REPORT ON EXAMINATION

OF

NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION

AS OF

DECEMBER 31, 2015

DATE OF REPORT	MAY 1, 2017
EXAMINER	KAREN GARD, CFE

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NEW YORK STATE
DEPARTMENT of
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Maria T. Vullo
Superintendent

May 1, 2017

Honorable Maria T. Vullo
Superintendent
New York State Department of Financial Services
Albany, New York 12257

Madam:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 31473 dated April 12, 2016, attached hereto, I have made an examination into the condition and affairs of National Public Finance Guarantee Corporation as of December 31, 2015, and submit the following report thereon.

Wherever the designation "the Company" or "National" appears herein without qualification, it should be understood to indicate National Public Finance Guarantee Corporation.

Wherever the term "the Department" appears herein without qualification, it should be understood to mean the New York State Department of Financial Services.

The examination was conducted at the Company's home office located at 1 Manhattanville Road Suite 301 Purchase, New York 10577-2100.

1. SCOPE OF EXAMINATION

The Department has performed an individual examination of the Company, a multi-state insurer. The previous examination was conducted as of December 31, 2011. This examination covered the four-year period from January 1, 2012 through December 31, 2015. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner. The examination of the Company was performed concurrently with the examination of MBIA Insurance Corporation ("MBIA Corp").

This examination was conducted in accordance with the National Association of Insurance Commissioners ("NAIC") Financial Condition Examiners Handbook ("Handbook"), which requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company and evaluating system controls and procedures used to mitigate those risks. This examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All financially significant accounts and activities of the Company were considered in accordance with the risk-focused examination process. This examination also included a review and evaluation based upon the Company's Sarbanes Oxley documentation and testing. The examiners also relied upon audit work performed by the Company's independent public accountants when appropriate.

This examination report includes a summary of significant findings for the following items as called for in the Handbook:

Company history
Corporate records
Management and control

Fidelity bonds and other insurance
Territory and plan of operation
Loss experience
Reinsurance
Accounts and records
Financial statements
Summary of recommendations
Significant subsequent events

A review was also made to ascertain what action was taken by the Company with regard to comments contained in the prior report on examination.

This report on examination is confined to financial statements and comments on those matters that involve departures from laws, regulations or rules, or that are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

National Public Finance Guarantee Corporation was incorporated as Inland National Insurance Company under the laws of the state of Illinois on December 28, 1959, and began business on March 9, 1960. The name was changed on December 17, 1984 to Bond Investors Guaranty Insurance Company, which was then a subsidiary of Bond Investors Group ("BIG").

Effective January 5, 1990, MBIA Inc. purchased all the outstanding shares of BIG, the Company's former parent. MBIA Inc. then contributed the stock of BIG to its subsidiary, Municipal Bond Investors Assurance Corporation, now known as MBIA Insurance Corporation ("MBIA Corp."). Subsequent to the contribution, BIG was liquidated, making MBIA Corp. the direct parent of the Company. The Company changed its name to MBIA Insurance Corporation of Illinois ("MBIA IL") on August 21, 1990.

On February 17, 2009, the Department approved a restructuring (also known as "Transformation") of MBIA Corp. As part of the restructuring, the stock of MBIA IL was transferred to a newly established intermediate holding company, National Public Finance

Guarantee Holdings, Inc. ("National Holdings"), which is wholly-owned by MBIA Inc. National was capitalized with approximately $2.1 billion from funds distributed by MBIA Corp. to MBIA Inc. as a dividend and return of capital, which MBIA Inc. then contributed to National through National Holdings. Effective December 1, 2009, the Company re-domesticated from Illinois to New York, and changed its name to National.

In June 2009, a group of 18 financial institutions commenced a legal proceeding challenging the Department's actions in approving Transformation. In March 2013, the Supreme Court of the State of New York dismissed this proceeding, thereby upholding the Department's decision to approve MBIA Corp.'s restructuring. Two of the financial institutions, Bank of America ("BoA") and Société Générale ("SocGen"), filed a notice of appeal. The same group of financial institutions also filed suit alleging that certain terms of the restructuring transactions constituted fraudulent conveyances and a breach of the implied covenant of good faith and fair dealing under New York law. In May 2013, MBIA Inc., MBIA Corp. and National entered into various settlement agreements with BoA and SocGen. As a result of these settlements, all litigation related to the restructuring of MBIA Corp. has been resolved.

In February 2010, National established National Real Estate Holdings of Armonk, LLC ("NREHA"), a wholly-owned subsidiary of National in order to purchase MBIA Corp.'s interest in certain real estate for purposes of conducting National's business, including leasing its property to certain affiliates. In the fourth quarter 2015, after the sale of its office complex in Armonk, NY that once served as the Company's headquarters, National liquidated its investment in NREHA.

Common capital stock paid in of $15,000,000 is comprised of 500,000 shares par value $30 authorized, issued and outstanding as of December 31, 2015. Gross paid in and contributed surplus is $547,441,226.

A. Management

Pursuant to the Company's charter and by-laws, management of the Company is vested in a board of directors consisting of not less than seven nor more than 21 members. The board meets quarterly during each calendar year. At December 31, 2015, the board of directors was comprised of the following seven members:

Name and Residence	Principal Business Affiliation
William C. Fallon Rye, NY	Chairman, Chief Executive Officer and President National Public Finance Guarantee Corporation
Adam T. Bergonzi White Plains, NY	Managing Director, Chief Risk Officer and Assistant Secretary National Public Finance Guarantee Corporation
Patricia K. Ferrari New York, NY	Managing Director National Public Finance Guarantee Corporation
Douglas C. Hamilton Armonk, NY	Assistant Vice President and Controller MBIA Inc.
Andrea E. Randolph Stamford, CT	Chief Technology Officer and Managing Director National Public Finance Guarantee Corporation
Joseph R. Schachinger Eastchester, NY	Managing Director MBIA Services Corporation
Ram D. Wertheim Westport, CT	Executive Vice President and Chief Legal Officer MBIA Inc.

A review of the minutes of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended and each board member had an acceptable record of attendance.

As of December 31, 2015, the principal officers of the Company were as follows:

Name	Title
William C. Fallon	Chairman, Chief Executive Officer and President
Daniel E. McManus, Jr.	Managing Director, Chief Compliance Officer and Secretary
Christopher H. Young	Managing Director, Chief Financial Officer and Treasurer
Adam T. Bergonzi	Managing Director, Chief Risk Officer and Assistant Secretary

B. Territory and Plan of Operation

As of December 31, 2015, the Company was licensed to write business in all 50 states, the District of Columbia, and Puerto Rico.

As of the examination date, the Company was authorized to transact the kinds of insurance as defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

Paragraph	Line of Business
16	Fidelity and surety
17	Credit
25	Financial guaranty

Based on the lines of business for which the Company is licensed and the Company's current capital structure, and pursuant to the requirements of Articles 13, 41 and 69 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of $66,400,000.

The following schedule shows the direct premiums written by the Company both in total and in New York for the period under examination:

Calendar Year	Premiums Written in New York State	Total Direct Premiums Written	Direct Premiums Written in New York State as a Percentage of Total Premium
2012	$ 923	$ 923	100.00%
2013	$ 686	$ 686	100.00%
2014	$ 498	$6,475,596	0.01%
2015	$58,338	$4,568,671	1.28%

Due to the litigation resulting from the Transformation restructuring and the low ratings given by the rating agencies, National was not able to write a significant amount of business during the period under examination. On March 18, 2014, Standard & Poor's Financial Services LLC

("S&P") upgraded its rating on National to AA- with a stable outlook. Subsequently, National commenced writing new business in the public finance sector.

The financial guarantees issued by National provide an unconditional and irrevocable guarantee of payment when due of the principal, interest or other amounts owing on insured obligations. Insured obligations consists of U.S. public finance exposures, such as municipal bonds, including tax-exempt and taxable indebtedness of U.S. political subdivisions, as well as utility districts, airports, health care institutions, higher education facilities, student loan issuers, housing authorities and other similar agencies and obligations issued by private entities that finance public-purpose projects. Payments to be made by the issuer of the bonds or notes may be backed by a pledge of revenues, reserve funds, letters of credit, investment contracts or collateral in the form of mortgages or other assets. The right to such funds or collateral would typically become National's upon the payment of a claim by National.

Prior to commencing writing new business in 2014, National's insured portfolio consisted exclusively of legacy business arising from:

1) National's assumption of MBIA Corp.'s U.S. public finance financial guarantee policies pursuant to the Quota Share Reinsurance Agreement, executed in connection with Transformation;

2) Certain public finance financial guarantee policies of Financial Guaranty Insurance Company ("FGIC") which were originally reinsured by MBIA Corp., subsequently assigned to and reinsured by National in connection with Transformation, and ultimately novated to National pursuant to a novation agreement between National and FGIC effective August 2013.

In 2015, substantially all of National's earned premium of $349,655,880 is attributable to this legacy business.

C. <u>Reinsurance</u>

Assumed reinsurance accounted for approximately 74% of the Company's gross premium written as of December 31, 2015. During the period covered by this examination, the Company's assumed reinsurance business has decreased since the last examination. Substantially all of the

Company's assumed premiums arise from the quota share reinsurance agreement with MBIA Corp. described below. The Company utilizes reinsurance accounting as defined in Statement of Statutory Accounting Principle ("SSAP") No. 62R for all of its assumed reinsurance business.

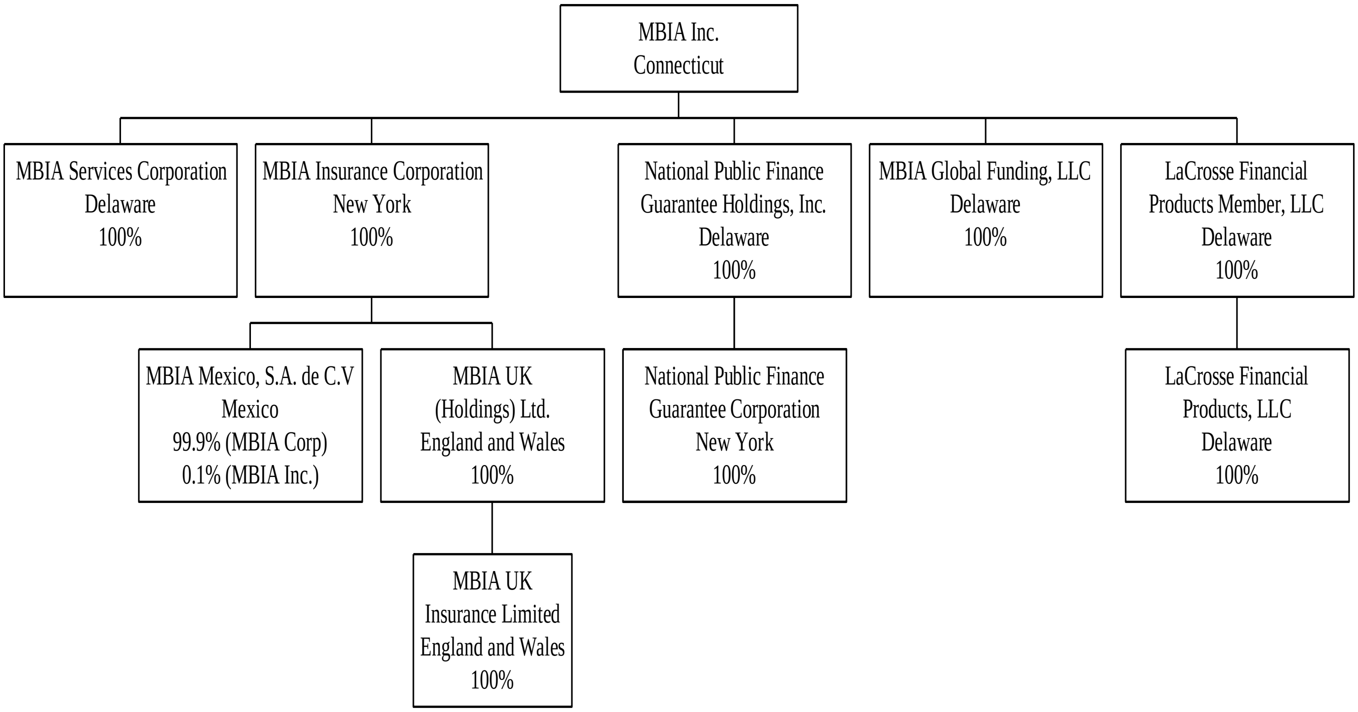
Effective January 1, 2009, National and MBIA Corp. entered into a 100% Quota Share Reinsurance Agreement, executed as part of Transformation, pursuant to which MBIA Corp. ceded all of its U.S. public finance exposure to National.

This agreement was filed with the Department in accordance with Section 1505 of the New York Insurance Law.

D. Holding Company System

The Company is an indirect wholly-owned subsidiary of MBIA Inc., a Connecticut corporation, with its principal offices in Purchase, New York. A review of the Holding Company Registration Statements filed with this Department indicated that such filings were complete and were filed in a timely manner pursuant to Article 15 of the New York Insurance Law and Department Regulation 52.

The following is an abridged chart of the holding company system at December 31, 2015:


MBIA Inc.
Connecticut
MBIA Services Corporation
Delaware
100%
MBIA Insurance Corporation
New York
100%
National Public Finance
Guarantee Holdings, Inc.
Delaware
100%
MBIA Global Funding, LLC
Delaware
100%
LaCrosse Financial
Products Member, LLC
Delaware
100%
MBIA Mexico, S.A. de C.V
Mexico
99.9% (MBIA Corp)
0.1% (MBIA Inc.)
MBIA UK
(Holdings) Ltd.
England and Wales
100%
National Public Finance
Guarantee Corporation
New York
100%
LaCrosse Financial
Products, LLC
Delaware
100%
MBIA UK
Insurance Limited
England and Wales
100%

As of December 31, 2015, the Company was party to the following agreements with other members of its holding company system:

Repurchase and Reverse Repurchase Agreement ("Asset Swap") with MBIA Inc.

In the first quarter of 2009, National entered into an agreement with MBIA Inc. whereby National held securities under agreements to resell and under agreements to repurchase up to $2.0 billion based on the fair value of the securities borrowed by MBIA Inc. The Asset Swap provides MBIA Inc. with eligible assets to pledge under investment agreement contracts, and the agreements reset on a quarterly basis. As of December 31, 2015, the notional amount of the Asset Swap was below 5% of National's admitted assets. The Asset Swap was approved by the Department in connection with Transformation.

Master Services Agreement with MBIA Services Corporation ("MSC")

MSC (formerly known as Optinuity Alliance Resources Corporation), created in the first quarter of 2010, provides support services such as management, legal, accounting, treasury, and information technology for all business written or reinsured and all other authorized activities of affiliates, including National.

Tax Allocation Agreement

The Company is party to a tax allocation agreement with members of its holding company system effective January 1, 1987. The agreement was amended and restated effective September 8, 2011 to change the method of calculating each domestic insurer's tax liability to the method permitted by paragraph 3(a) of Department Circular Letter No. 33 (1979).

Sublease Agreement

Effective May 2014, the Company, entered into a sublease agreement with MSC and MBIA Corp. wherein the Company, as sub-landlord, subleases office space to MSC and MBIA Corp. Per the terms of the sub-lease agreement, MSC and MBIA Corp. pay rent equal to their proportionate share of the fixed annual rent, additional rent, and tenant improvement costs specified in the prime lease held by the Company.

All agreements subject to Section 1505 of the New York Insurance Law were submitted to the Department.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2015, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	1%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	49%
Two-year overall operating ratio	0%

The Company reported a negligible amount of premiums in course of collection at December 31, 2015. All of the above ratios fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

The underwriting ratios presented below are on an earned/incurred basis and encompass the four-year period covered by this examination:

	Amounts	Ratios
Losses and loss adjustment expenses incurred	$ 171,266,082	11.57%
Other underwriting expenses incurred	320,866,848	21.68
Net underwriting gain	988,102,785	66.75
Premiums earned	$1,480,235,715	100.00%

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2015 as reported by the Company:

	Assets	Assets Not Admitted	Net Admitted Assets
Bonds	$4,077,989,383	$ 0	$4,077,989,383
Common stocks	162,815,906	23,160,983	139,654,923
Cash, cash equivalents and short-term investments	402,614,764	0	402,614,764
Other invested assets	10,002,383		10,002,383
Receivables for securities	5,529,940	3,294	5,526,646
Investment income due and accrued	25,953,974	0	25,953,974
Uncollected premiums and agents' balances in the course of collection	29	0	29
Amounts recoverable from reinsurers	16,294	0	16,294
Net deferred tax asset	379,103,395	367,256,309	11,847,086
Electronic data processing equipment and software	1,257,779	1,257,779	0
Furniture and equipment, including health care delivery assets	14,944,224	14,944,224	0
Receivables from parent, subsidiaries and affiliates	202,644	0	202,644
Prepaid expenses	908,950	908,950	0
Other assets	2,797,331	28,259	2,769,072
Total assets	$5,084,136,996	$407,559,798	$4,676,577,198

Liabilities, Surplus and Other Funds

Losses and loss adjustment expenses	$ (29,848,059)
Other expenses (excluding taxes, licenses and fees)	17,910,397
Taxes, licenses and fees (excluding federal and foreign income taxes)	73,596
Current federal and foreign income taxes	17,476,220
Unearned premiums	1,042,418,873
Ceded reinsurance premiums payable (net of ceding commissions)	11,116
Amounts withheld or retained by company for account of others	5,423,221
Payable to parent, subsidiaries and affiliates	446,478
Payable for securities	36,386,237
Contingency reserve	910,041,842
Securities sold under agreement to repurchase	198,694,034
Other liability	566
Total liabilities	$2,199,034,521

Surplus and other funds

Common capital stock	$ 15,000,000
Gross paid in and contributed surplus	574,441,226
Unassigned funds (surplus)	1,888,101,451
Surplus as regards policyholders	$2,477,542,677
Total liability, surplus and other funds	$4,676,577,198

Note: The examiner is unaware of any potential exposure of the Company to any tax assessment and no liability has been established herein relative to such contingency. The Internal Revenue Service has not audited or scheduled an audit for the period under examination.

B. Statement of Income

The Company's net income during the four-year examination period January 1, 2012 through December 31, 2015 was $1,193,436,630, detailed as follows:

Underwriting Income		
Premiums earned		$1,480,235,715
Deductions:		
Losses and loss adjustment expenses incurred	$171,266,082	
Other underwriting expenses incurred	320,866,848	
Total underwriting deductions		492,132,930
Net underwriting gain or (loss)		988,102,785
Investment Income		
Net investment income earned	581,673,429	
Net realized capital gain	110,389,296	
Net investment gain or (loss)		692,062,725
Other Income		
Miscellaneous income		17,964,534
Net income before federal and foreign income taxes		$1,698,130,044
Federal and foreign income taxes incurred		504,693,414
Net income		$1,193,436,630

C. Capital and Surplus

Surplus as regards policyholders increased $1,053,880,565 during the four-year examination period January 1, 2012 through December 31, 2015, detailed as follows:

Surplus as regards policyholders per report on examination as of December 31, 2011			$1,423,662,112
	Gains in Surplus	Losses in Surplus	
Net income	$1,193,436,630		
Net unrealized capital gains or (losses)	4,044,060		
Change in net deferred income tax		$181,858,038	
Change in non-admitted assets	138,904,391		
Cumulative effect on change in accounting principles	13,017,655		
Surplus adjustments paid in	6		
Dividends to stockholders		547,857,965	
Allocation of surplus to contingency reserves	434,193,826	0	
Net increase (decrease) in surplus	$1,783,596,568	$729,716,003	$1,053,880,565
Surplus as regards policyholders per report on examination as of December 31, 2015			$2,477,542,677

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination negative liability for the captioned items of ($54,797,141), is the same as reported by the Company as of December 31, 2015. This negative liability was determined to be adequate.

The Capital Markets Division utilized the assistance of an independent financial advisory firm that specializes in complex assets to review the adequacy of the Company's modeling, assumptions, and surveillance policies and procedures as of December 31, 2015, and to determine the Company's adequacy of loss reserves.

To ensure proper coverage of risk factors, the portfolio was segregated into sectors. A review of all U.S. public finance was made, consisting of 4,500 distinct obligors, approximately $161 billion in gross par outstanding ("GPO"). Three levels of review were made before considering obligors that needed to be tested for losses. First, obligors whose credit rating was above A- or A3 were eliminated, then those obligors not in a high risk sector. The remaining 332 obligors, GPO of $37.3 billion, were of credit concern and reviewed in greater depth by analysts from the independent financial advisory firm. Of the 332 obligors, 24 obligors, comprising GPO of $18.4 billion, were considered likely to have claims and were evaluated under various scenarios.

The most significant liabilities with potential for future adverse loss and claims development are the various obligations of Puerto Rico and the obligations of the Chicago Board of Education.

The Company's estimate of reserves for losses on its exposures is based on certain assumptions. Changes in such assumptions could materially adversely affect such reserve estimates, including as a result of more adverse macroeconomic conditions, the bankruptcies of issuers of insured bonds or swap counterparties, and the amount and timing of any claims. Under certain conditions, many of which are event-driven and outside the control of the Company, these exposures may result in significant increases in claims beyond those assumed in the Company's reserve estimate (which may or may not result in an increase in such loss reserves). In addition, the value of the Company's investment portfolio could change and have a materially adverse effect.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained the following comments as follows (page numbers refer to the prior report):

ITEM		PAGE NO.
A	**Litigation risk** The examiner commented that prior to the settlement of the litigation, the management of National operated the Company as a going concern with the expectation that National would achieve ratings upgrades after the uncertainty of the restructuring litigation and MBIA Corp.'s put-back litigation would be resolved. As a result of the termination of the litigations, both S&P and Moody's have raised their financial strength ratings on National to A and Baa1, respectively.	18
	Since the dismissal of the Article 78 proceeding in 2013, the Company has received numerous upgrades by the rating organizations. As of December 31, 2015, the Company was rated AA+ with a stable outlook by Kroll Bond Rating Agency, AA- with a stable outlook by S&P, and A3 with a negative outlook by Moody's Investors Services, Inc.	
B	**Liquidity Risk – Loans to Affiliates** The examiner commented that during the year ended December 31, 2012, MBIA Corp. borrowed an additional $443 million under the secured loan agreement with National. The examiner further commented that the secured loan agreement was repaid in full and then terminated. Secondly the examiner commented that as of December 31, 2012, the notional amount utilized under the Asset Swap with MBIA Inc. was $481 million and the fair value of the collateral pledged by National and MBIA Inc. under these agreements was $502 million and $529 million, respectively. National has committed to the Department to use commercially reasonable efforts to reduce the amount of the Asset Swap over time.	19
	As of December 31, 2015, the Company has reduced the notional amount of the Asset Swap to below 5% of National's admitted assets.	

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

The examiner reviewed and evaluated certain risks that existed as of the examination date, and also assessed certain prospective risks that are anticipated to arise or extend past the examination completion date. The Company monitors on an ongoing basis prospective risks, including the following:

Reserving Risk

As of December 31, 2015, National has a consolidated exposure to Puerto Rico of approximately $3.9 billion, including insuring approximately $1.4 billion of Puerto Rico Electric Power Authority ("PREPA") bonds, approximately $1 billion of Commonwealth of Puerto Rico bonds, approximately $700 million of Puerto Rico Sales Tax Financing Corporation ("COFINA") bonds, approximately $700 million of Puerto Rico highway and transportation bonds ("PRHTA"), and $90 million of University of Puerto Rico bonds. S&P, Fitch Ratings and/or Moody's have downgraded the ratings of all Puerto Rico issuers (except InterAmerican University of Puerto Rico, Inc.) to below investment grade due to narrowing liquidity, sluggish economic growth and persistent structural deficits. Although National believes its Puerto Rico risks are comfortably within its claims-paying resources, and has undertaken alternate risk mitigation strategies (i.e. the restructuring support agreement with Puerto Rico and other stakeholders), the overall extent and duration of other stressed credits, coupled with Puerto Rico, are uncertain. Also, National has exposure to $998 million of Chicago Board of Education bonds which S&P and Moody's have rated as below investment grade.

Reputational Risk

Although the Company is a distinct legal entity from MBIA Corp., from which MBIA Corp. receives no recourse, the Company may face reputational damage if MBIA Corp. is not able to fulfill its claims obligations.

Respectfully submitted,

____
Karen Gard, CFE
Associate Insurance Examiner

STATE OF NEW YORK)
)ss:
COUNTY OF NEW YORK)

Karen Gard, being duly sworn, deposes and says that the foregoing report, subscribed by her, is true to the best of her knowledge and belief.

____
Karen Gard

Subscribed and sworn to before me

this__________ day of ____________________, 2017.

APPOINTMENT NO. 31473

NEW YORK STATE

DEPARTMENT OF FINANCIAL SERVICES

*I, **Maria T. Vullo**, Acting Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:*

Karen Gard

as a proper person to examine the affairs of the

National Public Finance Guarantee Corporation

and to make a report to me in writing of the condition of said

COMPANY

with such other information as she shall deem requisite.

In Witness Whereof, I have hereunto subscribed by name
and affixed the official Seal of the Department
at the City of New York

this 12th day of April, 2016

Maria T. Vullo
Acting Superintendent of Financial Services

By:

Eileen Fox
Assistant Chief Examiner