

Our conduit segment is operated through Meridian. Certain of MBIA's consolidated subsidiaries have received compensation for services provided to Meridian.

For the three and nine months ended September 30, 2013, total revenues decreased compared with the same periods of 2012 primarily due to the absence of net gains from the repurchases of debt issued by Meridian. Total expenses decreased compared with the same periods of 2012, primarily due to a decline in fees paid to our corporate segment for administrative and other services.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****RESULTS OF OPERATIONS (continued)****Taxes***Provision for Income Taxes*

The Company's income taxes and the related effective tax rates for the three and nine months ended September 30, 2013 and 2012 are presented in the following table:

In millions	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Pre-tax income (loss)	\$ 171	\$ (57)	\$ 122	\$ 759
Provision (benefit) for income taxes	\$ 39	\$ (64)	\$ 4	\$ 161
Effective tax rate	22.8%	112.3%	3.3%	21.2%

For the nine months ended September 30, 2013, our effective tax rate applied to our pre-tax income was lower than the U.S. statutory tax rate of 35% primarily due to a reduction in our valuation allowance against our deferred tax asset.

For the nine months ended September 30, 2012, our effective tax rate applied to our pre-tax income was lower than the U.S. statutory tax rate of 35% as a result of the decrease in the Company's valuation allowance, the release of a portion of the reserve for uncertain tax benefits and the benefit of tax-exempt interest income from investments.

As of December 31, 2012, the Company's consolidated net operating loss (NOL) carryforward was \$1.3 billion which will expire between tax years 2029 through 2032. As a result of commutation activity in the second quarter of 2013, the Company's NOL has significantly increased from December 31, 2012. As of September 30, 2013, the Company's NOL is approximately \$2.8 billion. As of December 31, 2012, the Company had a capital loss carryforward of \$165 million which will expire between tax years 2013 and 2017. However, as of September 30, 2013, the Company has generated year-to-date capital gain income sufficient to fully utilize the 2012 capital loss carryforward.

Refer to Note 10: Income Taxes in the Notes to Consolidated Financial Statements for a further discussion of income taxes, including the Company's valuation allowance against deferred tax assets and its accounting for tax uncertainties.

**CAPITAL RESOURCES**

The Company manages its capital resources to minimize its cost of capital while maintaining appropriate claims-paying resources (CPR) for National and MBIA Corp. The Company's capital resources consist of total shareholders' equity, total debt issued by MBIA Inc. for general corporate purposes, and surplus notes issued by MBIA Insurance Corporation. Total capital resources were \$4.7 billion and \$4.8 billion as of September 30, 2013 and December 31, 2012, respectively. MBIA Inc. utilizes its capital resources to support the business activities of its subsidiaries. As of September 30, 2013, MBIA Inc.'s investments in subsidiaries totaled \$4.1 billion.

In addition to managing the capital resources of MBIA Inc.'s subsidiaries, we also manage the capital resources of MBIA Inc. supporting our corporate and asset/liability products segments. This includes our corporate unsecured debt issued for general corporate purposes and debt and investment agreements for operating leverage purposes in support of our asset/liability products business. MBIA Inc. seeks to maintain sufficient liquidity and capital resources to meet its general corporate needs as well as the needs of the asset/liability products business. As of September 30, 2013 and December 31, 2012, the combined net debt of MBIA Inc.'s corporate segment and asset/liability products segment, which primarily comprised long-term debt, MTNs, investment agreements and derivative liabilities net of cash and investments at amortized cost and a tax receivable from subsidiaries, totaled \$1.3 billion and \$1.2 billion, respectively. The Company expects that MBIA Inc. will generate sufficient cash to satisfy its net debt and its general corporate needs over time from distributions from its operating subsidiaries. In addition, the Company may also consider raising third-party capital. There can be no assurance that the aforementioned factors will generate sufficient cash to

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satisfy its net debt. Refer to the following [Liquidity MBIA Inc. Liquidity](#) section for additional information about MBIA Inc.'s liquidity.

### ***Securities Repurchases***

Repurchases of debt and/or common stock may be made from time to time in the open market or in private transactions as permitted by securities laws and other legal requirements. We may also choose to redeem debt obligations where permitted by the relevant agreements. We believe that debt and/or share repurchases and redemptions can be an appropriate deployment of capital in excess of amounts needed to support our liquidity while maintaining the CPR of MBIA Corp. and National as well as other business needs.



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### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

#### **CAPITAL RESOURCES (continued)**

##### **Debt securities**

MBIA Inc. or its subsidiaries may repurchase or redeem their outstanding debt at prices that we deem to be economically advantageous. During the nine months ended September 30, 2013, the Company redeemed \$486 million par value outstanding of MTNs issued by the Company's conduit segment at a cost of 100% of par value. The Company also repurchased approximately \$80 million par value outstanding of GFL MTNs issued by the Company's asset/liability segment at a weighted average cost of approximately 92% of par value.

##### **Insurance Statutory Capital**

National and MBIA Insurance Corporation are incorporated and licensed in, and are subject to primary insurance regulation and supervision by, the State of New York. National and MBIA Insurance Corporation each are required to file detailed annual financial statements, as well as interim financial statements, with the NYSDFS and similar supervisory agencies in each of the other jurisdictions in which it is licensed. These financial statements are prepared in accordance with New York State and the National Association of Insurance Commissioners' statements of U.S. STAT and assist our regulators in evaluating minimum standards of solvency, including minimum capital requirements, and business conduct. U.S. STAT differs from GAAP in a number of ways. Refer to the statutory accounting practices note to consolidated financial statements of National and MBIA Corp. within exhibits 99.1 and 99.2, respectively, of MBIA Inc.'s Annual Report on Form 10-K for the year ended December 31, 2012 for an explanation of the differences between U.S. STAT and GAAP.

##### **National**

##### **Capital and Surplus**

National reported total statutory capital of \$3.4 billion as of September 30, 2013 compared with \$3.2 billion as of December 31, 2012. As of September 30, 2013, statutory capital comprised \$1.2 billion of contingency reserves and \$2.2 billion of policyholders' surplus. The increase in National's statutory capital is primarily due to statutory net income of \$153 million for the nine months ended September 30, 2013. Consistent with our plan to transform our insurance business, the Company received approval from the NYSDFS to reset National's unassigned surplus to zero, which was effective January 1, 2010. As of September 30, 2013, National's unassigned surplus was \$1.6 billion. In October 2010, the plaintiffs in the litigation challenging the establishment of National initiated a court proceeding challenging the approval of the surplus reset. Subsequent to the BofA Settlement Agreement and the Societe Generale settlement, all litigation brought originally by the group of eighteen domestic and international financial institutions, related to the establishment of National, has been resolved. Refer to Note 14: Commitments and Contingencies in the Notes to Consolidated Financial Statements for a discussion of this action.

In order to maintain its New York State financial guarantee insurance license, National is required to maintain a minimum of \$65 million of policyholders' surplus. National is also required to maintain contingency reserves to provide protection to policyholders in the event of extreme losses in adverse economic events. Refer to the following MBIA Insurance Corporation Capital and Surplus section for additional information about contingency reserves under the New York Insurance Law (NYIL). National's policyholders' surplus will grow over time from the recognition of unearned premiums and investment income and the expected release of the contingency reserves. Conversely, incurred losses would reduce policyholders' surplus. As of September 30, 2013 and December 31, 2012, National was not in compliance with its single risk limits requirements but was in compliance with its aggregate risk limits.

NYIL regulates the payment of dividends by financial guarantee insurance companies and provides that such companies may not declare or distribute dividends except out of statutory earned surplus. Under NYIL, the sum of (i) the amount of dividends declared or distributed during the preceding 12-month period and (ii) the dividend to be declared may not exceed the lesser of (a) 10% of policyholders' surplus, as reported in the latest statutory financial statements or (b) 100% of adjusted net investment income for such 12-month period (the net investment income for such 12-month period plus the excess, if any, of net investment income over dividends declared or distributed during the two-year period preceding such 12-month period), unless the Superintendent of the NYSDFS approves a greater dividend distribution based upon a finding that the insurer will retain sufficient surplus to support its obligations.



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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

**CAPITAL RESOURCES (continued)**

National is subject to NYIL with respect to the payment of dividends as described above. National had a positive earned surplus as of September 30, 2013, which provides National with dividend capacity. In connection with the court proceeding challenging the approval of the National surplus reset described above, we agreed that National would not pay dividends while the proceeding was adjourned. This agreement terminated in connection with the resolution of the proceeding. In addition, in connection with the approval of a release of excessive contingency reserves during 2011 for MBIA Insurance Corporation, the Company agreed that National would not pay dividends without the prior regulatory approval of the NYSDFS prior to July 19, 2013. Finally, as a condition to the NYSDFS' approval of the Asset Swap between MBIA Inc. and National, the NYSDFS requested that, until the notional amount of the Asset Swap has been reduced to 5% or less of National's admitted assets, each of MBIA Inc., MBIA Insurance Corporation and National provide the NYSDFS with three months prior notice, or such shorter period as the NYSDFS may permit, of its intent to initiate cash dividends on shares of its common stock. National provided the NYSDFS with such notice. Subsequent to September 30, 2013, National declared and paid a dividend of \$214 million to its ultimate parent, MBIA Inc.

National's statutory policyholders' surplus was lower than its GAAP shareholder's equity by \$1.7 billion as of September 30, 2013. U.S. STAT differs from GAAP in certain respects. Refer to Note 11: Statutory Accounting Practices in the Notes to Consolidated Financial Statements of National within exhibit 99.1 of MBIA Inc.'s Annual Report on Form 10-K for the year ended December 31, 2012 for an explanation of the differences between U.S. STAT and GAAP.

**Claims-Paying Resources (Statutory Basis)**

CPR is a key measure of the resources available to National to pay claims under its insurance policies. CPR consists of total financial resources and reserves calculated on a statutory basis. CPR has been a common measure used by financial guarantee insurance companies to report and compare resources and continues to be used by MBIA's management to evaluate changes in such resources. We have provided CPR to allow investors and analysts to evaluate National using the same measure that MBIA's management uses to evaluate National's resources to pay claims under its insurance policies. There is no directly comparable GAAP measure. Our calculation of CPR may differ from the calculation of CPR reported by other companies.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****CAPITAL RESOURCES (continued)**

National's CPR and components thereto, as of September 30, 2013 and December 31, 2012 are presented in the following table:

<b>In millions</b>	<b>As of September 30, 2013</b>	<b>As of December 31, 2012</b>
Policyholders' surplus	\$ 2,162	\$ 1,999
Contingency reserves	1,203	1,249
Statutory capital	3,365	3,248
Unearned premium reserve	1,772	2,041
Present value of installment premiums <sup>(1)</sup>	207	217
Premium resources <sup>(2)</sup>	1,979	2,258
Net loss and LAE reserves <sup>(1)</sup>	(81)	(109)
Salvage reserves	185	262
Gross loss and LAE reserve	104	153
Total claims-paying resources	\$ 5,448	\$ 5,659

(1) - Calculated using a discount rate of 4.54% as of September 30, 2013 and December 31, 2012.

(2) - Includes financial guarantee and insured credit derivative related premiums.

*MBIA Insurance Corporation*

**Capital and Surplus**

MBIA Insurance Corporation reported total statutory capital of \$1.0 billion as of September 30, 2013 compared with \$1.5 billion as of December 31, 2012. As of September 30, 2013, statutory capital comprised \$428 million of contingency reserves and \$612 million of policyholders' surplus. For the nine months ended September 30, 2013, MBIA Insurance Corporation had a statutory net loss of \$358 million, primarily due to losses and LAE incurred partially offset by net premiums earned. MBIA Insurance Corporation's policyholders' surplus as of September 30, 2013 included a negative unassigned surplus of \$1.4 billion. As of September 30, 2013, MBIA Insurance Corporation's policyholders' surplus was negatively impacted by \$39 million because under NYIL it was not permitted to treat as an admitted asset the portion of its investment in subsidiaries in excess of the greater of 50% of policyholders' surplus or 60% of surplus. This overage was caused by a decrease in MBIA Insurance Corporation's policyholders' surplus due to additional insured losses during the third quarter of 2013. MBIA Insurance Corporation's policyholders' surplus may be further negatively impacted if future additional insured losses are incurred and the percentage of its assets invested in subsidiaries continues to increase.

As of September 30, 2013, MBIA Insurance Corporation recognized estimated recoveries of \$714 million, net of reinsurance and income taxes at a rate of 35%, on a statutory basis related to put-backs of ineligible mortgage loans in its insured transactions. These expected insurance recoveries represented 69% of MBIA Insurance Corporation's statutory capital as of September 30, 2013. There can be no assurance that we will be successful or that we will not be delayed in realizing these recoveries. Refer to Executive Overview MBIA Corp. included herein for factors

that may influence MBIA Corp.'s ability to realize these recoveries.

In order to maintain its New York State financial guarantee insurance license, MBIA Insurance Corporation is required to maintain a minimum of \$65 million of policyholders' surplus. MBIA Insurance Corporation's policyholders' surplus is expected to grow over time from the recognition of unearned premiums and investment income and the expected release of the contingency reserves. In addition, MBIA Insurance Corporation's policyholders' surplus could be enhanced by the settlement, commutation or repurchase of insured transactions at prices less than its statutory loss reserves for such transactions. Conversely, incurred losses or an inability to collect on our ineligible mortgage loan put-back claims would reduce policyholders' surplus.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****CAPITAL RESOURCES (continued)**

Under NYIL, MBIA Insurance Corporation is also required to establish a contingency reserve to provide protection to policyholders in the event of extreme losses in adverse economic events. The amount of the reserve is based on the percentage of principal insured or premiums earned, depending on the type of obligation (net of collateral, reinsurance, refunding, refinancings and certain insured securities). Under NYIL, MBIA Insurance Corporation is required to invest its minimum surplus and contingency reserves, and 50% of its loss reserves and unearned premium reserves, in certain qualifying assets. Reductions in the contingency reserve may be recognized based on excessive reserves and under certain stipulated conditions, subject to the approval of the Superintendent of the NYSDFS. As of September 30, 2013, MBIA Insurance Corporation had a deficit of \$321 million of qualifying assets required to support its contingency reserves. The deficit was caused by the failure of certain mortgage originators to honor contractual obligations to repurchase ineligible mortgage loans from securitizations we insured thus requiring MBIA Insurance Corporation to sell liquid assets in order to make claim payments. The deficit may grow due to additional commutation and claim payments until such time as MBIA Corp. collects additional put-back recoveries. MBIA Insurance Corporation has reported the deficit to the NYSDFS. For risks associated with MBIA Insurance Corporation's failure to meet its contingency reserve requirement, see Part II, Item 1A Risk Factors Capital, Liquidity and Market Related Risk Factors. If our insurance companies fail to meet regulatory capital requirements they may become subject to regulatory action of this Quarterly Report on Form 10-Q.

As of September 30, 2013, MBIA Insurance Corporation exceeded its aggregate risk limits under the NYIL by \$61 million. The overage was caused by the decrease in statutory capital described above. MBIA Insurance Corporation plans to notify the NYSDFS of the overage and submit a plan to achieve compliance with the limits in accordance with the NYIL. If MBIA Insurance Corporation is not in compliance with its aggregate risk limits, the NYSDFS may prevent MBIA Insurance Corporation from transacting any new financial guarantee insurance business until it no longer exceeds the limitations. In 2013 and 2012, MBIA Insurance Corporation reported additional overages to the NYSDFS with respect to its single risk limits due to changes in its statutory capital.

In connection with MBIA Insurance Corporation obtaining approval from the NYSDFS to release excessive contingency reserves in previous periods, MBIA Insurance Corporation agreed that it would not pay any dividends without prior approval from the NYSDFS. Due to its significant negative earned surplus, MBIA Insurance Corporation has not had the statutory capacity to pay dividends since December 31, 2009 and is not expected to have any statutory capacity to pay any dividends in the near term.

MBIA Insurance Corporation's statutory policyholders' surplus is lower than its GAAP shareholders' equity by \$6 million as of September 30, 2013. U.S. STAT differs from GAAP in certain respects. Refer to Note 14: Statutory Accounting Practices in the Notes to Consolidated Financial Statements of MBIA Corp. within exhibit 99.2 of MBIA Inc.'s Annual Report on Form 10-K for the year ended December 31, 2012 for an explanation of the differences between U.S. STAT and GAAP.

**Claims-Paying Resources (Statutory Basis)**

CPR is a key measure of the resources available to MBIA Insurance Corporation to pay claims under its insurance policies. CPR consists of total financial resources and reserves calculated on a statutory basis. CPR has been a common measure used by financial guarantee insurance companies to report and compare resources, and continues to be used by MBIA's management to evaluate changes in such resources. We have provided CPR to allow investors and analysts to evaluate MBIA Insurance Corporation, using the same measure that MBIA's management uses to evaluate MBIA Insurance Corporation's resources to pay claims under its insurance policies. There is no directly comparable GAAP measure. Our calculation of CPR may differ from the calculation of CPR reported by other companies.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****CAPITAL RESOURCES (continued)**

MBIA Insurance Corporation's CPR and components thereto, as of September 30, 2013 and December 31, 2012 are presented in the following table:

<b>In millions</b>	<b>As of September 30, 2013</b>	<b>As of December 31, 2012</b>
Policyholders' surplus	\$ 612	\$ 965
Contingency reserves	428	493
Statutory capital	1,040	1,458
Unearned premium reserve	551	600
Present value of installment premiums <sup>(1)</sup>	841	1,035
Premium resources <sup>(2)</sup>	1,392	1,635
Net loss and LAE reserves <sup>(1)</sup>	(843)	(2,448)
Salvage reserves <sup>(3)</sup>	1,941	4,628
Gross loss and LAE reserve	1,098	2,180
Total claims-paying resources	\$ 3,530	\$ 5,273

(1) - Calculated using a discount rate of 5.72% as of September 30, 2013 and December 31, 2012.

(2) - Includes financial guarantee and insured credit derivative related premiums.

(3) - This amount primarily consists of expected recoveries related to the Company's put-back claims.

**LIQUIDITY**

As a financial services company, MBIA has been materially adversely affected by conditions in global financial markets. Current conditions and events in these markets, in addition to delays in obtaining recoveries related to ineligible mortgage loans in securitizations that we had insured, have put substantial stress on our liquidity resources.

We have utilized a liquidity risk management framework, the primary objectives of which are to monitor liquidity positions and projections in our legal entities and guide the matching of liquidity resources to needs. We monitor our cash and liquid asset resources using stress-scenario testing. Members of MBIA's senior management meet regularly to review liquidity metrics, discuss contingency plans and establish target liquidity cushions on an enterprise-wide basis. As part of our liquidity risk management framework, we evaluate and manage liquidity on a legal-entity basis to take into account the legal, regulatory and other limitations on available liquidity resources within the enterprise.

The majority of our liquidity management efforts focus on:

The liquidity resources of MBIA Inc., which are subject to: uncertainty in the timing and amount of cash inflows from dividends paid by National and MBIA Insurance Corporation; the necessity of having to meet the scheduled principal and interest on its corporate debt and investment agreements issued by the asset/liability products business; payments on derivative contracts related to the asset/liability products business; and ongoing operating expense needs. MBIA Inc. has a net debt, which comprised long-term debt, MTN s, investment agreements and derivative liabilities net of cash and investments at amortized cost and a tax receivable from subsidiaries, of \$1.3 billion as of September 30, 2013. In addition, the liquidity resources of MBIA Inc. are subject to collateralization requirements in connection with the liabilities it has issued to third parties and affiliates and in connection with third-party derivative contracts.

The liquidity resources of MBIA Corp., which are subject to: ongoing payments related to second-lien RMBS exposures; payments on its remaining CMBS exposures, due to the deterioration in such exposures; payments to counterparties in consideration for the commutation of insured transactions; payments on insured exposures that in some cases may be large bullet payments; and the availability of borrowing under the Blue Ridge Secured Loan. MBIA Corp. is currently subject to negative cash flow as a result of these payments and delays in collecting recoveries.

We also monitor the liquidity resources of National in order to ensure it maintains sufficient liquidity to pay claims and satisfy its other obligations. We do not believe there is material liquidity risk in National, although there is no assurance that there will not be material liquidity risk in National in the future in the event of material defaults and claims payments in National s insured portfolio. National s liquidity resources are subject to loss payments on its insured transactions and negative cash flow, primarily due to tax payments resulting from embedded earnings and investment income.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

In order to efficiently manage liquidity across the entire enterprise, certain of our subsidiaries, which are less liquidity constrained have entered into intercompany agreements that provide resources to subsidiaries that are more liquidity constrained. These resources include intercompany agreements described further below between our primary insurance subsidiaries and between these insurance subsidiaries and MBIA Inc., which in each case were approved by the NYSDFS and are subject to ongoing monitoring by the NYSDFS. MBIA Insurance Corporation may also draw on liquidity through the Blue Ridge Secured Loan described below.

***Key Lending Agreements*****Blue Ridge Secured Loan**

In connection with the BofA Settlement Agreement in May of 2013, MBIA Insurance Corporation and Blue Ridge entered into the Blue Ridge Secured Loan, pursuant to which Blue Ridge agreed to make revolving loans to MBIA Insurance Corporation in an aggregate amount of up to \$500 million. During the third quarter of 2013, MBIA Insurance Corporation borrowed \$50 million under this facility. As of September 30, 2013, the remaining amount available under the Blue Ridge Secured Loan was \$450 million. Refer to Note 9: Debt in the Notes to Consolidated Financial Statements for a description of prepayment conditions and other material terms of the Blue Ridge Secured Loan.

**National Secured Loan**

In 2011, National provided a \$1.1 billion National Secured Loan to MBIA Insurance Corporation in order to enable MBIA Insurance Corporation to fund settlements and commutations of its insurance policies. This loan was approved by the NYSDFS as well as by the boards of directors of MBIA Inc., MBIA Insurance Corporation and National. During 2012, MBIA Insurance Corporation borrowed an additional \$443 million under the National Secured Loan with the approval of the NYSDFS at the same terms as the original loan to fund additional commutations of its insurance policies. In connection with the BofA Settlement Agreement, in May of 2013, MBIA Insurance Corporation repaid this loan in full and it was extinguished.

**Asset Swap**

National maintains simultaneous repurchase and reverse repurchase agreements, ( Asset Swap ), with MBIA Inc. The Asset Swap provides MBIA Inc. with eligible assets to pledge under investment agreements and derivative contracts in the asset/liability products business. As of September 30, 2013, the notional amount utilized under each of these agreements was \$444 million and the fair value of collateral pledged by National and MBIA Inc. under these agreements was \$470 million and \$475 million, respectively. The net average interest rate on these transactions was 0.23% and 0.56% for the nine months ended September 30, 2013 and 2012, respectively. The NYSDFS approved the Asset Swap in connection with the re-domestication of National to New York. National has committed to the NYSDFS to use commercially reasonable efforts to reduce the amount of the Asset Swap over time.

**MBIA Insurance Corporation Secured Loan**

MBIA Insurance Corporation, as lender, maintained a master repurchase agreement, the MBIA Insurance Corporation Secured Loan, with MBIA Inc. for the benefit of MBIA Inc.'s asset/liability products business, which totaled \$2.0 billion at inception. This loan was repaid in May of 2012 and there were no further draws. This loan facility expired on May 3, 2013.

**Conduit Repurchase Agreement**

MBIA Inc. maintains a repurchase agreement with Meridian with a maximum funded amount of \$1.0 billion, subject to a pledge of collateral. As of September 30, 2013, there was no balance outstanding under this agreement.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)*****MBIA Inc. Liquidity***

MBIA Inc.'s liquidity resources support our corporate and asset/liability products segments. The activities of MBIA Inc. consist of holding and managing investments, servicing outstanding corporate debt instruments, investment agreements and MTNs issued by the asset/liability products and conduit segments, posting collateral under financing and hedging arrangements and investment agreements, making payments and collateral postings related to interest rate and foreign exchange swaps, and paying operating expenses. The primary sources of cash within MBIA Inc. used to meet its liquidity needs include available cash and liquid assets not subject to collateral posting requirements, scheduled principal and interest on assets held in its investment portfolio, dividends from subsidiaries, payments under tax sharing agreements with these subsidiaries (once the payments become unrestricted) and the ability to issue debt and equity. There can be no assurance as to the amount and timing of any such dividends or payments under the tax sharing agreements. MBIA Inc.'s corporate debt, investment agreements, and derivatives and the GFL MTNs may be accelerated by the holders of such instruments upon the occurrence of certain events, such as a breach of covenant or representation, a bankruptcy of MBIA Inc., in the case of the corporate debt, investment agreements and derivatives, the filing of an insolvency proceeding with respect to National, in the case of the corporate debt, a bankruptcy of GFL, in the case of the GFL MTNs, or the filing of an insolvency proceeding with respect to MBIA Insurance Corporation, in the cases of the investment agreements and GFL MTNs. MBIA Inc.'s obligations under its loans from GFL may be accelerated only upon the occurrence of a bankruptcy or liquidation of MBIA Inc. Refer to Note 11: Business Segments in the Notes to Consolidated Financial Statements for a description of the GFL loans and MTNs. In the event of any acceleration of all of our obligations, including under our corporate debt, investment agreements, GFL MTNs, or derivatives, we likely would not have sufficient liquid resources to pay amounts due. We provided the NYSDFS with notice of our intention to have National pay a dividend in the fourth quarter of 2013. Subsequent to September 30, 2013, National declared and paid a dividend of \$214 million to its ultimate parent, MBIA Inc. Refer to the Capital Resources Insurance Statutory Capital section for additional information on this dividend.

During the nine months ended September 30, 2013, pursuant to the tax sharing agreement, National settled its taxes related to the 2012 tax year of \$16 million with MBIA Inc. In addition, National paid to MBIA Inc. estimated 2013 taxes of \$81 million. Consistent with the tax sharing agreement, this amount was placed in an escrow account until the expiration of National's two-year NOL carry-back period under U.S. tax rules. At the expiration of National's carry-back period, any funds remaining after any reimbursement to National in respect of any NOL carry-backs would be available for general corporate purposes, including to satisfy any other obligations under the tax sharing agreement. During the first nine months of 2013, MBIA Inc. received \$115 million that was previously held in escrow under the MBIA group tax sharing agreement. The amount represents National's liability under the tax sharing agreement for the 2010 tax year, and was released pursuant to the terms of the agreement following the expiration of National's two-year NOL carry-back period under U.S. tax rules. As of September 30, 2013, \$427 million remained in escrow for the 2011 through the 2013 tax years. We expect to release up to \$160 million of this escrow related to the 2011 tax year in January 2014 which will increase MBIA Inc.'s liquidity position.

MBIA Inc. is subject to material liquidity risks and uncertainty. To mitigate these risks, we seek to maintain cash and liquidity resources that we believe will be sufficient to make all payments due on our obligations and to meet other financial requirements, such as posting collateral, at least through the next twelve months.

Liquidity risk within MBIA Inc. is primarily a result of the following factors:

Currently, the majority of the cash and securities of MBIA Inc. is pledged against investment agreement liabilities, intercompany financing arrangements and derivatives, which limit its ability to raise liquidity through asset sales. A significant portion of MBIA Inc.'s assets that are pledged against intercompany financing arrangement liabilities are structured finance securities which have been particularly susceptible to price fluctuations during periods of market volatility. In addition, if the market value or rating eligibility of the assets which are pledged against MBIA Inc.'s obligations were to decline, we would be required to pledge additional eligible assets in order to meet minimum required collateral amounts against these liabilities. In such event, we may sell additional assets, potentially with substantial losses, finance unencumbered assets through intercompany facilities, or use free cash or other assets, in some cases with NYSDFS approval, although there can be no assurance that these strategies will be available or adequate to meet

liquidity requirements.

Uncertainty of the timing and amount of cash inflows from dividends paid by MBIA's principal operating subsidiaries. Refer to the Capital Resources-Insurance Statutory Capital section for a discussion on our insurance subsidiaries' dividend restrictions.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

Because most of MBIA Inc.'s assets are pledged against the obligations described above, the widening of credit spreads would have an adverse impact on the market value of these assets and increase collateralization requirements for the portfolio. The following table presents the estimated pre-tax change in the aggregate fair value of the asset/liability products business's assets as of September 30, 2013 from instantaneous shifts in credit spread curves. This table assumes that all credit spreads move by the same amount; however, it is more likely that the actual changes in credit spreads will vary by investment sector and individual security. The table presents hypothetical increases and decreases in credit spreads of 50 and 200 basis points. Because downward movements of these amounts in some cases would result in negative spreads, a floor was assumed for minimum spreads.

In millions	Change in Credit Spreads (Asset/Liability Products Business)			
	200 Basis Point Decrease	50 Basis Point Decrease	50 Basis Point Increase	200 Basis Point Increase
Estimated change in fair value	\$ 96	\$ 31	\$ (29)	\$ (107)

During the first nine months of 2013, MBIA Inc. maintained three intercompany financing facilities to provide it with additional resources to meet its liquidity requirements within the asset/liability products business: the Asset Swap, the MBIA Insurance Corporation Secured Loan and the Conduit Repurchase Agreement. The MBIA Insurance Corporation Secured Loan expired in May of 2013. Refer to the preceding "Key Lending Agreements" section for a description of these facilities.

We believe that asset sales undertaken to date have reduced volatility in MBIA Inc.'s portfolio in the event of stressed market conditions. However, stressed credit market conditions could cause MBIA Inc. to have insufficient resources to cover collateral and/or other liquidity requirements. Management has identified certain actions to mitigate this risk. These contingent actions include: (1) accessing the capital markets; (2) additional sales of invested assets exposed to credit spread stress risk, which may occur at losses and increase MBIA Inc.'s net debt; (3) termination and settlement of interest rate swap agreements; and (4) other available advances from subsidiaries. These actions, if taken, are expected to result in either additional liquidity or reduced exposure to adverse credit spread movements. There can be no assurance that these actions will be sufficient to fully mitigate this risk. In the event that we cannot implement the contingent actions identified above to raise liquidity, we may have insufficient assets to make all payments on our obligations as they come due, which could result in a default by MBIA Inc. on its obligations and the potential for MBIA Corp., as guarantor of the investment agreements and GFL MTNs, to be called upon to satisfy obligations on those instruments as they come due. In addition, the Company expects that MBIA Inc. will generate sufficient cash to satisfy its net debt and its general corporate needs over time from distributions from its operating subsidiaries and by raising third-party capital, although there can be no assurance that such factors will generate sufficient cash to satisfy its net debt.

As of September 30, 2013, the liquidity position of MBIA Inc., which consists of the liquidity positions of its corporate and asset/liability products activities, was \$282 million and comprised cash and liquid assets of \$228 million available for general corporate liquidity purposes, excluding the amounts held in escrow under its tax sharing agreement, and \$54 million not pledged directly as collateral for its asset/liability products activities. As of December 31, 2012, MBIA Inc. had \$239 million of cash and liquid assets comprising \$170 million available for general corporate liquidity purposes, excluding the amounts held in escrow under its tax sharing agreement, and \$69 million not pledged directly as collateral for its asset/liability products activities. We believe this liquidity position provides MBIA Inc. with sufficient funds to cover expected obligations at least through the next twelve months.

**MBIA Corp. Liquidity**

Liquidity available in the structured finance and international insurance segment is affected by our ability to collect on recoveries associated with loss payments, the payment of claims on insured exposures, payments made to commute insured exposures, the repayment of outstanding borrowings, a reduction in investment income, any unanticipated expenses, or the impairment or a significant decline in the fair value of invested assets. We may also experience liquidity constraints as a result of NYIL requirements that we maintain specified, high quality assets to back our

reserves and surplus.

We believe the current liquidity position of MBIA Corp. is adequate to make expected future claim payments. MBIA Corp.'s liquidity position has been substantially strengthened as a result of the BofA Settlement Agreement, including the elimination of potential claims on Bank of America/Merrill Lynch CMBS exposures and the execution of the Blue Ridge Secured Loan entered into in May of 2013. The liquidity position of MBIA Corp. has been stressed due to ongoing payments on second-lien RMBS exposures, payments on its remaining CMBS exposures and the payments to counterparties in consideration for the commutation of insured transactions, which have resulted in a substantial reduction of exposure and potential loss volatility. While MBIA Corp. has made and may in the future make payments to counterparties in consideration for the commutation of insured transactions, MBIA Corp.'s ability to commute insured transactions will depend on management's assessment of available liquidity or ability to secure other sources of financing. Depending on the amounts of claims on policies issued by MBIA Corp., MBIA Corp. may not have sufficient liquid assets to pay such claims when due.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

Payment requirements for the structured finance and international financial guarantee contracts fall into three categories: (i) timely interest and ultimate principal; (ii) ultimate principal only at final maturity; and (iii) payments upon settlement of individual collateral losses as they occur after any deductible or subordination has been exhausted, which payments are unscheduled and therefore more difficult to predict, and which category applies to most of the transactions on which we have recorded loss reserves. Insured transactions that require payment in full of the principal insured at maturity could present liquidity risks for MBIA Corp. since payment of the principal is due at maturity but any salvage could be recovered over time after payment of the principal amount. MBIA Corp. has insured transactions with substantial principal amounts due at maturity that are scheduled to mature in the near term. MBIA Corp. expects the transactions to be repaid on or prior to the maturity date. MBIA Corp. is generally required to satisfy claims within one to three business days, and as a result seeks to identify potential claims in advance through our monitoring process. While our financial guarantee policies generally cannot be accelerated, thereby helping to mitigate liquidity risk, the insurance of CDS contracts may, in certain circumstances, including the occurrence of certain insolvency or payment defaults under the CDS contracts, be subject to termination by the counterparty, triggering a claim for the fair value of the contract. In order to monitor liquidity risk and maintain appropriate liquidity resources, we use the same methodology as we use to monitor credit quality and losses within our insured portfolio, including stress scenarios. Refer to Note 5: Loss and Loss Adjustment Expense Reserves in the Notes to Consolidated Financial Statements for a discussion of our loss process.

Our structured finance and international insurance segment also requires cash for the payment of operating expenses, as well as principal and interest related to its surplus notes. Pursuant to Section 1307 of the NYIL and the Fiscal Agency Agreement governing MBIA Corp.'s surplus notes, any payment on the notes may be made only with the prior approval of the Superintendent of the NYSDFS whenever, in his judgment, the financial condition of [MBIA Corp.] warrants and payment may be made only out of MBIA Corp.'s free and divisible surplus. If these conditions are not met, MBIA Corp. is not permitted to make any applicable interest payment and no default or event of default would occur under the Fiscal Agency Agreement or any of the Company's other agreements. From the January 15, 2013 interest payment to the present, MBIA Corp.'s requests for approval of the note interest payments have not been approved by the NYSDFS. In accordance with the terms of the Fiscal Agency Agreement, MBIA Corp. is required to provide, and has provided, notice to the Fiscal Agent that it has not made these scheduled interest payments. The deferred interest payments will become due on the first business day on or after which MBIA Corp. obtains approval to make such payments. No interest will accrue on the deferred interest. There can be no assurance that the NYSDFS will approve these or any subsequent interest payments, or that it will approve any principal payments at maturity or any optional redemption payment that MBIA Corp. may seek to make. Subsequent to September 30, 2013, S&P revised their criteria related to the ratings for certain hybrid capital instruments. As a result, S&P lowered the ratings of MBIA Corp.'s surplus notes and MBIA Corp.'s preferred stock to D.

Since the fourth quarter of 2007 through September 30, 2013, MBIA Corp. has made \$13.5 billion of cash payments, before reinsurance and collections and excluding LAE (including payments made to debt holders of consolidated VIEs), associated with second-lien RMBS securitizations and with commutations and claim payments primarily relating to CDS contracts. These cash payments include loss payments of \$1.0 billion made on behalf of MBIA Corp.'s consolidated VIEs. Of the \$13.5 billion, MBIA Corp. has paid \$6.9 billion of gross claims (before reinsurance and collections and excluding LAE) on policies insuring second-lien RMBS securitizations, driven primarily by an extensive number of ineligible mortgage loans being placed in the securitizations in breach of the representations and warranties of the sellers/servicers. In addition, MBIA Corp. has paid \$6.6 billion of gross settlement and claim payments (before reinsurance and collections and excluding LAE) on insured credit derivatives. Also, since the fourth quarter of 2007 through September 30, 2013, MBIA Corp. has collected \$1.8 billion in cash and securities related to put-back recoveries and \$224 million of excess spread before reinsurance.

MBIA Corp. is seeking to enforce its rights to have mortgage sellers/servicers cure, replace or repurchase ineligible mortgage loans from securitizations and has recorded a total of \$1.1 billion of related expected recoveries on our consolidated balance sheets as of September 30, 2013, including expected recoveries recorded in our consolidated VIEs. To date, the Company has resolved or agreed to resolve substantially all of its claims related to ineligible loans, with the exception of those loans securitized by Credit Suisse Securities (USA) LLC. However, there can be no assurance that we will be successful or that we will not be delayed in realizing these recoveries. Such risks are contemplated in the scenarios we utilize to calculate these recoveries, which are recognized on our consolidated balance sheets. We collected our put-back claim against Bank of America in May of 2013, which substantially reduced our remaining consolidated expected recoveries. In May of 2013, MBIA Insurance Corporation also consented to a plan to resolve its claims against ResCap and certain of its affiliates. We anticipate that we will receive an initial distribution of funds from ResCap in late 2013 or early 2014, which will further substantially reduce our remaining consolidated expected recoveries. The Plan is subject to bankruptcy court approval. This anticipated timeline may change due to developments

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related to the Junior Secured Note litigation which occurred in October of 2013 or other matters that develop in the course of events in the bankruptcy court plan confirmation process. Furthermore, there can be no assurance that the Plan will ultimately be approved in its current form, or that MBIA will receive its expected recoveries. Refer to Note 5: Loss and Loss Adjustment Expense Reserves in the Notes to Consolidated Financial Statements for a discussion of the claims related to Credit Suisse Securities (USA) LLC and the ResCap agreement.



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

A portion of the commutation payments made since the fourth quarter of 2011 were financed through the National Secured Loan, which was paid in full and extinguished in May of 2013 in connection with the BofA Settlement Agreement and the settlement of Flagstar Bank's put-back obligation. Future commutation payments may be financed through draws on the Blue Ridge Secured Loan subject to its continued availability. MBIA Insurance Corporation's ability to repay the Blue Ridge Secured Loan and any accrued interest will be largely dependent on MBIA Corp.'s ability to collect on its future receivables, including its ability to successfully enforce its rights to have the mortgage sellers/servicers cure, replace or repurchase ineligible mortgage loans from insured securitizations.

MBIA Corp. also insures third-party holders of our asset/liability products segment's obligations. MBIA Insurance Corporation, as lender, maintained a master repurchase agreement, the MBIA Insurance Corporation Secured Loan, with MBIA Inc. for the benefit of MBIA Inc.'s asset/liability products business, which totaled \$2.0 billion at inception. This loan was repaid in May of 2012 and there were no further draws. This loan facility expired on May 3, 2013.

As of September 30, 2013, MBIA Corp. held cash and available-for-sale investments of \$866 million, of which \$97 million comprised cash and highly liquid assets that was immediately available to MBIA Insurance Corporation. Included in the \$866 million was \$634 million of cash and available-for-sale investments held by its subsidiaries and not immediately available to MBIA Insurance Corporation. In connection with the BofA Settlement Agreement, MBIA Insurance Corporation entered into the Blue Ridge Secured Loan, which provides MBIA Corp. with an additional maximum amount of \$500 million in liquidity. During the third quarter of 2013, MBIA Insurance Corporation borrowed \$50 million from this facility at 7.76%. As of September 30, 2013, the remaining amount available under the Blue Ridge Secured Loan was \$450 million. As of December 31, 2012, MBIA Corp. held cash and available-for-sale investments of \$1.3 billion, of which \$345 million comprised cash and highly liquid assets that was immediately available to MBIA Insurance Corporation. Included in the \$1.3 billion was \$659 million of cash and available-for-sale investments held by its subsidiaries and not immediately available to MBIA Insurance Corporation. We believe that MBIA Corp.'s liquidity resources, including expected cash inflows, will adequately provide for anticipated cash outflows. Depending on the amount of actual claims on the policies issued by MBIA Corp., including claims on insured exposures that in some cases may require large bullet payments, MBIA Corp. may not have sufficient liquid assets to pay such claims. In the event of unexpected liquidity requirements, we may have insufficient resources to meet our obligations or insufficient qualifying assets to support our surplus and reserves, and may seek to increase our cash holdings position by drawing on the Blue Ridge Secured Loan or raising external capital, and there can be no assurance that we will be able to draw on these additional sources of liquidity.

***National Liquidity***

Despite continued adverse macroeconomic conditions in the U.S., the incidence of default among U.S. public finance issuers remains extremely low and we believe that the liquidity position of our U.S. public finance insurance segment is sufficient to meet cash requirements in the ordinary course of business.

Liquidity risk arises in our U.S. public finance insurance segment primarily from the following:

The insurance policies issued or reinsured by National, the entity from which we conduct our U.S. public finance insurance business, provide unconditional and irrevocable guarantees of payments of the principal of, and interest or other amounts owing on, insured obligations when due or, in the event that the insurance company has the right, at its discretion, to accelerate the payment under its policies upon the acceleration of the underlying insured obligations due to default or otherwise. In the event of a default in payment of principal, interest or other insured amounts by an issuer, National generally promises to make funds available in the insured amount within one to three business days following notification. In some cases, the amount due can be substantial, particularly if the default occurs on a transaction to which National has a large notional exposure or on a transaction structured with large, bullet-type principal maturities. The fact that the U.S. public finance insurance segment's financial guarantee contracts generally cannot be accelerated by a party other than the insurer helps to mitigate liquidity risk in this segment.

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National has entered into certain intercompany transactions to support the liquidity needs of its affiliates. One of these transactions includes the Asset Swap through which National exchanges liquid assets with MBIA Inc. As a result of this transaction, National is subject to repayment risk, which may adversely affect its liquidity. In addition, changes in the market value of securities sold to National under its Asset Swap with the asset/liability products business may adversely affect its liquidity position if MBIA Inc. were unable to pledge additional eligible assets in order to meet minimum required collateral amounts.

National held cash and short-term investments of \$1.5 billion as of September 30, 2013, which was highly liquid and consisted predominantly of highly rated municipal, U.S. agency and corporate bonds. As of December 31, 2012, National held cash and short-term investments of \$470 million, of which \$419 million was highly liquid and consisted predominantly of highly rated municipal, U.S. agency and corporate bonds.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)*****Consolidated Cash Flows***

Information about our consolidated cash flows by category is presented on our consolidated statements of cash flows. The following table presents a summary of our consolidated cash flows for the nine months ended September 30, 2013 and 2012:

In millions	Nine Months Ended September 30,		Percent Change
	2013	2012	
Net cash provided (used) by:			
Operating activities	\$ 1,033	\$ (955)	n/m
Investing activities	297	3,106	-90%
Financing activities	(1,224)	(2,343)	-48%

n/m - Percent change not meaningful.

***Operating activities***

Net cash provided by operating activities increased for the nine months ended September 30, 2013 when compared with the same period of 2012 primarily due to an increase in financial guarantee recoveries received and decreases in losses and loss adjustment expense and interest expense paid. This is partially offset by a decrease in cash received from investment income.

***Investing activities***

Net cash provided by investing activities decreased for the nine months ended September 30, 2013 when compared with the same period of 2012 primarily due to declines in proceeds from net sales and redemptions of securities for purposes of funding commutation and loss payments.

***Financing activities***

Net cash used by financing activities decreased for the nine months ended September 30, 2013 when compared with the same period of 2012 primarily due to decreases in payments for drawdowns of investment agreements, payments to retire debt related to our conduit segment, and payments for securities sold under agreements to repurchase.

***Investments***

The following discussion of investments, including references to consolidated investments, excludes cash and investments reported under Assets of consolidated variable interest entities on our consolidated balance sheets. Cash and investments of VIEs support the repayment of VIE obligations and are not available to settle obligations of MBIA.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

Our available-for-sale investments comprise high-quality fixed-income securities and short-term investments. As of September 30, 2013 and December 31, 2012, the fair values of our consolidated available-for-sale investments were \$6.2 billion and \$5.6 billion, respectively, as presented in the following table. Additionally, consolidated cash and cash equivalents as of September 30, 2013 and December 31, 2012 were \$1.1 billion and \$814 million, respectively.

<b>In millions</b>	<b>As of September 30, 2013</b>	<b>As of December 31, 2012</b>	<b>Percent Change</b>
Available-for-sale investments:			
U.S. public finance insurance			
Amortized cost	\$ 4,496	\$ 3,006	50%
Unrealized net gain (loss)	(54)	105	n/m
Fair value	4,442	3,111	43%
Structured finance and international insurance			
Amortized cost	524	886	-41%
Unrealized net gain (loss)	16	22	-27%
Fair value	540	908	-41%
Corporate			
Amortized cost	468	543	-14%
Unrealized net gain (loss)	(57)	(36)	58%
Fair value	411	507	-19%
Advisory services			
Amortized cost	5	11	-55%
Unrealized net gain (loss)	-	-	-%
Fair value	5	11	-55%
Wind-down operations			
Amortized cost	794	1,039	-24%
Unrealized net gain (loss)	29	20	45%
Fair value	823	1,059	-22%
Total available-for-sale investments:			
Amortized cost	6,287	5,485	15%
Unrealized net gain (loss)	(66)	111	n/m
Total available-for-sale investments at fair value	6,221	5,596	11%



**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

In millions	As of September 30, 2013	As of December 31, 2012	Percent Change
Investments carried at fair value:			
U.S. public finance insurance			
Amortized cost	185	190	-3%
Unrealized net gain (loss)	(8)	-	n/m
Fair value	177	190	-7%
Structured finance and international insurance			
Amortized cost	27	27	-%
Unrealized net gain (loss)	2	3	-33%
Fair value	29	30	-3%
Corporate			
Amortized cost	60	38	58%
Unrealized net gain (loss)	(3)	(10)	-70%
Fair value	57	28	104%
Advisory services			
Amortized cost	4	4	-%
Unrealized net gain (loss)	1	-	n/m
Fair value	5	4	25%
Wind-down operations			
Amortized cost	-	5	-100%
Unrealized net gain (loss)	-	-	-%
Fair value	-	5	-100%
Total investments carried at fair value:			
Amortized cost	276	264	5%
Unrealized net gain (loss)	(8)	(7)	14%
Total investments carried at fair value	268	257	4%
Other investments at amortized cost:			
U.S. public finance insurance operations segment	6	9	-33%
Total other investments at amortized cost	6	9	-33%
Consolidated investments at carrying value	\$ 6,495	\$ 5,862	11%

n/m - Percent change not meaningful.

The fair value of the Company's investments is based on prices which include quoted prices in active markets and prices based on market-based inputs that are either directly or indirectly observable, as well as prices from dealers in relevant markets. Differences between fair value and amortized cost arise primarily as a result of changes in interest rates and general market credit spreads occurring after a fixed-income security is purchased, although other factors may also influence fair value, including specific credit-related changes, supply and demand forces and other market factors. When the Company holds an available-for-sale investment to maturity, any unrealized gain or loss currently recorded in accumulated other comprehensive income (loss) in the shareholders' equity section of the balance sheet is reversed. As a result, the Company would realize a value substantially equal to amortized cost. However, when investments are sold prior to maturity, the Company will realize any difference between amortized cost and the sale price of an investment as a realized gain or loss within its consolidated statements of operations.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)***Credit Quality*

The credit quality distribution of the Company's available-for-sale fixed-maturity investment portfolios, excluding short-term investments, based on ratings from Moody's as of September 30, 2013 is presented in the following table. Alternate ratings sources, such as S&P or the best estimate of the ratings assigned by the Company, have been used for a small percentage of securities that are not rated by Moody's.

In millions	U.S. Public Finance		Structured Finance and International		Advisory Services		Corporate		Wind-down Operations		Total	
	% of Fixed-		% of Fixed-		% of Fixed-		% of Fixed-		% of Fixed-		% of Fixed-	
	Fair Value	Income Investments	Fair Value	Income Investments	Fair Value	Income Investments	Fair Value	Income Investments	Fair Value	Income Investments	Fair Value	Income Investments
Available-for-sale:												
Aaa	\$ 1,494	43%	\$ 210	63%	\$ 1	50%	\$ -	0%	\$ 191	26%	\$ 1,896	40%
Aa	1,118	33%	85	26%	-	0%	2	1%	107	15%	1,312	28%
A	533	16%	11	3%	1	50%	10	5%	208	28%	763	16%
Baa	118	3%	6	2%	-	0%	2	1%	201	27%	327	7%
Below investment grade	27	1%	17	5%	-	0%	157	82%	16	2%	217	5%
Not rated	143	4%	3	1%	-	0%	20	11%	15	2%	181	4%
Total	\$ 3,433	100%	\$ 332	100%	\$ 2	100%	\$ 191	100%	\$ 738	100%	\$ 4,696	100%
Short-term investments	1,003		207		2		221		82		1,515	
Investments carried at fair value	177		29		5		57		-		268	
Other investments	11		1		1		-		3		16	
Consolidated investments at carrying value	\$ 4,624		\$ 569		\$ 10		\$ 469		\$ 823		\$ 6,495	

As of September 30, 2013, the weighted average credit quality of the Company's available-for-sale investment portfolios, excluding short-term and other investments, as presented in the preceding table are as follows:

	U.S. Public Finance	Structured Finance and International Insurance	Advisory Services	Corporate	Wind-down Operations
Weighted average credit quality ratings	Aa	Aa	Aa	Below investment grade	A
<i>Insured Investments</i>					



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MBIA's consolidated investment portfolio includes investments that are insured by various financial guarantee insurers ( Insured Investments ), including investments insured by MBIA Corp. and National ( Company-Insured Investments ). As of September 30, 2013, Insured Investments at fair value represented \$643 million or 10% of consolidated investments, of which \$393 million or 7% of consolidated investments were Company-Insured Investments.

As of September 30, 2013, based on the actual or estimated underlying ratings of our consolidated investment portfolio, without giving effect to financial guarantees, the weighted average rating of the consolidated investment portfolio would be in the Aa range, the weighted average rating of only the Insured Investments in the investment portfolio would be in the Baa range, and 3% of the total investment portfolio would be rated below investment grade in the Insured Investments.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

The distribution of our Insured Investments by financial guarantee insurer as of September 30, 2013 is presented in the following table:

In millions	U.S. Public Finance		Structured Finance and International		Corporate		Wind-Down Operations		Total	
	Fair Value	% of Total Investments	Fair Value	% of Total Investments	Fair Value	% of Total Investments	Fair Value	% of Total Investments	Fair Value	% of Total Investments
MBIA Corp.	\$ -	0%	\$ -	0%	\$ 106	2%	\$ 117	2%	\$ 223	4%
National	65	1%	-	0%	-	0%	105	2%	170	3%
Assured Guaranty Municipal Corp.	56	1%	-	0%	-	0%	123	2%	179	3%
Ambac Financial Group, Inc.	9	0%	-	0%	8	0%	24	0%	41	0%
FGIC	3	0%	3	0%	15	0%	6	0%	27	0%
Other	3	0%	-	0%	-	0%	-	0%	3	0%
Total	\$ 136	2%	\$ 3	0%	\$ 129	2%	\$ 375	6%	\$ 643	10%

In purchasing Insured Investments, the Company independently assesses the underlying credit quality, structure and liquidity of each investment, in addition to the creditworthiness of the insurer. Insured Investments are diverse by sector, issuer and size of holding. The Company assigns underlying ratings to its Insured Investments without giving effect to financial guarantees based on underlying ratings assigned by Moody's, or another external agency when a rating is not published by Moody's. When an external underlying rating is not available, the underlying rating is based on the Company's best estimate of the rating of such investment. A downgrade of a financial guarantee insurer will likely have an adverse effect on the fair value of investments insured by the downgraded financial guarantee insurer. If MBIA determines that declines in the fair values of Insured Investments are other-than-temporary, the Company will record a realized loss through earnings.

The underlying ratings of the Company-Insured Investments as of September 30, 2013 are reflected in the following table. Amounts represent the fair value of such investments including the benefit of the MBIA guarantee. The ratings in the following table are based on ratings from Moody's. Alternate ratings sources, such as S&P, have been used for a small percentage of securities that are not rated by Moody's.

In millions						
		U.S. Public Finance Insurance	Structured Finance and International Insurance	Corporate	Wind-down Operations	Total
Underlying Ratings Scale						
National:						
Aa		\$ 30	\$ -	\$ -	\$ 14	\$ 44
A		35	-	-	16	51
Baa		-	-	-	75	75
Total National		\$ 65	\$ -	\$ -	\$ 105	\$ 170
MBIA Corp.:						
Aa		\$ -	\$ -	\$ -	\$ 56	\$ 56
A		-	-	-	12	12

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Baa	-	-	3	49	52
Below investment grade	-	-	103	-	103
<b>Total MBIA Corp.</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 106</b>	<b>\$ 117</b>	<b>\$ 223</b>
 Total MBIA Insured Investments	 \$ 65	 \$ -	 \$ 106	 \$ 222	 \$ 393

Without giving effect to the MBIA guarantee of the Company-Insured Investments in the consolidated investment portfolio, as of September 30, 2013, based on actual or estimated underlying ratings, the weighted average rating of the consolidated investment portfolio was in the Aa range, the weighted average rating of only the Company-Insured Investments was in the Baa range, and investments rated as below investment grade in the Company-Insured Investments were 2% of the total consolidated investment portfolio.

### *Impaired Investments*

As of September 30, 2013 and December 31, 2012, we held impaired available-for-sale investments (investments for which fair value was less than amortized cost) with a fair value of \$2.5 billion and \$1.3 billion, respectively.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****LIQUIDITY (continued)**

We analyze impaired investments within our investment portfolio for other-than-temporary impairments on a quarterly basis. Key factors considered when assessing other-than-temporary impairments include but are not limited to: (a) structural and economic factors among security types that represent our largest exposure to credit impairment losses; (b) the duration and severity of the unrealized losses (i.e., a decline in the market value of a security by 20% or more at the time of the review, or 5% impaired at the time of review with a fair value below amortized cost for a consecutive 12-month period); and (c) the results of various cash flow modeling techniques. Our cash flow analysis considers all sources of cash, including credit enhancement, that support the payment of amounts owed by an issuer of a security. This includes the consideration of cash expected to be provided by financial guarantors, including MBIA Corp., resulting from an actual or potential insurance policy claim.

Refer to Note 7: Investments in the Notes to Consolidated Financial Statements for a detailed discussion about impaired investments.

**Debt Obligations**

Principal payments due under our debt obligations for the three months ending December 31, 2013 and each of the subsequent four years ending December 31 and thereafter are presented in the following table. The repayment of principal on our surplus notes is reflected in 2018, which is the next call date. Principal payments under investment agreements are based on expected withdrawal dates. All other principal payments are based on contractual maturity dates. Foreign currency denominated liabilities are presented in U.S. dollars using applicable exchange rates as of September 30, 2013, and liabilities issued at a discount reflect principal amounts due at maturity.

	As of September 30, 2013						
	Three Months						
	Ending						
	December 31,						
In millions	2013	2014	2015	2016	2017	Thereafter	Total
Structured finance and international insurance segment:							
Variable interest entity notes	\$ 97	\$ 333	\$ 439	\$ 324	\$ 387	\$ 4,109	\$ 5,689
Surplus notes	-	-	-	-	-	940	940
Blue Ridge secured loan	50	-	-	-	-	-	50
Corporate segment:							
Long-term debt	-	-	-	-	-	583	583
Asset/liability products segment:							
Investment agreements	37	136	44	49	57	518	841
Medium-term notes	17	32	239	131	54	1,710	2,183
Conduit segment:							
Medium-term notes	-	-	-	-	-	149	149
Total	\$ 201	\$ 501	\$ 722	\$ 504	\$ 498	\$ 8,009	\$ 10,435

**Table of Contents****Item 3. Quantitative and Qualitative Disclosures About Market Risk**

In general, MBIA's market risk relates to changes in the value of financial instruments that arise from adverse movements in factors such as interest rates, foreign exchange rates and credit spreads. MBIA is exposed to changes in interest rates, foreign exchange rates and credit spreads that affect the fair value of its financial instruments, namely investment securities, investment agreement liabilities, MTNs, debentures and certain derivative transactions. The Company's investment portfolio holdings are primarily U.S. dollar-denominated fixed-income securities including municipal bonds, U.S. government bonds, MBS, collateralized mortgage obligations, corporate bonds and ABS. In periods of rising and/or volatile interest rates, foreign exchange rates and credit spreads, profitability could be adversely affected should the Company have to liquidate these securities.

MBIA minimizes its exposure to interest rate risk, foreign exchange risk and credit spread movement through active portfolio management to ensure a proper mix of the types of securities held and to stagger the maturities of its fixed-income securities. In addition, the Company enters into various swap agreements that hedge the risk of loss due to interest rate and foreign currency volatility.

**Interest Rate Sensitivity**

Interest rate sensitivity can be estimated by projecting a hypothetical instantaneous increase or decrease in interest rates. The following table presents the estimated pre-tax change in fair value of the Company's financial instruments as of September 30, 2013 from instantaneous shifts in interest rates:

In millions	Change in Interest Rates					
	300 Basis	200 Basis	100 Basis	100 Basis	200 Basis	300 Basis
	Point Decrease	Point Decrease	Point Decrease	Point Increase	Point Increase	Point Increase
Estimated change in fair value	\$ (51)	\$ (12)	\$ 6	\$ (34)	\$ (71)	\$ (111)

**Foreign Exchange Sensitivity**

Foreign exchange rate sensitivity can be estimated by projecting a hypothetical instantaneous increase or decrease in foreign exchange rates. The following table presents the estimated pre-tax change in fair value of the Company's financial instruments as of September 30, 2013 from instantaneous shifts in foreign exchange rates:

In millions	Change in Foreign Exchange Rates			
	Dollar Weakens		Dollar Strengthens	
	20%	10%	10%	20%
Estimated change in fair value	\$ (51)	\$ (26)	\$ 26	\$ 51

**Credit Spread Sensitivity**

Credit spread sensitivity can be estimated by projecting a hypothetical instantaneous increase or decrease in credit spreads. The following table presents the estimated pre-tax change in fair value of the Company's financial instruments as of September 30, 2013 from instantaneous shifts in credit spread curves. For this table it was assumed that all credit spreads move by the same amount. It is more likely that the actual changes in credit spreads will vary by security. National's investment portfolio would generally be expected to experience lower credit spread volatility than the investment portfolio of the asset/liability products segment because of higher credit quality and portfolio composition in sectors that have been less volatile historically. The table shows hypothetical increases and decreases in credit spreads of 50 and 200 basis points. Because downward movements of these amounts in some cases would result in negative spreads, a floor was assumed for minimum spreads. The changes in fair value reflect partially offsetting effects as the value of the investment portfolios generally changes in an opposite direction from the liability portfolio.



**Table of Contents****Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)**

	Change in Credit Spreads			
	200 Basis Point Decrease	50 Basis Point Decrease	50 Basis Point Increase	200 Basis Point Increase
<b>In millions</b>				
Estimated change in fair value	\$ (44)	\$ 35	\$ (59)	\$ (259)
<b>Credit Derivatives Sensitivity</b>				

MBIA issued insurance policies insuring payments due on structured credit derivative contracts and directly entered into credit derivative contracts, which are marked-to-market through earnings under the accounting principles for derivatives and hedging activities. All these transactions were insured by the Company's structured finance and international insurance operations. The majority of these structured CDSs related to structured finance transactions with underlying reference obligations of cash securities and CDSs referencing liabilities of corporations or of other structured finance securitizations. The asset classes of the underlying reference obligations included corporate, ABS, RMBS and CMBS. These transactions were usually underwritten at or above a triple-A credit rating level. As of September 30, 2013, approximately 29% of the tranches insured by the Company were rated triple-A.

In the first nine months of 2013, MBIA Corp. has observed a tightening of its own credit spreads. As changes in fair value can be caused by factors unrelated to the performance of MBIA Corp.'s business and credit portfolio, including general market conditions and perceptions of credit risk, as well as market use of credit derivatives for hedging purposes unrelated to the specific referenced credits in addition to events that affect particular credit derivative exposures, the application of fair value accounting will cause the Company's earnings to be more volatile than would be suggested by the underlying performance of MBIA's business operations and credit portfolio.

The following tables reflect sensitivities to changes in credit spreads, collateral prices, rating migrations, recovery rates and MBIA Corp.'s own credit spreads and recovery rates. Each table stands on its own and should be read independently of each other. Refer to Note 6: Fair Value of Financial Instruments in the Notes to Consolidated Financial Statements for further information about the Company's financial assets and liabilities that are accounted for at fair value, including valuation techniques and disclosures required by GAAP.

Sensitivity to changes in credit spreads can be estimated by projecting a hypothetical instantaneous shift in credit spread curves. The following table presents the estimated pre-tax change in fair value and the cumulative estimated net fair value of MBIA Corp.'s credit derivatives portfolio of instantaneous shifts in credit spreads as of September 30, 2013. In scenarios where credit spreads decreased, a floor of zero was used.

	Change in Credit Spreads (Structured Finance and International Insurance)						
	600 Basis Point Decrease	200 Basis Point Decrease	50 Basis Point Decrease	0 Basis Point Change	50 Basis Point Increase	200 Basis Point Increase	600 Basis Point Increase
<b>In millions</b>							
Estimated pre-tax net gains (losses)	\$ 613	\$ 286	\$ 74	\$ -	\$ (76)	\$ (306)	\$ (925)
Estimated net fair value	\$ (750)	\$ (1,077)	\$ (1,289)	\$ (1,363)	\$ (1,439)	\$ (1,669)	\$ (2,288)

Actual shifts in credit spread curves will vary based on the credit quality of the underlying reference obligations. In general, within any asset class, higher credit rated reference obligations will exhibit less credit spread movement than lower credit rated reference obligations. Additionally, the degree of credit spread movement can vary significantly for different asset classes. The basis point change presented in the preceding table, however, represents a fixed basis point change in referenced obligation credit spreads across all credit quality rating categories and asset classes and, therefore, the actual impact of spread changes would vary from this presentation depending on the credit rating and distribution across asset classes, both of which will adjust over time depending on new business written and runoff of the existing portfolio.

MBIA Corp. uses collateral prices as an input into the Direct Price Model for certain multi-sector insured CDOs, a sensitivity analysis below shows the estimated pre-tax change in fair value and the cumulative estimated net fair value of MBIA Corp.'s insured credit derivatives portfolio of a 10% and 20% change in collateral prices as of September 30, 2013.

In millions	Change in Collateral Prices (Structured Finance and International Insurance)				
	20% Increase	10% Increase	No Change	10% Decrease	20% Decrease
Estimated pre-tax net gains (losses)	\$ 4	\$ 2	\$ -	\$ (2)	\$ (5)
Estimated net fair value	\$ (1,359)	\$ (1,361)	\$ (1,363)	\$ (1,365)	\$ (1,368)



**Table of Contents****Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)**

Sensitivity to changes in the collateral portfolio credit quality can be estimated by projecting a hypothetical change in rating migrations. The following table presents the estimated pre-tax change in fair value and the cumulative estimated net fair value of MBIA Corp.'s insured credit derivatives portfolio of a one and three notch rating change in the credit quality as of September 30, 2013. A notch represents a one step movement up or down in the credit rating.

In millions	Change in Credit Ratings (Structured Finance and International Insurance)				
	Three Notch Increase	One Notch Increase	No Change	One Notch Decrease	Three Notch Decrease
Estimated pre-tax net gains (losses)	\$ 612	\$ 188	\$ -	\$ (192)	\$ (877)
Estimated net fair value	\$ (751)	\$ (1,175)	\$ (1,363)	\$ (1,555)	\$ (2,240)

Recovery rates on defaulted collateral are an input into MBIA Corp.'s valuation model. Sensitivity to changes in the recovery rate assumptions used by MBIA Corp. can be estimated by projecting a hypothetical change in these assumptions. The following table presents the estimated pre-tax change in fair value and the cumulative estimated net fair value of MBIA Corp.'s insured credit derivatives portfolio of a 10% and 20% change in the recovery rate assumptions as of September 30, 2013.

In millions	Change in Recovery Rates (Structured Finance and International Insurance)				
	20% Increase	10% Increase	No Change	10% Decrease	20% Decrease
Estimated pre-tax net gains (losses)	\$ 142	\$ 67	\$ -	\$ (62)	\$ (120)
Estimated net fair value	\$ (1,221)	\$ (1,296)	\$ (1,363)	\$ (1,425)	\$ (1,483)

Accounting principles for fair value measurements require MBIA Corp. to incorporate its own nonperformance risk in its valuation methodology. Sensitivity to changes in MBIA Corp.'s credit spreads can be estimated by projecting a hypothetical change in this assumption. The following table presents the estimated pre-tax change in fair value and the cumulative estimated net fair value of MBIA Corp.'s insured credit derivative portfolio using upfront credit spreads of 0%, an increase of 7 percentage points, and an increase of 15 percentage points. The actual upfront spread used in the valuation as of September 30, 2013 ranged from 4.13% to 20.63% based on the tenor of each transaction. The below amounts include an additional annual running credit spread of 5%.

In millions	MBIA Corp.'s Upfront Credit Spread (Structured Finance and International Insurance)			
	Increase by 15 Percentage Points	Increase by 7 Percentage Points	No Change	Decrease to 0 Percentage Points
Estimated pre-tax net gains (losses)	\$ 277	\$ 129	\$ -	\$ (224)
Estimated net fair value	\$ (1,086)	\$ (1,234)	\$ (1,363)	\$ (1,587)

With the inclusion of MBIA Corp.'s recovery rate in the calculation of nonperformance risk for MBIA Corp.'s insured credit derivatives portfolio, the following sensitivity table presents the estimated pre-tax change in fair value of insured credit derivatives due to changes in that recovery rate. The values shown below reflect an approximate trading range of MBIA Corp.'s recovery rate.

**MBIA Corp. s Recovery Rate**  
**(Structured Finance and International Insurance)**

<b>In millions</b>	<b>Decrease to 30 Percentage Points</b>	<b>No Change</b>	<b>Increase to 60 Percentage Points</b>
Estimated pre-tax net gains (losses)	\$ 7	\$ -	\$ (10)
Estimated net fair value	\$ (1,356)	\$ (1,363)	\$ (1,373)

MBIA Corp. s insurance of structured credit derivatives typically remain in place until the maturity of the derivative. With respect to MBIA Corp. s insured structured credit derivatives, in the absence of credit impairments or the termination of derivatives at losses, the cumulative unrealized losses should reverse before or at maturity of the contracts. Additionally, in the event of the termination and settlement of a contract prior to maturity, any resulting gain or loss upon settlement will be recorded in our consolidated financial statements. In February 2008, the Company announced its intention not to insure credit derivatives in the future, except in transactions that are intended to reduce its overall exposure to insured derivatives.

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**Item 4. Controls and Procedures**

As of the end of the period covered by this report, an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15(d)-15(e) under the Securities Exchange Act of 1934) was performed under the supervision and with the participation of the Company's senior management, including the Chief Executive Officer and the Chief Financial Officer. Based on that evaluation, the Company's management, including the Chief Executive Officer and the Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report. In addition, there have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) during the fiscal quarter to which this report relates that have materially affected, or are likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents****PART II OTHER INFORMATION****Item 1. Legal Proceedings**

For a discussion of the Company's litigation and related matters, see Note 14: Commitments and Contingencies in the Notes to Consolidated Financial Statements of MBIA Inc. and Subsidiaries in Part I, Item 1. In the normal course of operating its businesses, MBIA Inc. may be involved in various legal proceedings. As a courtesy, the Company posts on its website under the section Legal Proceedings, selected information and documents in reference to selected legal proceedings in which the Company is the plaintiff or the defendant. The Company will not necessarily post all documents for each proceeding and undertakes no obligation to revise or update them to reflect changes in events or expectations. The complete official court docket can be publicly accessed by contacting the clerk's office of the respective court where each litigation is pending.

**Item 1A. Risk Factors**

References in the risk factors to the Company are to MBIA Inc., together with its domestic and international subsidiaries. References to we, our and us are to MBIA Inc. or the Company, as the context requires. Our risk factors are grouped into categories and are presented in the following order: Insured Portfolio Loss Related Risk Factors, Capital, Liquidity and Market Related Risk Factors, Strategic Plan Related Risk Factors and General Risk Factors. Risk factors are listed in order of significance within each category. These risk factors and their order of significance supersede the risk factors discussed under Risk Factors in Part I, Item 1A of MBIA Inc.'s Annual Report on Form 10-K for the year ended December 31, 2012.

**Insured Portfolio Loss Related Risk Factors**

*Deteriorating performance of CMBS and CRE loans in our structured finance insured portfolio due to adverse developments in the CRE segment of the credit markets may materially and adversely affect our financial condition, results of operations and future business.*

MBIA Corp. has insured a substantial amount of credit default swaps (CDS) contracts that are backed by structured commercial mortgage-backed securities (CMBS) pools and commercial real estate (CRE) collateralized debt obligations (CDOs). Through September 30, 2013 we have recorded impairments and loss adjustment expense (LAE) of \$4.1 billion (including \$487 million of impairments and LAE in the first nine months of 2013) related to CMBS and CRE exposure. MBIA Corp. has experienced ratings erosion in the total CMBS collateral underlying our insured static pools. Whereas approximately 16% of the total CMBS collateral underlying the pools outstanding as of September 30, 2013 was originally rated BBB and below and approximately 49% was originally rated AAA, approximately 68% of the total CMBS collateral underlying these pools as of September 30, 2013 was rated below investment grade.

Currently, we insure four static CMBS pools that were originally insured in 2006 and 2007, and in which substantially all of the underlying collateral comprised CMBS tranches originally rated BBB and lower. Total gross par outstanding on these pools was \$800 million as of September 30, 2013. Additionally, we insure two static CMBS pools, totaling \$3.0 billion of gross par outstanding as of September 30, 2013, that were originally insured in 2007, and are comprised of CMBS collateral which was originally rated A. If the economy does not continue to improve, it is possible that we will experience severe losses on these transactions, particularly if the underlying loans are unable to pay off at their expected maturity dates. Although we believe MBIA Corp. will have adequate resources to pay expected claims, there can be no assurance that this will be the case.

Ultimate loss rates remain uncertain, and we have recorded additional impairments on our insured CMBS portfolio every quarter since the beginning of 2010 as actual deterioration has been more than expected during that time period. It is possible that we will experience severe losses or near-term liquidity needs due to increased deterioration in our insured CMBS portfolio or our failure to commute the policies, primarily on the four static CMBS pools in which substantially all of the underlying collateral comprised CMBS tranches originally rated BBB and lower, in particular if the economy does not continue to improve, there is a new recession, increased delinquencies, higher levels of liquidations of delinquent loans, or higher severities of loss upon liquidation. Furthermore, MBIA Corp.'s guarantees of structured CMBS pools generally are in the form of CDS referencing the CMBS bonds in static pooled transactions, and the same CMBS bonds may be referenced in multiple pools. Accordingly, a collateral failure on a small number of CMBS bonds may require MBIA Corp. to make payments on several insured CDS transactions. In the event MBIA Corp. fails to make these payments, MBIA Corp.'s CDS contract obligations could be accelerated, which could materially and adversely affect our financial condition and results of operations.

**Table of Contents****Item 1A. Risk Factors (continued)**

***Continued poor performance of ineligible loans in the transactions that we insured in the residential mortgage sector and any delay or failure in collecting expected recoveries may materially and adversely affect our financial condition, results of operations and future business.***

As of September 30, 2013, we recorded expected receipts of \$756 million (on a present value basis) from excess spread (the difference between interest inflows on assets and interest outflows on liabilities) in our second-lien residential mortgage-backed securities ( RMBS ) transactions, in reimbursement of our past and future expected claims. Of this amount, \$669 million is included in Insurance loss recoverable and \$87 million is included in Loss and loss adjustment expense reserves on the Company's consolidated balance sheets. The amount of excess spread depends on future interest rates, borrower refinancing and defaults. There can be no assurance that the \$756 million will be received in its entirety or in the expected timeframe.

In addition, we continue to be exposed to risk of losses as a result of poor performance of ineligible loans included in our insured second-lien RMBS transactions, including transactions where we have reached settlements with the sellers/servicers but continue to insure the transaction. Furthermore, Credit Suisse continues to breach its obligations under the relevant contracts to repurchase, replace or cure ineligible mortgage loans. We believe that the inclusion of these ineligible mortgage loans has substantially contributed to the RMBS losses that the Company has incurred to date. Since the fourth quarter of 2007, MBIA Corp. has paid \$6.9 billion of claims before reinsurance and collections, excluding LAE and including \$1.0 billion of claims made on behalf of consolidated variable interest entities ( VIEs ), on policies insuring second-lien RMBS securitizations. Losses in these transactions and in other transactions due to the inclusion of ineligible loans could continue. In sizing loss reserves relating to these transactions, we take into account expected recoveries from those sellers/servicers arising from our contractual rights of put-back of ineligible loans. As of September 30, 2013, we recorded estimated recoveries of \$1.1 billion related to insured transactions. The recovery amount is based upon a number of factors, including an assessment of the financial abilities of the sellers/servicers using external credit ratings. The impact of such factors on cash flows related to expected recoveries is incorporated into the Company's probability-weighted scenarios.

Finally, although we sought to underwrite RMBS and other structured finance transactions with levels of subordination and other credit enhancements designed to protect us from loss in the event of poor performance of the underlying assets collateralizing the securities, the misrepresentations concerning the quality of the collateral backing those transactions has rendered insufficient the original level of subordination and other credit enhancements to prevent losses. No assurance can be given that any remaining credit enhancements will prove to be adequate to protect us from incurring additional material losses.

***There can be no assurance that we will be successful, or that we will not be delayed, in realizing our remaining estimated loan put-back recoveries of \$1.1 billion, or \$737 million net of reinsurance and income taxes, which is 23% of the consolidated total shareholders' equity of MBIA Inc., excluding preferred stock of subsidiary and noncontrolling interest.***

As of September 30, 2013, we have recognized remaining estimated loan put-back recoveries of \$1.1 billion related to our insured transactions. As of September 30, 2013, the estimated loan put-back recoveries net of reinsurance and income taxes are \$737 million, which is 23% of the consolidated total shareholders' equity of MBIA Inc., excluding preferred stock of subsidiary and noncontrolling interest. If we fail to ultimately realize the expected recoveries, our current loss reserve estimates may not be adequate for MBIA Corp. to cover potential claims, and MBIA Corp. may have insufficient resources to meet its obligations.

To date, the Company has resolved substantially all of its claims related to ineligible loans with the exception to those loans securitized by Credit Suisse and included in the home equity mortgage trust securitization. The Company's assessment of the ineligibility of individual mortgage loans has been challenged by Credit Suisse in litigation and there is no assurance that the Company's determinations will prevail, or that the Company will be successful in collecting its estimated recoveries. Estimated recoveries may differ from realized recoveries due to the uncertainty of litigation, the cost of litigation, error in determining breach rates, counterparty credit risk, the potential for delay and other sources of uncertainty. In addition, the litigation may take several years to resolve, during which time we will be required to pay losses on the subject transaction.

**Table of Contents****Item 1A. Risk Factors (continued)**

We have also recorded substantial recoveries related to put-backs against two wholly-owned subsidiaries of Residential Capital, LLC ( ResCap ), GMAC Mortgage, LLC ( GMAC ) and Residential Funding Company, LLC ( RFC ), whose ultimate parent company is Ally Financial Inc. ( Ally ). On May 14, 2012, ResCap, RFC and GMAC each filed for bankruptcy protection under Chapter 11 of the United States Bankruptcy Code. As of May 23, 2013, Ally, ResCap, RFC, GMAC and the Consenting Claimants (which includes the Company), among other parties, executed a term sheet and supplemental term sheet agreeing to, among other things, a settlement amount of \$796 million to be paid to the Company as part of a proposed plan to resolve claims against Ally and RFC, GMAC and ResCap. In August 2013, a disclosure statement filed indicated an increased expected recovery for the Company of approximately \$828 million. The increased recovery was primarily due to the favorable disposition of assets and settlements of claims. The settlement and anticipated recoveries are consistent with the put-back recoveries recorded by the Company. In June of 2013, the bankruptcy court issued a Memorandum Opinion approving the Plan Support Agreement (the Plan ). The Plan is subject to confirmation by the bankruptcy court, with confirmation hearings currently scheduled in November 2013. MBIA anticipates an initial distribution of funds to the Company and other claimants in late 2013 or early 2014. This anticipated timeline may change in the course of events in the bankruptcy court plan confirmation process. Furthermore, there can be no assurance that the Plan will ultimately be confirmed in its current form, or that MBIA will receive its expected recoveries.

***Continued poor performance of RMBS and ABS CDOs in our structured finance insured portfolio due to adverse developments in the residential mortgage sector and the broader economy may materially and adversely affect our financial condition, results of operations and future business.***

The Company is exposed to credit risks in our portfolio that have arisen from the deterioration and continued poor performance of certain segments of the credit markets, particularly our RMBS and CDOs of asset-backed securities ( ABS ) portfolios, which has led to the deterioration in the quality of assets and the collection of cash flows from such assets within structured securities that we have guaranteed. Beginning in the second half of 2007, deterioration of the global credit markets coupled with the re-pricing of credit risk created extremely difficult market conditions and volatility in the credit markets. The concerns on the part of market participants were initially focused on the subprime segment of the United States ( U.S. ) mortgage-backed securities market and expanded to include a broad range of mortgage and asset-backed and other fixed-income securities, including those rated investment grade, the U.S. and international credit and interbank money markets generally, and a wide range of financial institutions and markets, asset classes and sectors. The deterioration in the credit markets was accompanied by a severe economic recession precipitated, in part, by the collapse of U.S. residential home prices. The U.S. economy continues to show sluggish growth in the employment, housing and financial sectors. While many segments of the global credit markets and the economy have since recovered, the performance of certain credits we insure, in particular RMBS and CDOs of ABS have deteriorated significantly since 2007 and those credits continue to perform poorly.

In the first nine months of 2013, we recorded \$312 million of losses and LAE related to insured second-lien RMBS exposures in our structured finance portfolio before the \$448 million benefit related to an increase in recoveries of ineligible mortgage loans and before the elimination of a \$44 million benefit as a result of consolidating VIEs. Furthermore, since the fourth quarter of 2007, we have recorded losses and LAE of \$2.0 billion, before the elimination of a \$73 million benefit as a result of consolidating VIEs, (including a benefit of \$136 million in the first nine months of 2013 before the elimination of a \$44 million benefit as a result of consolidating VIEs) related to insured second-lien RMBS exposures. We have made \$6.9 billion of claims payments before reinsurance and collections, excluding LAE and including \$1.0 billion of claims on behalf of consolidated VIEs. In addition, to date, we have recorded losses and LAE of \$380 million, before the elimination of a \$52 million expense as a result of consolidating VIEs (including a \$86 million benefit in the first nine months of 2013 before the elimination of a \$39 million benefit as a result of consolidating VIEs), on the financial guarantee CDOs of ABS and could continue to experience poor performance in some of the structured finance securities we insure and losses on these portions of our insured portfolio.

***Our ability to implement our risk reduction and liquidity strategies is dependent on our ability to draw on our credit facility, collect expected put-back recoveries, and obtain regulatory approvals.***

In recent years key components of our strategy have included commuting volatile insured exposures, purchasing instruments issued or guaranteed by us in order to reduce future expected economic losses and managing the liquidity requirements and risk in our insured portfolios and asset/liability products segment. In order to implement this strategy, we put in place intercompany agreements that allocate liquidity resources among our entities in order to fund commutations and provide liquidity where needed. The intercompany agreements with our insurance subsidiaries have required the approval of the New York State Department of Financial Services ( NYSDFS ) and are described further under Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity Key Lending Agreements in Part I, Item 2 of this Form 10-Q.



**Table of Contents****Item 1A. Risk Factors (continued)**

In addition, during the second quarter of 2013, MBIA Insurance Corporation entered into a \$500 million three-year secured revolving credit agreement with Blue Ridge Investments, L.L.C., an affiliate of Bank of America (the Blue Ridge Secured Loan), which is required to be prepaid with, among other things, proceeds from any put-back recoveries. MBIA Corp. expects to rely on available borrowings under the Blue Ridge Secured Loan and put-back recoveries to fund commutations and other expenses. If MBIA Corp.'s access to the Blue Ridge Secured Loan or other financing were unavailable, reduced or were to become significantly more expensive for any reason, including, without limitation, due to its inability to meet any condition in the facility, it may not have sufficient liquidity to commute volatile exposures or to meet its obligations generally. In addition, if it is unable to collect expected put-back recoveries prior to the termination of the facility and is not able to refinance the facility, it may not be able to repay its borrowings.

Our counterparties may also request as a condition to commuting their policies with us that the transaction receive approval from the NYSDFS or the United Kingdom Prudential Regulation Authority. There can be no assurance that we will be able to obtain such approvals. In the event that we do not obtain such regulatory approvals, we do not expect to be able to effect additional commutations of volatile exposures.

Finally, if we do not obtain approvals to draw on intercompany financing, MBIA Inc. may not have sufficient assets to meet its collateral posting requirements and other liquidity needs, as described further under Adverse developments in the credit markets may materially and adversely affect MBIA Inc.'s ability to meet liquidity needs. Furthermore, in connection with obtaining required insurance regulatory approvals to enter into certain transactions, MBIA Inc. and its insurance subsidiaries have agreed, and may in the future agree, to comply with certain conditions, including providing notice to the NYSDFS prior to entering into transactions or taking other corporate actions (such as paying dividends when applicable statutory tests are satisfied), that would not otherwise require regulatory approval.

***Loss reserve estimates and credit impairments are subject to additional uncertainties and loss reserves may not be adequate to cover potential claims.***

The financial guarantees issued by our insurance companies insure the financial performance of the obligations guaranteed over an extended period of time, in some cases over 30 years, under policies that we have, in most circumstances, no right to cancel. We do not use traditional actuarial approaches to determine our loss reserves. The establishment of the appropriate level of loss reserves is an inherently uncertain process involving numerous estimates and subjective judgments by management, and therefore, there can be no assurance that actual paid claims in our insured portfolio will not exceed its loss reserves. Additionally, we use both internal models as well as models generated by third-party consultants and customized by us to project future paid claims on our insured portfolio and establish loss reserves. Since our insured credit derivatives have similar terms, conditions, risks, and economic profiles to our financial guarantee insurance policies, we evaluate them for impairment periodically in the same way that we estimate loss and LAE for our financial guarantee policies. There can be no assurance that the future loss projections based on these models are accurate.

Small changes in the assumptions underlying loss reserve estimates could significantly impact loss expectations. For example, our loss reserves are discounted to a net present value reflecting MBIA's general obligation to pay claims over time and not on an accelerated basis. Risk-free rates are used to discount our loss reserves under GAAP, and the yield-to-maturity of each insurer's investment portfolio as of year-end is used to discount each insurer's loss reserves under U.S. STAT. Accordingly, changes in the risk-free rates or the yield in our insurers' investment portfolios may materially impact loss reserves. Losses on second-lien RMBS caused by the large number of ineligible mortgage loans included in second-lien RMBS securitizations that we insured as well as unprecedented volatility in the credit markets that began in the fourth quarter of 2007 have caused us to increase our loss projections substantially several times especially for second-lien RMBS transactions, where expected losses are significantly greater than originally projected and in many cases exceed the worst historical losses in this category. As a result, historical loss data may have limited value in predicting future second-lien RMBS losses. Moreover, in sizing loss reserves with respect to our insured transactions, we take into account expected recoveries from sellers/servicers of the transactions arising from our contractual rights of put-back of ineligible loans, and these estimated recoveries may differ from realized recoveries due to the outcome of litigation, the cost of litigation, error in determining breach rates, counterparty credit risk, the potential for delay and other sources of uncertainty. Our balance sheet also reflects estimated recoveries in reimbursement of past and future expected claims through excess spread in insured second-lien RMBS transactions. Excess spread is primarily included on our GAAP consolidated balance sheet in Insurance loss recoverable. Excess spread is included on MBIA Corp.'s U.S. STAT balance sheets in Losses. Excess spread is generated by performing loans within insured RMBS securitizations and is the difference between interest inflows on mortgage loan collateral and interest outflows on insured beneficial interests. The amount of excess spread depends on the future delinquency and loss trends, future prime and LIBOR interest rates and borrower refinancing behavior, which results in voluntary prepayments. There can be no assurance that we will collect excess spread recoveries in the amounts we have recorded.



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We recorded our first credit impairments related to CMBS and CRE exposure in 2010, and have increased our credit impairments on these exposures during each subsequent quarter as a result of the deterioration of our CMBS and CRE portfolio and the increased cost of commuting our exposures. While our credit impairments reflect our current estimate of ultimate losses, if the deterioration of the CRE market worsens, we could incur substantial additional losses on our CMBS and CRE portfolio in excess of these estimates.

Future deterioration in the performance of RMBS, CMBS, ABS CDOs or other obligations we insure or reinsure could lead to the establishment of additional loss reserves or impairments and further losses or reductions in income. There can be no assurance that the estimates of probable and estimable losses are accurate. Actual paid claims could exceed our estimate and could significantly exceed our loss reserves. If our loss reserves are not adequate to cover actual paid claims, our results of operations and financial condition could be materially adversely affected.

**Table of Contents****Item 1A. Risk Factors (continued)*****Economic conditions in the United States and the Eurozone may materially adversely affect our business and results of operations.***

Our results of operations are materially affected by general economic conditions, both in the U.S. and elsewhere around the world. While the U.S. economy has consistently grown since the fourth quarter of 2009 and many segments of the global capital markets have recovered from the financial crisis that began in the second half of 2007, markets have continued to experience periods of extreme volatility, and economic activity in Europe remains weak. While we do not insure any direct European sovereign debt, our indirect European sovereign debt exposure totaled \$8.0 billion as of September 30, 2013 and included obligations of sovereign-related and sub-sovereign issuers, such as regions, departments, and sovereign-owned entities that are supported by a sovereign state, region or department. Of the \$8.0 billion of insured gross par outstanding, \$817 million, \$491 million, and \$258 million related to Spain, Portugal, and Ireland, respectively. The remaining \$6.4 billion related to the United Kingdom. A default by one or more sovereigns, or sovereign-related or sub-sovereign entities that rely on sovereign support, could have an adverse effect on our insured and investment portfolios. Moreover, budget deficits at all levels of government in the U.S., continued concerns over the availability and cost of credit for certain borrowers, austerity measures imposed by certain European governments and slowdowns in certain international economies have contributed to diminished expectations for certain parts of the global economy and certain markets going forward.

Losses resulting from poor economic conditions and the related weak performance of RMBS (including due to the inclusion of ineligible loans in second-lien RMBS we insured), ABS CDOs and CMBS, have adversely impacted, and continue to impact our results and financial condition. In addition, recessions, increases in corporate, municipal, sovereign, sub-sovereign or consumer default rates and other general economic conditions may adversely impact the Company's prospects for future business, as well as the performance of our insured portfolios and the Company's investment portfolio. In addition, public finance obligations supported by specified revenue streams, such as revenue bonds issued by toll road authorities, municipal utilities or airport authorities, may be adversely affected by revenue declines resulting from economic recession, reduced demand, changing demographics or other factors.

***Termination payments on insured credit derivatives could present a material liquidity risk.***

The structured finance and international segment's financial guarantee contracts and CDS contracts generally cannot be accelerated, thereby mitigating liquidity risk. However, with respect to the insurance of CDS contracts, in certain circumstances, including the occurrence of certain insolvency or payment defaults under the CDS contracts, the CDS contracts may be subject to termination by the counterparty, triggering a claim for the fair value of the contract. In addition, credit derivative transactions are governed by International Swaps and Derivatives Association (ISDA) documentation and operate differently from financial guarantee insurance policies. For example, the Company's control rights with respect to a reference obligation under a credit derivative may be more limited than when it issues a financial guarantee insurance policy on a direct primary basis. In addition, a credit derivative may be terminated for a breach of the ISDA documentation or other specific events, unlike financial guarantee insurance policies. If a credit derivative is terminated, the Company could be required to make a mark-to-market payment as determined under the ISDA documentation.

***Servicer risk could adversely impact performance of structured finance transactions.***

Structured finance obligations contain certain risks including servicer risk, which relates to problems with the transaction servicer (the entity which is responsible for collecting the cash flow from the asset pool) that could affect the servicing and performance of the underlying assets. Structural risks primarily involve bankruptcy risks, such as whether the servicer of the assets may be required to delay the remittance of any cash collections held by it or received by it after the time it becomes subject to bankruptcy or insolvency proceedings. Structured finance transactions are usually structured to reduce the risk to the investors from the bankruptcy or insolvency of the servicer. The ability of the servicer to properly service and collect on the underlying assets can contribute to the performance of a transaction. In addition, the lawsuit we have filed against Credit Suisse alleges that the servicer has failed to perform its duties as contractually required.

***Some of the state and local governments and finance authorities that issue public finance obligations we insure are experiencing unprecedented fiscal stress that could result in increased credit losses or impairments on those obligations.***

We have historically experienced low levels of defaults in our U.S. public finance insured portfolio, including during the financial crisis that began in mid-2007. However, many state and local governments that issue some of the obligations we insure have reported unprecedented fiscal stress that has required them to significantly raise taxes and/or cut spending in order to satisfy their obligations. While there has been some support provided by the U.S. federal government designed to provide aid to state and local governments, certain state and local governments remain under extreme financial stress. In particular, certain jurisdictions have significant unfunded pension liabilities which are placing additional stress on their finances and are particularly challenging to restructure either through negotiation or under Chapter 9 of the United

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States Bankruptcy Code. If the issuers of the obligations in our public finance portfolio are unable to raise taxes, cut spending, or receive federal assistance, we may experience losses or impairments on those obligations, which could materially and adversely affect our business, financial condition and results of operations. In particular, an increasing number of municipalities are experiencing severe financial stress and, as a consequence, more municipal issuers are considering filing for protection under Chapter 9. The outcome of a Chapter 9 proceeding is unpredictable and could result in impairments on a greater number of general obligation bonds and other insured transactions. For example, the City of Detroit has proposed treating certain National insured general obligation bonds as unsecured debt with no right to specific voter-approved revenues, which could result in significant impairments on those bonds if the city's proposal succeeds. While National intends to vigorously challenge this treatment, there can be no assurance that it will ultimately be successful. Refer to Note 14: Commitments and Contingencies in the Notes to Consolidated Financial Statements for a description of this litigation.

**Table of Contents****Item 1A. Risk Factors (continued)**

*Financial modeling contains uncertainty over ultimate outcomes, which makes it difficult to estimate liquidity, potential paid claims, loss reserves and mark-to-market.*

The Company uses third-party and internal financial models to estimate liquidity, potential paid claims, loss reserves and mark-to-market. We use internal financial models to conduct liquidity stress-scenario testing to ensure that we maintain cash and liquid securities in an amount in excess of all stress scenario payment requirements. These measurements are performed on a legal entity and operating segment basis. We also rely on financial models, generated internally and supplemented by models generated by third parties, to estimate factors relating to the highly complex securities we insure, including future credit performance of the underlying assets, and to evaluate structures, rights and our potential obligations over time. We also use internal models for ongoing portfolio monitoring and to estimate case basis loss reserves and, where applicable, to mark our obligations under our contracts to market and may supplement such models with third-party models or use third-party experts to consult with our internal modeling specialists. Both internal and external models are subject to model risk and there can be no assurance that these models are accurate or comprehensive in estimating our liquidity, potential future paid claims and related loss reserves or that they are similar to methodologies employed by our competitors, counterparties or other market participants. Estimates of our future paid claims, in particular, may materially impact our liquidity position. In addition, changes to our paid claims, loss reserve or mark-to-market models have been made recently and may be warranted in the future. These changes could materially impact our financial results.

*Our risk management policies and procedures may not detect or prevent future losses.*

We assess our risk management policies and procedures on a periodic basis. As a result of such assessment, we may take steps to change our internal risk assessment capabilities and procedures, our portfolio management policies, systems and processes and our policies and procedures for monitoring and assessing the performance of our insured portfolio in changing market conditions. There can be no assurance, however, that these steps will be adequate to avoid future losses. In some cases, losses can be substantial, particularly if a loss occurs on a transaction in which we have a large notional exposure or on a transaction structured with large, bullet-type principal maturities.

*Geopolitical conditions may adversely affect our business prospects and insured portfolio.*

General global unrest, fraud, terrorism, catastrophic events, natural disasters, pandemics or similar events could disrupt the economy in the U.S. and the other countries where we have insured exposure or operate our businesses and could have a direct material adverse impact on certain industries and on general economic activity. Furthermore, in certain jurisdictions outside the U.S. we face higher risks of governmental intervention through nationalization or expropriation of assets, an inability to enforce our rights in court or otherwise and corruption, which may cause us to incur losses on the assets we insure or reputational harm. The Company has exposure in certain sectors that could suffer increased delinquencies and defaults as a direct result of these types of events. Moreover, we are exposed to correlation risk as a result of the possibility that multiple credits will experience losses as a result of any such event or series of events, in particular exposures that are backed by revenues from business and personal travel, such as aircraft securitizations and bonds backed by hotel taxes and car rental fleet securitizations. To the extent that certain corporate sectors may be vulnerable to credit deterioration and increased defaults in the event of future global unrest, CDOs backed by pools of corporate debt issuances in those stressed sectors could also be adversely impacted.

The Company's insurance operations underwrite exposures to the Company's reasonable expectation of future performance as well as at various stress levels estimating defaults and other conditions at levels higher than are reasonably expected to occur. There can be no assurance, however, that the Company will not incur material losses if the economic stress and increased defaults in certain sectors caused by global unrest, fraud, terrorism, catastrophic events, natural disasters, pandemics or similar events in the future is or will be more severe than the Company currently foresees and had assumed in underwriting its exposures and estimating loss reserves.

**Capital, Liquidity and Market Related Risk Factors**

*Continuing elevated loss payments and ongoing delays in our ability to realize expected recoveries on insured RMBS transactions as well as certain other factors may materially and adversely affect MBIA Corp.'s ability to meet liquidity needs, which could in turn have an adverse impact on the Company.*

As an insurance company MBIA Corp. is particularly sensitive to liquidity risk, which is the probability that an enterprise will not have sufficient resources to meet contractual payment obligations when due. Management of liquidity risk is of critical importance to financial services companies, and most failures of financial institutions have occurred in large part due to their inability to maintain sufficient liquidity resources under adverse circumstances. Generally, lack of sufficient resources results from an enterprise's inability to sell assets at values

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necessary to satisfy payment obligations, the inability to access new capital and/or an unexpected acceleration of payments required to settle liabilities.

**Table of Contents****Item 1A. Risk Factors (continued)**

The effects of the credit crisis which began in the subprime segment of the U.S. mortgage-backed securities market and spread to a wide range of financial institutions and markets, asset classes, sectors and countries, have caused the Company to experience material increased liquidity risk pressures. In particular, since the fourth quarter of 2007, MBIA Corp. has paid \$6.9 billion of claims before reinsurance and collections, excluding LAE and including \$1.0 billion of claims made on behalf of consolidated VIEs, on policies insuring second-lien RMBS securitizations, which we believe were driven by a substantial number of ineligible mortgage loans being placed in the securitizations in breach of the representations and warranties of the sellers/servicers. Furthermore, since the fourth quarter of 2007, total credit impairments on insured derivatives were estimated at \$6.1 billion across 74 CDO insured issues, inclusive of 71 insured issues for which we made settlement and claim payments of \$5.8 billion, net of reinsurance and collections. Accordingly, we expect to realize additional net losses of \$337 million. If current trends worsen and result in substantial defaults and losses on the underlying loans, we could incur substantial additional losses on our insured exposures in the future. In addition, portions of MBIA Corp.'s outstanding insured portfolio have exhibited high degrees of payment volatility and continue to pose material liquidity risk to MBIA Corp.

Management's expected liquidity and capital forecasts for MBIA Corp. for 2013 reflect adequate resources to pay expected claims. In addition, MBIA Corp. can borrow under the Blue Ridge Secured Loan and use its expected recoveries from the ResCap agreement to pay claims. However, there is risk to the liquidity forecast as the Company's second-lien RMBS and remaining insured CMBS pools are potentially volatile. There are risks to the capital forecast due to those potential liabilities, potential volatility in the collection of put-back recoverables and potential volatility associated with remaining ABS CDO exposures. Further, the remaining insured portfolio, aside from these exposures, could deteriorate and result in loss reserves and claim payments. While management believes MBIA Corp. will have adequate resources to pay expected claims, if it experiences higher than expected claims payments or is unable to commute exposures that represent substantial risk to the Company, it may ultimately have insufficient resources to continue paying claims, which could cause the NYSDFS to put MBIA Insurance Corporation into a rehabilitation or liquidation proceeding. An MBIA Insurance Corporation proceeding could accelerate certain of the Company's other obligations and have other adverse consequences.

*Adverse developments in the credit markets may materially and adversely affect MBIA Inc.'s ability to meet liquidity needs.*

MBIA Inc. is subject to material liquidity risks and uncertainty. To mitigate these risks, we seek to maintain cash and liquidity resources that we believe will be sufficient to make all payments due on our obligations and to meet other financial requirements, such as posting collateral, at least through the next twelve months.

Liquidity risk to MBIA Inc. is primarily a result of the following factors:

Currently, the majority of the cash and securities of MBIA Inc. is pledged against investment agreement liabilities, intercompany financing arrangements and derivatives, which limit its ability to raise liquidity through asset sales. A significant portion of MBIA Inc.'s assets that are pledged against intercompany financing arrangement liabilities are structured finance securities which have been particularly susceptible to price fluctuations during periods of market volatility. In addition, if the market value or rating eligibility of the assets which are pledged against MBIA Inc.'s obligations were to decline, we would be required to pledge additional eligible assets in order to meet minimum required collateral amounts against these liabilities. In such event, we may sell additional assets, potentially with substantial losses, finance unencumbered assets through intercompany facilities, or use free cash or other assets, in some cases with NYSDFS approval, although there can be no assurance that these strategies will be available or adequate to meet liquidity requirements.

The timing and amount of cash inflows from dividends paid by MBIA's principal operating subsidiaries is uncertain. See Our holding company structure and certain regulatory and other constraints could affect our ability to pay dividends and make other payments below.

Stressed credit market conditions could cause MBIA Inc. to have insufficient resources to cover collateral and/or other liquidity requirements. Management has identified certain actions to mitigate this risk. These contingent actions include: (1) accessing the capital markets, which may not be open to us on favorable terms, or at all; (2) additional sales of invested assets exposed to credit spread stress risk, which may occur at losses and increase the deficit of invested assets to liabilities; (3) termination and settlement of interest rate swap agreements; and (4) other available advances from subsidiaries. These actions, if taken, are expected to result in either additional liquidity or reduced exposure to adverse credit spread movements. There can be no assurance that these actions will be sufficient to fully mitigate this risk. In the event that we cannot

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implement the contingent actions identified above to raise liquidity, or eliminate the deficit, we may have insufficient assets to make all payments on our obligations as they come due, which could result in a default by MBIA Inc. on its obligations and the potential for MBIA Corp., as guarantor of the investment agreements and MBIA Global Funding, LLC medium-term notes ( MTNs ), to be called upon to satisfy obligations on those instruments as they come due.

**Table of Contents****Item 1A. Risk Factors (continued)*****An inability to access capital could adversely affect our business, operating results and financial condition and ultimately adversely affect liquidity.***

The Company's access to external sources of financing, as well as the cost of such financing, is dependent on various factors, including (i) the long-term debt ratings of the Company, (ii) the insurance financial strength ratings and long-term business prospects of our insurance companies, (iii) the perceptions of the financial strength of our insurance companies and MBIA Inc. and (iv) the outcome of our undertakings to collect recoveries in connection with ineligible mortgage loans in our insured RMBS securitizations. Our debt ratings are influenced by numerous factors, either in absolute terms or relative to our peer group, such as financial leverage, balance sheet strength, capital structure and earnings trends. If we cannot obtain adequate capital on favorable terms or at all, our business, future growth, operating results and financial condition could be adversely affected. While MBIA Corp. currently maintains a credit facility, there can be no assurance that replacement facilities will be available in the future on favorable terms or at all. Refer to [Our ability to implement our risk reduction and liquidity strategies](#) is dependent on our ability to draw on our credit facility, collect expected put-back recoveries, and obtain regulatory approvals [above](#). The inability to obtain adequate replacement capital on favorable terms or at all could have an adverse impact on the Company's business and financial condition.

To the extent that we are unable to access capital, our insurance companies may not have sufficient liquidity to meet their obligations, will have less capacity to write business and may not be able to pay dividends to us without experiencing adverse rating agency action. Accordingly, our inability to maintain access to capital on favorable terms could have an adverse impact on our ability to pay losses and debt obligations, to pay dividends on our capital stock, to pay principal and interest on our indebtedness, to pay our operating expenses and to make capital investments in our subsidiaries. See [Our holding company structure and certain regulatory and other constraints could affect our ability to pay dividends and make other payments](#) [below](#).

***Our holding company structure and certain regulatory and other constraints could affect our ability to pay dividends and make other payments.***

We are a holding company and rely to a significant degree on the operations of our principal operating subsidiaries, National, MBIA Corp. and Cutwater, and certain other smaller subsidiaries. As such, we are largely dependent on dividends or advances in the form of intercompany loans from our insurance companies to pay dividends, to the extent payable, on our capital stock, to pay principal and interest on our indebtedness and to make capital investments in our subsidiaries, among other items. Our insurance companies are subject to various statutory and regulatory restrictions, applicable to insurance companies generally, that limit the amount of cash dividends, loans and advances that those subsidiaries may pay to us. Other regulations relating to capital requirements affecting some of our other subsidiaries may also restrict their ability to pay dividends and other distributions and make loans to us.

Under New York law, National and MBIA Corp. may generally pay stockholder dividends only out of statutory earned surplus and subject to additional limits, as described in [Business Insurance Regulation](#) in Part I, Item 1 and [Note 14: Insurance Regulations and Dividends](#) in the Notes to Consolidated Financial Statements of MBIA Inc. and Subsidiaries in Part II, Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2012. In connection with MBIA Insurance Corporation obtaining approval from the NYSDFS to release excessive contingency reserves as of September 30, 2011, December 31, 2011 and March 31, 2012, MBIA Insurance Corporation agreed that it would not pay any dividends without prior approval from the NYSDFS. Due to its significant negative earned surplus, MBIA Insurance Corporation has not had the statutory capacity to pay dividends since December 31, 2009 and is not expected to have any statutory capacity to pay any dividends in the near term. In addition, as a condition to the NYSDFS' approval of the asset swap between MBIA Inc. and National, the NYSDFS requested that, until the notional amount of the Asset Swap has been reduced to 5% or less of National's admitted assets, each of MBIA Inc., MBIA Insurance Corporation and National provide the NYSDFS with three months prior notice, or such shorter period as the NYSDFS may permit, of its intent to initiate cash dividends on shares of its common stock. National has provided the NYSDFS with such notice.

Dividend payments by MBIA UK and MBIA Mexico to MBIA Insurance Corporation are also limited by laws and regulatory consideration in their respective jurisdictions. The inability of our insurance companies to pay dividends in an amount sufficient to enable us to meet our cash requirements at the holding company level could affect our ability to repay our debt and have a material adverse effect on our operations.



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### **Item 1A. Risk Factors (continued)**

***MBIA Inc. has long-term debt, MTNs, investment agreements and derivative liabilities in excess of its cash, investments at amortized cost and tax receivables.***

As of September 30, 2013 and December 31, 2012, the combined net debt of MBIA Inc.'s corporate segment and asset/liability products segment, which primarily comprised long-term debt, MTNs, investment agreements and derivative liabilities net of cash and investments at amortized cost and a tax receivable from subsidiaries, totaled \$1.3 billion and \$1.2 billion, respectively. The Company expects that MBIA Inc. will generate sufficient cash to satisfy its net debt over time from distributions from its operating subsidiaries and by raising third-party capital, although there can be no assurance that such factors will generate sufficient cash to satisfy its net debt.

***We have substantial indebtedness and may incur substantial additional indebtedness, which could adversely affect our financial health and our ability to obtain financing in the future, react to changes in our business and satisfy our obligations.***

As of September 30, 2013, we had \$1.7 billion of consolidated long-term debt, \$1.6 billion of consolidated medium-term note liabilities and \$760 million of consolidated investment agreement liabilities. Our substantial indebtedness and other liabilities could have material consequences, including:

our ability to obtain additional financing for working capital, capital expenditures, acquisitions, debt service requirements or general corporate purposes and our ability to satisfy our obligations with respect to our debt may be impaired in the future;

a large portion of MBIA Inc.'s financial resources must be dedicated to the payment of principal and interest on our debt, thereby reducing the funds available to us for other purposes;

it may be more difficult for us to satisfy our obligations to our creditors, resulting in possible defaults on, and acceleration of, such debt;

we may be more vulnerable to general adverse economic and industry conditions;

our ability to refinance debt may be limited or the associated costs may increase;

our flexibility to adjust to changing market conditions could be limited, or we may be prevented from carrying out capital spending that is necessary or important to our growth strategy and efforts to improve operating margins of our businesses; and

we are exposed to the risk of fluctuations in interest rates and foreign currency exchange rates because a portion of our liabilities are at variable rates of interest or denominated in foreign currencies.

***If our insurance companies fail to meet regulatory capital requirements they may become subject to regulatory action.***

Our insurance companies are subject to various statutory and regulatory restrictions that require them to maintain qualifying investments to support their reserves and minimum surplus. Furthermore, our insurance companies may be restricted from making commutation or other payments if doing so would cause them to fail to meet such requirements, and the NYSDFS may impose other remedial actions on us as described further below to the extent the Company does not meet such requirements. While National currently satisfies its statutory capital requirements, as of September 30, 2013, MBIA Corp. had a deficit of \$321 million of qualifying assets required to support its contingency reserves. The deficit was caused by MBIA Corp.'s sale of liquid assets in order to make claim payments and the failure of certain RMBS sellers/servicers to honor their contractual obligations to repurchase ineligible mortgage loans from securitizations the Company insured. The

deficit is expected to grow due to additional commutation and claim payments until such time as MBIA Corp. collects additional put-back recoveries. The Company has reported the deficit to the NYSDFS. MBIA Corp. previously requested approval from the NYSDFS to release an aggregate of \$321 million of contingency reserves, which was disapproved by the NYSDFS. Prior to September 30, 2012, MBIA Corp. released to surplus an aggregate of \$1.1 billion of contingency reserves pursuant to approvals granted by the NYSDFS in accordance with the New York Insurance Law during 2011 and 2012. Absent these releases MBIA Corp. would have had deficits of qualifying assets to meet its contingency reserve requirements.

Additionally, under New York law, the Superintendent of the NYSDFS may apply for an order directing the rehabilitation or liquidation of a domestic insurance company under certain circumstances, including upon the insolvency of the company, if the company has willfully violated its charter or New York law or if the company is found, after examination, to be in such condition that further transaction of business would be hazardous to its policyholders, creditors or the public. The Superintendent of the NYSDFS may also suspend an insurer's license, restrict its license authority, or limit the amount of premiums written in New York if, after a hearing, the Superintendent of the NYSDFS determines that the insurer's surplus to policyholders is not adequate in relation to its outstanding liabilities or financial needs. If the Superintendent of the NYSDFS were to take any such action with respect to National or MBIA Insurance Corporation, it would likely result in the reduction or elimination of the payment of dividends to MBIA Inc.

**Table of Contents****Item 1A. Risk Factors (continued)*****Changes in interest rates and foreign currency exchange rates could adversely affect our financial condition and future business.***

Increases in prevailing interest rate levels can adversely affect the value of MBIA's investment portfolio and, therefore, our financial condition. In the event that investments must be sold in order to make payments on insured exposures or other liabilities, including the liabilities of our asset/liability products segment, such investments would likely be sold at discounted prices. Lower interest rates can also result in lower net interest income since a substantial portion of assets are now held in cash and cash equivalents given the increased focus on liquidity. Additionally, in the insurance operations, increasing interest rates could lead to increased credit stress on transactions in our insured portfolio, while a decline in interest rates could result in larger loss reserves on a present value basis.

While we are not currently writing a meaningful amount of new financial guarantee insurance, we expect to do so in the future. Prevailing interest rate levels can affect demand for financial guarantee insurance. Lower interest rates are typically accompanied by narrower spreads between insured and uninsured obligations. The purchase of insurance during periods of relatively narrower interest rate spreads will generally provide lower cost savings to the issuer than during periods of relatively wider spreads. These lower cost savings could be accompanied by a corresponding decrease in demand for financial guarantee insurance. Increased interest rates may decrease attractiveness for issuers to enter into capital markets transactions, resulting in a corresponding decreasing demand for financial guarantee insurance in the future.

In addition, the Company is exposed to foreign currency exchange rate fluctuation risk in respect of assets and liabilities denominated in currencies other than U.S. dollars. In addition to insured liabilities denominated in foreign currencies, some of the remaining liabilities of our asset/liability management business are denominated in currencies other than U.S. dollars and the assets of our asset/liability management business are generally denominated in U.S. dollars. Accordingly, the weakening of the U.S. dollar versus foreign currencies could substantially increase our potential obligations and statutory capital exposure. Conversely, the Company regularly makes investments denominated in a foreign currency, in particular as part of a remediation strategy or as an economic hedge against potential future loss payments, and the weakening of the foreign currency versus the U.S. dollar will diminish the value of such non-U.S. dollar denominated asset. Exchange rates have fluctuated significantly in recent periods and may continue to do so in the future, which could adversely impact the Company's financial position, results of operations and cash flows.

***Revenues and liquidity would be adversely impacted by a decline in realization of installment premiums.***

Due to the installment nature of a significant percentage of its premium income, MBIA Corp. has an embedded future revenue stream. The amount of installment premiums actually realized by MBIA Corp. could be reduced in the future due to factors such as not insuring new transactions, early termination of insurance contracts, accelerated prepayments of underlying obligations, commutation of existing financial guarantee insurance policies or non-payment. Such a reduction would result in lower revenues and reduced liquidity.

***We are required to report credit derivatives at fair value, which subjects our results of operations to volatility and losses and could lead to negative shareholders' equity for the Company or MBIA Corp. on a GAAP basis.***

Any event causing credit spreads on an underlying security referenced in a credit derivative we insure, or on a credit derivative referencing an MBIA Inc. security, to either widen or tighten will affect the fair value of the credit derivative and may increase the volatility of our earnings.

Since changes in fair value can be caused by factors unrelated to the performance of our business and structured finance credit portfolio, including general market conditions and perceptions of credit risk, as well as market use of credit derivatives for hedging purposes unrelated to the specific referenced credits in addition to events that affect particular credit derivative exposure, the application of fair value accounting may cause our earnings to be more volatile than would be suggested by the underlying performance of our business operations and structured finance credit portfolio. Furthermore, volatility in our asset values, loss reserves, impairments or fair value of insured credit derivatives could cause our shareholders' equity, and/or that of MBIA Corp., to be negative under accounting principles generally accepted in the United States of America (GAAP) basis in a future period, which may adversely impact investors' perceptions of the value of the Company.

The global re-pricing of credit risk that began in the fourth quarter of 2007 caused unprecedented volatility and markdowns in the valuation of these credit derivatives. In addition, due to the complexity of fair value accounting and the application of the accounting guidance for derivative instruments and the accounting guidance for fair value measurement, future amendments or interpretations of derivative and fair value accounting may cause us to modify our accounting methodology in a manner which may have an adverse impact on our financial results. See

Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates in Part II, Item 7 of Form 10-K for the year ended December 31, 2012 for additional information on the valuation of derivatives.



**Table of Contents****Item 1A. Risk Factors (continued)**

Current accounting standards mandate that we measure the fair value of our insurance policies of CDS. Market prices are generally available for traded securities and market standard CDS but are less available or accurate for highly customized CDS. Most of the derivative contracts the Company insures are the latter as they are non-traded structured credit derivative transactions. Moreover, at the present time, we do not have access to the fair value estimates of the insurance beneficiaries and there can be no assurance that those counterparties' (or any other market participants') estimates would be the same as our fair values.

The mark-to-market for the insured credit derivative portfolio has fluctuated significantly during the last five years, resulting in volatility in MBIA's earnings. Since the fourth quarter of 2007, MBIA's mark-to-market on insured credit derivatives fluctuated from a high quarterly loss of \$3.6 billion in the first quarter of 2008 to a high quarterly gain of \$3.3 billion in the second quarter of 2008, and the mark-to-market caused several quarter over quarter fluctuations in earnings of more than \$1 billion and frequent quarter over quarter shifts in earnings from a gain to a loss or a loss to a gain. The mark-to-market volatility was primarily a result of fluctuations in MBIA's credit spreads and recovery rates, changes in credit spreads on the underlying collateral, collateral erosion, rating migration and model and input enhancements.

**Strategic Plan Related Risk Factors**

*An inability to achieve high stable insurer financial strength ratings for National or any of our other insurance companies from the major rating agencies or to generate investor demand for their financial guarantees may adversely affect our results of operations and business prospects.*

National's and our other insurance companies' ability to write new business and to compete with other financial guarantors is currently largely dependent on the financial strength ratings assigned to them by the major rating agencies and the financial enhancement rating also assigned by Standard & Poor's Financial Services LLC (S&P), as well as the financial strength of our insurance companies and investors' perceptions of their financial strength. Many requirements imposed by the rating agencies in order for our insurance companies to achieve and maintain high insurer financial strength ratings are outside of our control, and such requirements may necessitate that we raise additional capital or take other remedial actions in a relatively short time frame in order to achieve or maintain the ratings necessary to attract new business and compete with other financial guarantee insurers and could make the conduct of the business uneconomical. Our inability to raise capital on favorable terms could therefore materially adversely affect the business prospects of our insurance companies. Furthermore, no assurance can be given that we will successfully comply with rating agency requirements, that these requirements or the related models and methodologies will not change or that, even if we comply with these requirements, one or more rating agency will not lower or withdraw its financial strength ratings with respect to any of our insurance companies. The absence of higher ratings from S&P's and Moody's Investor Service, Inc. (Moody's), which have typically been required to write financial guarantee insurance, has adversely impacted the premiums our insurers can charge and could diminish the acceptance of our financial guarantee insurance products.

In addition, no assurance can be given that investor demand for our guarantees will increase regardless of our ratings. Finally, our inability to come into compliance with the rating agency and regulatory single risk limits that National and MBIA Corp. exceeded may also prevent us from writing future new business in the categories of risks that were exceeded, in the case of the regulatory limits, or result in an inability to achieve or maintain our desired ratings, in the case of rating agency limits, and may adversely affect our business prospects, and our failure to come into compliance with these guidelines and rules increases the risk of experiencing a large single loss or series of losses.

*Downgrades of the ratings of securities that we insure may materially adversely affect our business, results of operations and financial condition.*

Individual credits in our insured portfolio (including potential new credits) are assessed a rating agency capital charge based on a variety of factors, including the nature of the credits' risk types, underlying ratings, tenor and expected and actual performance. In the event of an actual or perceived deterioration in creditworthiness, a reduction in the underlying rating or a change in the rating agency capital methodology, we may be required to hold more capital in reserve against credits in the insured portfolio, regardless of whether losses actually occur, or against potential new business. Significant reductions in underlying ratings of credits in an insured portfolio can produce significant increases in assessed capital charges. There can be no assurance that each of our insurance company's capital position will be adequate to meet any increased rating agency reserve requirements or that each insurance company will be able to secure additional capital necessary to support increased reserve requirements, especially at a time of actual or perceived deterioration in creditworthiness of new or existing credits. Unless we were able to increase available capital, an increase in capital charges could reduce the amount of capital available to support our ratings and could have an adverse effect on our ability to write new business.



**Table of Contents****Item 1A. Risk Factors (continued)**

Since 2008, Moody's and S&P announced the downgrade of, or other negative ratings actions with respect to, certain transactions that we insure, as well as a large number of structured finance transactions that serve as collateral in structured finance transactions that we insure. There can be no assurance that additional securities in our insured portfolio will not be reviewed and downgraded in the future. Moreover, we do not know if, and when, the rating agencies might review additional securities in our insured portfolio or review again securities that have already been reviewed and/or downgraded. Downgrades of credits that we insure will result in higher capital charges to that insurance company under the relevant rating agency model or models, which could adversely affect our results of operations and financial condition going forward.

***Competition may have an adverse effect on our businesses.***

Our financial guarantee insurers face competition from other financial guarantee insurance companies and other forms of credit enhancement, including senior-subordinated structures, credit derivatives, letters of credit and guarantees (for example, mortgage guarantees where pools of mortgage loans secure debt service payments) provided by banks and other financial institutions. In addition, alternative financing structures may be developed that do not employ third-party credit enhancement. Furthermore, while one financial guarantee insurance company has written the vast majority of U.S. public finance new business since 2009, an additional recently established bond insurer is actively engaged in the market, and we have observed other new competitors indicating an interest in entering the bond insurance market and continue to consider strategies for launch. Increased competition, either in terms of price, alternative structures, or the emergence of new providers of credit enhancement, could have an adverse effect on our insurance companies' business prospects. The uncertainty created by market conditions and the related unpredictable actions of the regulators in the U.S. and foreign markets we serve may create unforeseen competitive advantages for our competitors due to, among other things, explicit or implied support from the government.

Cutwater faces intense competition from banks, insurance companies and independent companies who provide investment advisory services, as well as with companies who manage their investments in-house. Competition varies by product and typically can range from very large asset management firms to very small operations. Cutwater's ability to compete for new advisory services business and to retain existing accounts is largely dependent on its investment performance for a specific client or in general (typically versus established benchmark indices), the consistency of performance through market cycles, fee levels charged and the level of client service provided. A decline in our competitive position as to one or more of these factors could adversely affect our profitability and assets under management. Furthermore, many of Cutwater's competitors are large and well established and some have greater market share and breadth of distribution and offer a broader range of products, services or features. In order to compete for business, Cutwater may be required to expend a significant portion of its earnings on attracting new business, which would diminish the amount of dividends it can pay to MBIA Inc. Such competition could have an adverse impact on its ability to attract and retain business, which could have an adverse effect on our financial position and results of operations.

***Future demand for financial guarantee insurance depends on market and other factors that we do not control.***

The demand for financial guarantee insurance depends upon many factors, some of which are beyond the control of the Company. Our ability to attract and compete for financial guarantee business is largely dependent on the financial strength ratings assigned to our insurance companies by the major rating agencies. In addition, the perceived financial strength of all financial guarantee insurers also affects demand for financial guarantee insurance. Since 2008, all financial guarantee insurers' insurer financial strength ratings have been downgraded, placed on review for a possible downgrade or had their outlooks changed to negative, and the industry-wide downgrades may have eroded investors' confidence in the benefits of bond insurance. We do not expect the demand for financial guarantee insurance to regain its former levels in the near term, if ever.

We believe that issuers and investors distinguish among financial guarantors on the basis of various factors, including rating agency assessment, capitalization, size, insured portfolio concentration and financial performance. These distinctions may result in differentials in trading levels for securities insured by particular financial guarantors which, in turn, may provide a competitive advantage to those financial guarantors with better trading characteristics. In addition, various investors may, due to regulatory or internal guidelines, lack additional capacity to purchase securities insured by certain financial guarantors, which may provide a competitive advantage to guarantors with fewer insured obligations outstanding. Differentials in trading values or investor capacity constraints that do not favor us would have an adverse effect on our ability to attract new business at appropriate pricing levels.

**Table of Contents****Item 1A. Risk Factors (continued)**

***Regulatory change could adversely affect our businesses, and regulations limit investors' ability to effect a takeover or business combination that shareholders might consider in their best interests.***

The financial guarantee insurance industry has historically been and will continue to be subject to the direct and indirect effects of governmental regulation, including insurance laws, securities laws, tax laws, legal precedents and accounting rules affecting asset-backed and municipal obligations, as well as changes in those laws. These laws limit investors' ability to affect a takeover or business combination without the approval of our insurance regulators, and the failure to comply with applicable laws and regulations could expose our insurance companies, their directors or shareholders to fines, the loss of their insurance licenses, and the inability to engage in certain business activity, as the case may be.

In addition, future legislative, regulatory or judicial changes could adversely affect our insurance companies' ability to pursue business, materially impacting our financial results. Since 2009, both the NYSDFS and the New York legislature have proposed enhanced regulation of financial guarantee insurers which would impose limits on the manner and amount of business written by the Company. On the U.S. federal level, we could become subject to federal oversight or enhanced capital requirements, including if we are deemed systemically important under the Dodd-Frank Reform and Consumer Protection Act (the Dodd-Frank Act). Internationally, MBIA UK could also become subject to enhanced capital requirements as a result of the Solvency II Directive.

While it is not possible to predict if new laws, regulations or interpretations will be enacted or the impact they would have, any changes to such laws and regulations or the NYSDFS' interpretation thereof could subject MBIA to further restrictions on the type of business that it is authorized to insure, especially in the structured finance area. Any such restrictions could have a material effect on the amount of premiums that MBIA earns in the future. Additionally, any changes to such laws and regulations could subject our insurance companies to increase reserving and capital requirements or more stringent regulation generally, which could materially adversely affect our financial condition, results of operations and future business. Finally, changes to accounting standards and regulations may require modifications to our accounting methodology, both prospectively and for prior periods; and such changes could have an adverse impact on our reported financial results and/or make it more difficult for investors to understand the economics of our business, and may thus influence the types or volume of business that we may choose to pursue.

***Developments in the regulation of derivatives may create additional burdens on the Company.***

In July 2010, the Dodd-Frank Act was signed into law for the purpose of enacting broad financial industry regulatory reform, including by enhancing regulation of the over-the-counter derivatives markets. Among other reforms, the Dodd-Frank Act requires swap dealers and major swap participants to register with either or both of the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC), and to be subject to enhanced regulation, including capital requirements. The CFTC and SEC have promulgated rules to implement this enhanced regulatory framework, including final rules that require the Company to include its legacy insured derivatives in tests used to determine whether it is a major swap participant. MBIA Insurance Corporation registered with the CFTC as a major swap participant and on an ongoing basis is required to comply with the CFTC's business conduct rules as applied to portfolios in place prior to the enactment of the Dodd-Frank Act. As further rules are enacted, we expect to seek exemptions from certain of the rules that we do not believe we will be able to comply with, including capital requirements.

Because the CFTC has not yet issued final rules establishing capital requirements for major swap participants, the ultimate impact of such requirements on the Company is not yet clear. However, to the extent that the Company becomes subject to significant additional capital requirements, it is unlikely that the Company will be able to meet those standards.

**General Risk Factors**

***Any impairment in the Company's future taxable income can materially affect the recoverability of our deferred tax assets.***

The basis for evaluating the recoverability of a deferred tax asset is the existence of future taxable income of appropriate character. To the extent that the Company's ability to recognize future taxable income from its existing insurance portfolio through scheduled premium earnings and net investment income becomes impaired, the recoverability of certain deferred tax assets may be materially affected by a corresponding increase to its valuation allowance.

***A different view of the Internal Revenue Service from our current tax treatment of realized losses relating to insured CDS contracts can adversely affect our financial position.***



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As part of the Company's financial guarantee business, we have insured credit derivative contracts that were entered into by LaCrosse Financial Products, LLC with various financial institutions. We treat these insured derivative contracts as insurance contracts for statutory accounting purposes, which is the basis for computing U.S. federal taxable income. As such, the realized losses in connection with an insured event are considered loss reserve activities for tax purposes. Because the federal income tax treatment of CDS contracts is an unsettled area of tax law, in the event that the Internal Revenue Service has a different view with respect to the tax treatment, our results of operations and financial condition could be materially adversely affected.

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### **Item 1A. Risk Factors (continued)**

#### ***Private litigation claims could materially adversely affect our reputation, business, results of operations and financial condition.***

As further set forth in Note 14: Commitments and Contingencies in the Notes to Consolidated Financial Statements of MBIA Inc. and Subsidiaries in Part I, Item 1 of this Form 10-Q, the Company is named as a defendant in certain litigations. In the ordinary course of business, the Company and its subsidiaries may be defendants in or parties to pending and threatened legal actions and proceedings brought on behalf of various classes of claimants, including counterparties in various transactions. Although the Company intends to vigorously defend against the aforementioned actions and against other potential actions, an adverse ultimate outcome in these actions could result in a loss and have a material adverse effect on our reputation, business, results of operations or financial condition.

#### ***Ownership Change under Section 382 of the Internal Revenue Code can have adverse tax consequences.***

In connection with transactions in our shares from time to time, we may in the future experience an ownership change within the meaning of Section 382 of the Internal Revenue Code. In general terms, an ownership change may result from transactions increasing the aggregate ownership of certain stockholders in our stock by more than 50 percentage points over a testing period (generally three years). If an ownership change were to occur, our ability to use certain tax attributes, including certain losses, credits, deductions or tax basis, may be limited. Calculating whether a Section 382 ownership change has occurred is subject to uncertainties, including the complexity and ambiguity of Section 382 and limitations on a publicly traded company's knowledge as to the ownership of, and transactions in, its securities. The Company performs detailed calculations during each quarter to determine if an ownership change has occurred and, based on the Company's current methodology of calculation, a Section 382 ownership change has not taken place.

#### ***Interruption in telecommunication, information technology and other operational systems, or a failure to maintain the security, confidentiality or privacy of sensitive data residing on such systems, could harm our business.***

We depend heavily on our telecommunication, information technology and other operational systems and on the integrity and timeliness of data we use to run our businesses. These systems may fail to operate properly or become disabled as a result of events or circumstances wholly or partly beyond our control. Further, we face the risk of operational and technology failures by others, including various financial intermediaries and of vendors and parties to which we outsource the provision of services or business operations. If these parties do not perform as anticipated, we may experience operational difficulties, increased costs and other adverse effects on our business.

Despite our implementation of a variety of security measures, our information technology and other systems could be subject to physical or electronic break-ins, unauthorized tampering or other security breaches, resulting in a failure to maintain the security, confidentiality or privacy of sensitive data, including personal information relating to clients or transaction counterparties.

Interruption in telecommunication, information technology and other operational systems, or a failure to maintain the security, confidentiality or privacy of sensitive data residing on such systems, whether due to actions by us or others, could delay or disrupt our ability to do business, harm our reputation, subject us to regulatory sanctions and other claims, lead to a loss of clients and revenues and otherwise adversely affect our business.

#### ***The Company is dependent on key executives and the loss of any of these executives, or its inability to retain other key personnel, could adversely affect its business.***

The Company's success substantially depends upon its ability to attract and retain qualified employees and upon the ability of its senior management and other key employees to implement its business strategy. The Company believes there are only a limited number of available qualified executives in the business lines in which the Company competes. Although the Company is not aware of any planned departures, the Company relies substantially upon the services of Joseph W. Brown, Chief Executive Officer, and other senior executives. There is no assurance that the Company will be able to retain the services of key executives. The loss of the services of any of these individuals or other key members of the Company's management team could adversely affect the implementation of its business strategy.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

In connection with the Bank of America Settlement Agreement described in Note 1: Business Developments and Risks and Uncertainties in the Notes to Consolidated Financial Statements, on May 6, 2013, MBIA Inc. issued Blue Ridge Investments, L.L.C. ( Blue Ridge ), a subsidiary of Bank of America, a warrant to purchase 9,942,458 million shares of MBIA Inc. common stock at an exercise price of \$9.59 per share. The warrants were issued in reliance on an exemption from registration under Section 4(a)(2) under the 1933 Act as transactions by an issuer not involving any public offering.

Pursuant to the anti-dilution provisions of warrants that were issued by MBIA Inc. to Warburg Pincus Private Equity X, L.P. and certain of its affiliates ( Warburg Pincus ) under the Investment Agreement by and between MBIA Inc. and Warburg Pincus, dated as of December 10, 2007, as amended and restated as of February 6, 2008, (the Investment Agreement ), as a result of the issuance of the warrant to Blue Ridge (a) Warburg Pincus s 21,327,646 warrants exercisable at \$30.25 per share were revised to 21,914,446 warrants exercisable at \$29.44 per share and (b) Warburg Pincus s 4,000,000 of warrants exercisable at \$16.20 per share were revised to 4,004,945 warrants exercisable at \$16.18 per share. In addition, under the Investment Agreement Warburg has certain gross up rights that are triggered in connection with the offering by the Company of any equity securities. As a settlement of any such gross-up rights Warburg Pincus may have had under the Investment Agreement due to the issuance of the warrant to Blue Ridge, on August 5, 2013 MBIA Inc. issued Warburg Pincus a warrant to purchase 1,910,417 shares of MBIA Inc. common stock at an exercise price of \$9.59 per share in exchange for Warburg Pincus delivering to the Company 536,375 shares of MBIA Inc. common stock having a value of \$7,262,518 based on the closing price of the Company s stock as of the close of business on July 23, 2013. The warrants issued pursuant to the anti-dilution adjustments and the gross-up rights were issued in reliance on an exemption from registration under Section 4(a)(2) under the 1933 Act as transactions by an issuer not involving any public offering.

The table below presents repurchases made by the Company in each month during the third quarter of 2013:

Month	Total Number of Shares Purchased <sup>(1)</sup>	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Amount That May Be Purchased Under the Plan (in millions) <sup>(2)</sup>
July	330	\$ 13.54	-	\$ 23
August	649,038 <sup>(3)</sup>	13.35	-	23
September	85,148	11.40	-	23
	734,516	\$ 13.12	-	\$ 23

(1) - 196,255 shares were repurchased by the Company in open market transactions for settling awards under the Company s long-term incentive plans and 1,886 shares were purchased in open market transactions as an investment in the Company s non-qualified deferred compensation plan.

(2) - On February 1, 2007, the Company s Board of Directors authorized the repurchase of common stock up to \$1 billion under a new share repurchase program, which superseded the previously authorized program.

(3) - Includes 536,375 shares, having a value of \$13.54 per share as of the close of business on July 23, 2013, received from Warburg Pincus in exchange for the issuance to Warburg Pincus of a warrant to purchase 1,910,417 shares of MBIA Inc. common stock at an exercise price of \$9.59 per share as a settlement of any gross-up rights Warburg Pincus may have had, as described further above.

**Item 5. Other Information**

On November 11, 2013 Kewsong Lee resigned from the Board of Directors of MBIA Inc. Mr. Lee was elected to the Board of Directors in January 2008.

Mr. Lee was nominated by Warburg Pincus Private Equity X, L.P. ( Warburg Pincus ) to be elected to the Board of Directors pursuant to the amended and restated Investment Agreement dated as of February 6, 2008 (the Investment Agreement ) between MBIA Inc. and Warburg Pincus. Under the Investment Agreement, David A. Coulter, Warburg Pincus s remaining member of the Board of Directors, has the right to

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designate Mr. Lee's replacement on the Board of Directors, and the Board of Directors is required to use its reasonable best efforts to take all action required to fill the vacancy resulting from Mr. Lee's resignation with Mr. Coulter's designee.

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**Item 6. Exhibits**

- 4.1. Warrant Agreement, dated as of August 5, 2013, between MBIA Inc. and Warburg Pincus Private Equity X, L.P., incorporated by reference to Exhibit 4.2 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2013.
- +31.1. Chief Executive Officer - Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- +31.2. Chief Financial Officer - Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- \*32.1. Chief Executive Officer - Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- \*32.2. Chief Financial Officer - Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- +99.1. Additional Exhibits - National Public Finance Guarantee Corporation and Subsidiaries GAAP Consolidated Financial Statements.
- +99.2. Additional Exhibits - MBIA Insurance Corporation and Subsidiaries GAAP Consolidated Financial Statements.
- +99.3. Novation Agreement, dated as of September 14, 2012, between Financial Guaranty Insurance Company and National Public Finance Guarantee Corporation.
- +101. Additional Exhibits - MBIA Inc. and Subsidiaries Consolidated Financial Statements and Notes to Consolidated Financial Statements from the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2013, formatted in XBRL.

+ Filed Herewith

\* Furnished Herewith

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MBIA Inc.

Registrant

Date: November 12, 2013

/s/ C. Edward Chaplin  
C. Edward Chaplin  
Chief Financial Officer

Date: November 12, 2013

/s/ Douglas C. Hamilton  
Douglas C. Hamilton  
Controller (Principal Accounting Officer)