

April 13, 2010

The New York Insurance Department Provides FGIC With Additional Time To Bring Its Minimum Surplus Into Compliance

This is an update to the Chadbourne & Parke LLP Client Alert, "New York Insurance Department Orders FGIC to Stop Writing Insurance Policies and to Cease Paying Claims Until Its Minimum Surplus is Brought Into Compliance," dated December 3, 2009. That alert discussed the actions taken by the New York Insurance Department (the "Insurance Department") in connection with Financial Guaranty Insurance Company's ("FGIC") noncompliance with New York's surplus and capital requirements. The Insurance Department initially ordered FGIC, a New York domiciled financial guaranty insurer, to remedy its capital impairment and to bring its minimum surplus to policyholders into compliance by March 25, 2010. However, on March 25, 2010, the Insurance Department extended this deadline to June 15, 2010.

The Insurance Department initially ordered FGIC to cease writing any new policies and to suspend payment of all claims effective November 24, 2009 (the "Order"). That Order followed the release of FGIC's Quarterly Statement for the third quarter of 2009, in which FGIC reported that as of September 30, 2009, it suffered a policyholder surplus deficit of \$865,834,577 and an impairment of its required minimum surplus to policyholders of \$932,234,577. Under the Order, the Insurance Department gave FGIC until January 5, 2010 to submit a detailed and final proposed Surplus Restoration Plan.

On December 22, 2009 FGIC provided the Insurance Department with a proposed Surplus Restoration Plan. According to FGIC's 2009 Annual Statement, the Surplus Restoration Plan is designed to fulfill the requirements of the Insurance Department Order and contemplates the following key loss mitigation components: (i) remediating a substantial portion of FGIC's exposure to residential mortgage-backed securities ("RMBS") and asset-backed securities ("ABS CDO"), and (ii) commuting, restructuring or reinsuring a substantial portion of FGIC's remaining exposure to ABS CDOs and to certain other obligations for which it has established statutory loss reserves, including RMBS insured by FGIC in the secondary market, pursuant to consensual transactions. Also, according to FGIC's 2009 Annual Statement, its policyholder surplus deficit has increased to \$1.28 billion as of December 31, 2009.

As part of this plan, FGIC recently announced that it and its subsidiary, FGIC Credit Products LLC ("FGIC Credit"), entered into commitment and support agreements ("CSA") with seven counterparties to credit default swaps ("CDS") with FGIC Credit allowing FGIC to mitigate its exposure to claims based upon mark-to-market termination payments under the CDS. The outstanding CDS held by the counterparties have been insured by FGIC and have a par value of approximately \$11.7 billion. Under the CSA, the counterparties have agreed to refrain from exercising certain rights thereunder, notably early termination rights,

until the earlier of July 31, 2010, or the occurrence of certain specified events. The CSA contemplates that FGIC will form and capitalize a wholly owned subsidiary (“Drop Down Company”) to assume FGIC’s rights, obligations, and liabilities in connection with the FGIC policies covering those CDS. Upon closing, the counterparties would waive all early termination rights existing as of the closing date under all CDS held by them and would modify all future early termination rights under the CDS covered by the FGIC policies assumed by Drop Down Company. Each CDS counterparty, however, would retain the right to terminate the CDS should the Insurance Department appoint the

Superintendent as liquidator or rehabilitator of Drop Down Company. For its part, Drop Down Company would receive 1.5% of the gross par amount less certain capitalization costs from FGIC.

To date, the Insurance Department has not publicly stated whether it deems the Surplus Restoration Plan satisfactory but has not taken any further action beyond extension of the deadline for FGIC to remedy its capital and policyholder surplus deficit. As noted, FGIC’s policyholder surplus deficit has increased since the third quarter of 2009 to \$1.28 billion as of December 31, 2009. We will continue to monitor developments as to FGIC.

Our client alerts are for general informational purposes and should not be regarded as legal advice. If you would like additional information or have any questions, please contact:

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