National Public Finance Guarantee Corporation

Statutory-Basis Financial Statements
December 31, 2014 and 2013

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Independent Auditor's Report

To the Board of Directors of National Public Finance Guarantee Corporation:

We have audited the accompanying statutory financial statements of National Public Finance Guarantee Corporation (the "Company"), which comprise the statutory statements of admitted assets, liabilities and capital and surplus as of December 31, 2014 and 2013, and the related statutory statements of income, changes in capital and surplus, and cash flows for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the accounting practices prescribed or permitted by the New York State Department of Financial Services. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles

As described in Note 2 to the financial statements, the financial statements are prepared by the Company on the basis of the accounting practices prescribed or permitted by the New York State Department of Financial Services, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

The effects on the financial statements of the variances between the statutory basis of accounting described in Notes 2 and 7 and accounting principles generally accepted in the United States of America are material.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the "Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles" paragraph, the financial statements referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the Company as of December 31, 2014 and 2013, or the results of its operations or its cash flows for the years then ended.

Opinion on Statutory Basis of Accounting

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and capital and surplus of the Company as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended, in accordance with the accounting practices prescribed or permitted by the New York State Department of Financial Services described in Note 2.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental schedules listed in the attached index of the Company as of December 31, 2014 and for the year then ended are presented for purposes of additional analysis and are not a required part of the financial statements. The supplemental schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The effects on the supplemental schedules of the variances between the statutory basis of accounting and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material. As a consequence, the supplemental schedules do not present fairly, in conformity with accounting principles generally accepted in the United States of America, such information of the Company as of December 31, 2014 and for the year then ended. The supplemental schedules have been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplemental schedules are fairly stated, in all material respects, in relation to the financial statements taken as a whole.

PricewaterhouseCoopers LLP

March 2, 2015

NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION

STATUTORY-BASIS STATEMENTS OF ADMITTED ASSETS, LIABILITIES and CAPITAL and SURPLUS

(Dollars in thousands except share and per share amounts)

	December 31, 2014	December 31, 2013
Admitted Assets		
Investments:		
Fixed-maturity securities, at amortized cost		
(fair value $4,235,693 and $3,972,293, respectively)	$ 4,163,506	$ 4,056,686
Investments in unaffiliated common stock, at fair value	127,200	118,892
Securities purchased under agreements to resell (parent)	443,200	446,500
Short-term investments, at amortized cost		
which approximates fair value	99,780	407,268
Receivable for securities	21,255	612
Other invested assets	44,970	45,478
Total investments	4,899,911	5,075,436
Cash and cash equivalents	187,418	190,924
Total cash and investments	5,087,329	5,266,360
Accrued investment income	27,810	29,373
Current tax receivable	-	6,126
Deferred tax asset	25,392	25,704
Other assets	1,831	12,125
Total admitted assets	$ 5,142,362	$ 5,339,688
Liabilities, Capital and Surplus		
Liabilities:		
Deferred premium revenue	$ 1,375,075	$ 1,677,966
Loss and loss adjustment expense reserves (net of subrogation recoverable)	(12,540)	(86,739)
Contingency reserve	1,075,897	1,172,026
Securities sold under agreements to repurchase (parent)	443,200	446,500
Current income taxes	9,192	-
Payable for securities	39,819	29,665
Other liabilities	21,309	14,138
Total liabilities	2,951,952	3,253,556
Capital and Surplus:		
Common stock, par value $30 per share;		
authorized, issued and outstanding - 500,000 shares	15,000	15,000
Additional paid-in capital	574,441	574,441
Unassigned surplus	1,600,969	1,496,691
Total capital and surplus	2,190,410	2,086,132
Total liabilities, capital and surplus	$ 5,142,362	$ 5,339,688

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

NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION
STATUTORY-BASIS STATEMENTS OF INCOME

(Dollars in thousands)

	Years ended December 31, 2014	Years ended December 31, 2013
Revenues:		
Gross premiums written	$ 13,209	$ 12,055
Ceded premiums	-	-
Net premiums written	13,209	12,055
Decrease in deferred premium revenue	303,218	362,754
Net premiums earned	316,427	374,809
Expenses:		
Losses incurred	76,315	39,267
Loss adjustment expenses incurred	11,892	29,395
Other underwriting expenses	49,862	76,145
Total underwriting expenses	138,069	144,807
Net underwriting gain	178,358	230,002
Investment income:		
Net investment income	117,815	133,274
Net realized capital gains (less tax of $6,636 and $10,336)	12,120	28,724
Net investment gain	129,935	161,998
Other income, net	17,968	7
Income before income taxes (after capital gains tax)	326,261	392,007
Provision for income taxes	88,123	136,058
Net income	$ 238,138	$ 255,949

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

NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION

STATUTORY-BASIS STATEMENTS OF CHANGES IN CAPITAL AND SURPLUS

For the years ended December 31, 2014 and 2013

(Dollars in thousands except share amounts)

	Common Stock		Additional Paid-in	Unassigned	Total Capital and
	Shares	Amount	Capital	Surplus	Surplus
Balance, January 1, 2013	500,000	$ 15,000	$ 574,441	$ 1,409,098	$ 1,998,539
Net income	-	-	-	255,949	255,949
Change in deferred income taxes	-	-	-	(5,052)	(5,052)
Change in non-admitted assets	-	-	-	9,966	9,966
Change in contingency reserve	-	-	-	77,054	77,054
Change in unrealized capital gains, net of tax	-	-	-	(36,594)	(36,594)
Dividend paid	-	-	-	(213,730)	(213,730)
Balance, December 31, 2013	500,000	15,000	574,441	1,496,691	2,086,132
Net income	-	-	-	238,138	238,138
Change in deferred income taxes	-	-	-	(46,869)	(46,869)
Change in non-admitted assets	-	-	-	33,062	33,062
Change in contingency reserve	-	-	-	96,129	96,129
Change in unrealized capital gains, net of tax	-	-	-	3,818	3,818
Dividends paid	-	-	-	(220,000)	(220,000)
Balance, December 31, 2014	500,000	$ 15,000	$ 574,441	$ 1,600,969	$ 2,190,410

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

NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION
STATUTORY-BASIS STATEMENTS OF CASH FLOWS
(Dollars in thousands)

	Years ended December 31, 2014	Years ended December 31, 2013
Cash from operations		
Premiums collected, net of reinsurance	$ 13,209	$ 12,055
Net investment income	138,898	118,577
Miscellaneous income	17,968	7
Total	170,075	130,639
Loss payments	2,990	70,828
Commissions, expenses paid and loss adjustment expenses paid	56,620	49,909
Federal income taxes paid	79,441	108,152
Total	139,051	228,889
Net cash provided (used) by operations	31,024	(98,250)
Cash from investments		
Proceeds from investments sold, matured or repaid:		
Fixed-maturity securities	912,352	1,028,922
Repayment of secured loan to affiliate	-	1,595,620
Miscellaneous proceeds	2	6,708
Total investment proceeds	912,354	2,631,250
Cost of investments acquired:		
Fixed-maturity securities	1,020,147	2,089,485
Miscellaneous applications	11,487	-
Total investments acquired	1,031,634	2,089,485
Net cash (used) provided by investment activities	(119,280)	541,765
Cash from financing and miscellaneous sources		
Securities under agreement to repurchase (parent)	(3,300)	(34,000)
Dividends paid	(220,000)	(213,730)
Other cash used	(2,738)	(1,378)
Net cash used for financing and miscellaneous sources	(226,038)	(249,108)
Net change in cash, cash equivalents and short-term investments	(314,294)	194,407
Cash, cash equivalents and short-term investments - beginning of year	1,044,692	850,285
Cash, cash equivalents and short-term investments - end of year	$ 730,398	$ 1,044,692

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

1. Business Developments and Risks and Uncertainties

National Public Finance Guarantee Corporation ("National" or "the Company") is a wholly owned subsidiary of MBIA Inc. ("the Parent" or "Parent Company") through an intermediary holding company, National Public Finance Guarantee Holdings, Inc. ("National Holdings"). " National Real Estate Holdings of Armonk, LLC ("NREHA") is a wholly-owned subsidiary of National.

Through its reinsurance of United States ("U.S.") public finance financial guarantees from MBIA Insurance Corporation ("MBIA Corp.") and transfers by novation of all policies under a reinsurance agreement with Financial Guaranty Insurance Company ("FGIC"), National's insurance portfolio consists 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. Municipal bonds and privately issued bonds used for the financing of public purpose projects generally are supported by taxes, assessments, user fees or tariffs related to the use of these projects, by lease payments or by other similar types of revenue streams. As of December 31, 2014, National had insured gross par outstanding of $222.3 billion.

In August of 2013, the novation agreement between 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 Corp. 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.

Business Developments

Ratings and New Business Opportunities

National's ability to write new business and compete with other financial guarantors is largely dependent on the financial strength ratings assigned to National by major rating agencies. As of December 31, 2014, National was rated AA+ with a stable outlook by Kroll Bond Rating Agency, AA- with stable outlook by Standard & Poor's Financial Services LLC, and A3 with negative outlook by Moody's Investors Service, Inc.

National seeks to generate shareholder value through appropriate risk adjusted pricing; however, current market conditions and the competitive landscape may limit National's new business opportunities and its abilities to price and underwrite risk with attractive returns. Refer to "Risks and Uncertainties" below for a discussion of business risks related to National's insured portfolio.

Key Lending Agreements

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 MBIA Inc.'s asset/liability products business. As of December 31, 2014, the notional amount utilized under each of these agreements was $443 million and the fair value of collateral pledged by National and MBIA Inc. under these agreements was $458 million and $474 million, respectively. The net average interest rate on these transactions was 0.23% and 0.24% for the years ended December 31, 2014 and 2013, respectively. The New York State Department of Financial Services ("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.

Advances Agreement

MBIA Inc., National, MBIA Corp. and certain other MBIA Inc. subsidiaries are party to an intercompany advances agreement that was established in 2001. This agreement permits MBIA Corp. to make or accept advances from MBIA Inc., National and other MBIA group companies that are party to the agreement at a rate per annum equal to the London Interbank Offered Rate ("LIBOR") plus 0.25%, in the case of advances to or from MBIA Corp. and National, or LIBOR minus 0.10% in the case of advances from any other MBIA group company. Advances may not exceed 3% of either MBIA Corp.'s or National's admitted assets as of the last year end. During the years ended December 31, 2014 and 2013, there were no amounts drawn under this agreement.

Dividend

During the fourth quarters of 2014 and 2013, National declared and paid dividends of $220 million and $214 million, respectively, to its Parent Company.

Other

As of December 31, 2014, National had statutory capital of $3.3 billion. Statutory capital, defined as policyholders' surplus and contingency reserves, is a key measure of an insurance company's financial condition under insurance laws and regulations. Failure to maintain adequate levels of statutory surplus and total statutory capital could lead to intervention by National's insurance regulators in its operations and constitute an event of default under certain of National's contracts, thereby materially and adversely affecting National's financial condition and results of operations.

Risks and Uncertainties

National'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 National to revise its estimates and assumptions or could cause actual results to differ from National's estimates. While National 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. The discussion below highlights the significant risks and uncertainties that could have a material effect on National's financial statements and business objectives in future periods.

National's insured portfolio continued to perform satisfactorily against a backdrop of strengthening domestic economic activity. While this trend will generally benefit tax revenues and fees charged for essential municipal services which secure National's insured bond portfolio, some state and local governments and territory obligors National insures remain under financial and budgetary stress. In addition, a few of these local governments have filed for protection under Chapter 9 of 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 National's insured transactions. National monitors and analyzes these situations and other stressed credits closely, and the overall extent and duration of this stress is uncertain.

2. Summary of Significant Accounting Policies

Basis of Presentation

The statutory financial statements of National are presented on the basis of accounting practices prescribed or permitted by the NYSDFS. The NYSDFS recognizes only statutory accounting practices prescribed or permitted by the State of New York for determining and reporting the financial condition and results of operations of an insurance company, and determining its solvency under the New York Insurance Law ("NYIL"). The National Association of Insurance Commissioners ("NAIC") *Accounting Practices and Procedures Manual* ("NAIC SAP") has been adopted as a component of prescribed or permitted practices by the State of New York. The Superintendent of the NYSDFS has the right to permit other specific practices that deviate from prescribed practices.

Effective January 1, 2010, National was granted a permitted practice by the NYSDFS to reset its unassigned funds (surplus) to zero by netting its negative unassigned surplus of $1.6 billion against $2.2 billion of gross paid-in and contributed surplus as summarized in the table below. Total policyholders' surplus was not impacted by this permitted practice.

in thousands	State of Domicile	**2014**	**2013**
NET INCOME			
Net income, state basis	NY	$ 238,138	$ 255,949
Effect of state prescribed practices	NY	-	-
Effect of state permitted practices	NY	-	-
Net income, NAIC SAP basis	NY	$ 238,138	$ 255,949
SURPLUS			
Policyholders' surplus, state basis	NY	$ 2,190,410	$ 2,086,132
Effect of state prescribed practices	NY	-	-
Effect of state permitted practices			
Gross paid-in and contributed surplus	NY	(1,623,146)	(1,623,146)
Unassigned surplus	NY	1,623,146	1,623,146
Policyholders' surplus, NAIC SAP basis	NY	$ 2,190,410	$ 2,086,132

Use of Estimates in the Preparation of the Financial Statements

The preparation of financial statements in conformity with Statutory Accounting Principles ("SAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. As additional information becomes available or actual amounts become determinable, the recorded estimates are revised and reflected in operating results. Actual results could differ from those estimates.

Cash, Cash Equivalents and Short-Term Investments

Cash and cash equivalents include cash on hand and demand deposits with banks with an original maturity of less than 90 days. Cash equivalents also include bonds and commercial paper with a maturity of less than 90 days at time of purchase. Short-term investments and cash equivalents are stated at amortized cost, net of any unrealized foreign exchange gains and losses, which approximate fair value.

Investments

Bonds with an NAIC designation of 1 or 2 that are not backed by other loans are reported at amortized cost. Amortized cost is calculated using the effective yield method. For bonds purchased at a price below par value, discounts are accreted over the remaining term of the bond. For bonds purchased at a price above par value, which have call features, premiums are amortized to the call date that produces the lowest yield. For premium bonds that do not have call features, such premium is amortized over the remaining term of the bond.

Bonds with an NAIC designation of 3 to 6 that are not backed by other loans are reported at the lower of amortized cost (as described above) or fair value as determined by the NAIC's Securities Valuation Office ("SVO"). In the event the SVO has not determined the fair value of a security, fair value amounts are determined by using independent market sources, when available, and appropriate valuation methodologies when market quotes are not available. In cases where specific market quotes are unavailable, interpreting market data and estimating market values require considerable judgment by management. Accordingly, the estimates presented are not necessarily indicative of the amount National could realize in the market.

Statement of Accounting Principles ("SSAP") No. 43R "Loan-backed and Structured Securities – Revised" establishes principles for investments in loan-backed and structured securities and increased disclosures regarding other-than-temporarily impaired securities. Loan-backed bonds and structured securities with an NAIC designation of 1 or 2 are reported at amortized cost using the effective interest method, including anticipated prepayments at the date of purchase. Changes in the estimated cash flows from the original purchase assumptions are accounted for using the retrospective method.

Loan-backed bonds and structured securities with an NAIC designation of 3 through 6 are reported at the lower of amortized cost or fair value as determined by the SVO. In the event the SVO has not determined the fair value of a security, fair value amounts are determined by using independent market sources, when available, and appropriate valuation methodologies when market quotes are not available. In cases where specific market quotes are unavailable, interpreting market data and estimating market values require considerable judgment by management. Accordingly, the estimates presented are not necessarily indicative of the amount National could realize in the market.

Investment income is recorded as earned. All investment income due and accrued with amounts that are over 90 days past due are recorded as nonadmitted assets. Realized gains and losses on the sale of investments are determined using the first-in, first-out method and are included in the Statement of Income as a separate component of revenues. Unrealized gains and losses from the revaluation of bonds and common stocks not valued at amortized cost are credited or charged to unassigned surplus.

Common stocks are stated at fair value except for investments in stocks of subsidiaries. In accordance with Section 1414 *Valuation of Investments* of the New York Insurance Statutes and SSAP No. 97 "Investments in Subsidiary, Controlled and Affiliated Entities," investments in the stock of subsidiaries and affiliates are valued at their statutory equity basis.

National recorded its investment in its subsidiary, NREHA, within "Other invested assets" on its Balance Sheet. Investments in limited liability companies are reported using an equity method as defined in SSAP No. 97. The change in policyholders' surplus is recorded in unrealized capital gains and losses, which is a component of unassigned surplus.

Investments in Affiliated Entities

National accounts for its investment in affiliated entities as an admitted asset in accordance with Section 1407(a)(4) *Non-reserve and prohibited investments for property/casualty and certain other insurers* of the NYIL. Section 1407(a)(4) provides that an insurer may invest in the obligations of another insurance corporation within the limits prescribed by Section 1408 *Acquisition of insurance company shares; limitations thereon* of the NYIL. Section 1408 provides that an insurer may invest in other insurance companies, including any corporation having a majority of its assets invested in insurance companies.

Other-Than-Temporary Impairments on Investment Securities

National's securities for which fair value is less than amortized cost are reviewed no less than quarterly in order to assess whether such a decline in value is other-than-temporary. This evaluation includes both qualitative and quantitative considerations. In assessing whether a decline in value is other-than-temporary, National considers several factors, including but not limited to (a) the magnitude and duration of the decline, (b) credit indicators and the reasons for the decline, such as general interest rate or credit spread movements, credit rating downgrades, issuer-specific changes in credit spreads, and the financial condition of the issuer, and (c) any guarantees associated with a security such as those provided by financial guarantee insurance companies. Based on this assessment, if National believes that either (a) the investment's fair value will not recover to an amount equal to its amortized cost or (b) National does not have the ability and intent to hold the investment to maturity or until the fair value recovers to an amount at least equal to amortized cost, it will consider the decline in value to be other-than-temporary. If National determines that a decline in the value of an investment is other-than-temporary, the investment is written down to its fair value and a realized loss is recorded in the Statements of Income.

For loan-backed and structured securities, National estimates cash flows expected to be collected over the life of the security. If National determines that if, based on current information and events, there is a decrease in cash flows expected to be collected (that is they will be unable to collect all cash flows expected at acquisition plus any additional cash flows expected to be collected arising from changes in estimates after acquisition) an other-than-temporary impairment ("OTTI") shall be considered to have occurred. For loan-backed securities that management has no intent to sell and believes that it is more likely than not such securities will not be required to be sold prior to recovery, only the credit loss component of the OTTI is recognized as a realized loss, while the rest of the fair value loss is recognized as a reduction to unassigned surplus. If management intends to sell the security or if management believes that it is more likely than not such securities will be required to be sold prior to recovery, the entire amount of the unrealized loss is recognized as a realized loss. These assessments require management to exercise judgment as to whether an investment is impaired based on market conditions and trends and the availability of relevant data. See "Note 5. Fair Value of Financial Instruments" for further information regarding valuation methodologies and related disclosures.

Premium Revenue Recognition

National's premiums written consist of upfront premiums and installment premiums received and accrued for policies issued in current and prior years. Upfront premiums are earned proportionately to the ratio of scheduled periodic maturity of principal and payment of interest ("debt service") to the original total principal and interest insured. Installment premiums are earned on a straight-line basis over each installment period, generally one year or less. Unearned premiums represent the portion of premiums written that is applicable to the unexpired risk of insured obligations. When an insured obligation is retired early, is called by the issuer, or is in substance paid in advance through a refunding accomplished by placing U.S. Government securities in escrow, the remaining unearned premium is earned at that time, since there is no longer risk to National. As the outstanding principal of an installment-based policy is paid down by the issuer of a National-insured obligation, less premium is collected and recognized by National. Additionally, National may receive premiums upon the early termination of installment-based policies, which are earned when received.

Premiums ceded to reinsurers reduce the amount of earned premium National will recognize from its insurance policies. For both upfront and installment policies, ceded premium is recognized in earnings in proportion to and at the same time the related gross premium revenue is recognized.

Expenses incurred in connection with the acquisition of new insurance business, including ceding commissions payable, are charged to operations as incurred. Expenses incurred are reduced for ceding commissions received or receivable, to the extent admissible.

National does not utilize anticipated investment income as a factor in the premium deficiency calculation. National had no premium deficiency as of December 31, 2014 or 2013.

Fees and Expense Reimbursements

National collects insurance related fees for services performed in connection with certain transactions. In addition, National may be entitled to reimbursement of third-party insurance expenses that it incurs in connection with certain transactions. These fees are included as a reduction to "Other underwriting expenses" within the Statements of Income.

Loss and Loss Adjustment Expense ("LAE") Reserves

National's financial guarantee insurance provides an unconditional and irrevocable guarantee of the payment of the principal of, and interest or other amounts owing on, insured obligations when due or, in the event that National has the right, at its discretion, to accelerate insured obligations upon default or otherwise, upon such acceleration by National. Loss and LAE reserves are established by National's Loss Reserve Committee, which consists of members of senior management, and require the use of judgment and estimates with respect to the occurrence, timing and amount of a loss on an insured obligation.

National recognizes loss reserves on a contract-by-contract basis where an insured event has occurred (i.e., a payment default on the insured obligation) or an insured event is expected in the future based upon credit deterioration which has already occurred and has been identified. Case reserves are measured based on the probability-weighted present value of expected net cash inflows and outflows to be paid under the contract, discounted using a rate equal to the yield-to-maturity of National's fixed-income investment portfolio, excluding cash and cash equivalents and other investments not intended to defease long-term liabilities. The loss reserve is subsequently remeasured each reporting period for expected increases or decreases due to changes in the likelihood of default and potential recoveries. Subsequent changes to the measurement of the loss reserves are recognized as losses incurred in the period of change. Measurement and recognition of loss reserves are reported net of any reinsurance. National estimates the likelihood of possible claims payments and possible recoveries using probability-weighted expected cash flows based on information available as of the measurement date, including market information. The methods for making such estimates are continually reviewed and any adjustments are reflected in the period determined. Once a case basis reserve is established for an insured obligation, National continues to record premium revenue to the extent premiums have been or are expected to be collected on that obligation.

National does not establish loss reserves for all payments due under an insured obligation. Case basis reserves cover the estimated amount of principal and interest National expects to pay on its insured obligations and the costs of settlement and other loss mitigation expenses, net of expected recoveries. National recognizes potential salvage and subrogation recoveries on paid losses based on a similar probability-weighted net cash flow projection discounted using the same rate discussed above, as of the measurement date.

When National becomes entitled to potential recoveries which are typically based on either, salvage rights, the rights conferred to National through the transactional documents (inclusive of the insurance agreement), subrogation rights embedded within insurance policies, or the underlying collateral of an insured obligation, it reports this type of salvage and subrogation as a contra-liability within "Loss and LAE reserves" on National's balance sheet. References in the aforementioned and following disclosures to these items should be considered to be salvage and subrogation for purposes of financial reporting on a statutory basis.

A number of variables are taken into account in establishing specific case basis reserves for individual policies. These variables include creditworthiness of the underlying issuer of the insured obligation, whether the obligation is secured or unsecured and the expected recovery rates on the insured obligation, the projected cash flow or market value of any assets that support the insured obligation and the historical and projected loss rates on such assets. Factors that may affect the actual ultimate underwriting losses for any policy include the state of the economy, changes in interest rates, rates of inflation and the salvage values of specific collateral. Management believes that National's reserves are adequate to cover the net cost of claims. However, because the reserves are based on management's judgment and estimates, there can be no assurance that the ultimate liability will not exceed such estimates.

Refer to "Note 9. Loss and Loss Adjustment Expense Reserves" for additional information regarding the Company's loss reserving methodology.

<u>Contingency Reserve</u>

A contingency reserve is established for the protection of all policyholders by direct charges to unassigned surplus and is established by National for past business and new business, as follows:

- For policies in force prior to July 1, 1989, National establishes and maintains a contingency reserve equal to 50% of the cumulative earned premiums on such policies.

- For policies written on or after July 1, 1989, a contingency reserve, which represents the greater of 50% of premiums written or a stated percentage of the principal guaranteed dependent on the category of obligation insured, is established over a 15 to 20 year period. The stated percentage ranges from 0.55% on municipal general obligation bonds to 2.5% on certain industrial development bonds and non-investment grade obligations.

Contingency reserves are established and maintained net of collateral and reinsurance. The reserves may be released in the same manner in which they were established and withdrawals, to the extent there may be excess, may be made with either the prior written approval of the Superintendent of the NYSDFS or upon thirty days prior written notice, depending upon the circumstances specified in *Article 69, Section 6903* of the NYIL. Contingency reserves established for policies which are terminated, matured or net of refundings to the extent that the refunded issue is paid off or secured by obligations, which are directly payable or guaranteed by the U.S. Government, may be released without prior approval or notice. Additionally, as of December 31, 2014 and 2013 contingency reserves have been released upon satisfaction of certain conditions of NYIL. National continually assesses its contingency reserve to determine if amounts are excessive in relation to the outstanding insured obligations and could potentially release additional contingency reserves in the future upon demonstrating to the satisfaction of the NYSDFS that the amounts are excessive.

Securities Purchased Under Agreements to Resell and Securities Sold Under Agreements to Repurchase

Securities purchased under agreements to resell and securities sold under agreements to repurchase are accounted for as collateralized transactions and are recorded at book value. It is National's policy to take possession of securities borrowed or purchased under agreements to resell. Repurchase agreements with third parties are primarily entered into for cash management purposes, to invest or obtain cash on a short-term basis, and are only transacted with high-quality dealer firms. National's investment guidelines require that these repurchase agreements to be fully collateralized, with collateral valued at fair value and additional collateral delivered if there is a shortfall. Cash collateral received is invested in short-term investments and the offsetting collateral liability is recorded on the Balance Sheet.

Income Taxes

National files its U.S. Corporation Income Tax Return as a member of MBIA Inc. consolidated group and participates in the MBIA Inc. tax sharing agreement under which National is allocated its share of the consolidated tax liability or tax benefit as determined under the tax sharing agreement. To the extent that the consolidated tax liability of the Parent Company and its subsidiaries is less than National's tax liability on a separate company basis, the difference would be held in escrow for two years in the event National were to incur a tax loss which could be carried back. Current tax losses not carried back on a separate return basis would be compensated for under the terms of the tax sharing agreement. Intercompany tax balances are settled annually following the Parent Company's filing of its federal income tax return.

The provision for federal income taxes is based on income from operations. Deferred income taxes are provided based on temporary differences between the financial reporting and tax basis of recording assets and liabilities. Changes in net deferred income taxes are recognized as a separate component of unassigned surplus.

Secured Loan with Affiliate

Interest income in 2013 was accrued at the contractual interest rate. Interest payments were deferred and capitalized to the loan balance at the option of MBIA Corp. The balance and accrued interest on the secured loan was repaid in May of 2013.

Recent Accounting Pronouncements

For the years ended December 31, 2014 and 2013, there have not been any recent accounting pronouncements adopted by National.

3. Investments

The Company's investment objective is to optimize long-term returns while emphasizing the preservation of capital through maintenance of high-quality investments with adequate liquidity. The Company's investment policies limit the amount of credit exposure to any one issuer. The fixed-maturity portfolio comprises high quality taxable and tax-exempt investments of diversified maturities.

The following tables set forth the book adjusted/carry value and fair value of the fixed-maturity investments and equity investments included in the investment portfolio of National, as of December 31, 2014 and December 31, 2013. Fair value is based upon valuations adopted and approved by the SVO of the NAIC. If the fair value of a security is not available from the SVO, an independent third-party source is used.

	As of December 31, 2014			
In thousands	Book Adjusted/ Carry Value	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. governments	$ 743,541	$ 5,991	$ (4,245)	$ 745,286
All other governments	754	35	-	790
States, territories and possessions	318,563	5,322	(3,956)	319,929
Political subdivisions of states, territories and possessions	239,467	8,576	(968)	247,075
Special revenue and special assessment obligations	1,516,785	34,654	(10,198)	1,541,241
Industrial and miscellaneous	1,218,440	24,611	(3,481)	1,239,570
Hybrid securities	14,550	1,127	(14)	15,663
Parent, subsidiaries and affiliates	111,406	14,733	-	126,139
Total fixed-maturity investments	4,163,506	95,049	(22,862)	4,235,693
Investments in unaffiliated common stock	105,292	21,908	-	127,200
Total fixed-maturity investments and stock	$ 4,268,798	$ 116,957	$ (22,862)	$ 4,362,893

The table above excludes unrealized losses on NAIC rated 3 through 6 securities that were carried at fair value where the fair value of the securities was lower than amortized cost. The Company has recorded unrealized losses on these securities to bring the book adjusted/ carrying value to fair value. The total fair value and unrealized loss for these securities as of December 31, 2014 was $9.8 million and $1 million, respectively.

	As of December 31, 2013			
In thousands	Book Adjusted/ Carry Value	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. governments	$ 556,880	$ 2,011	$ (16,207)	$ 542,684
States, territories and possessions	343,628	1,211	(19,111)	325,728
Political subdivisions of states, territories and possessions	287,667	3,638	(6,377)	284,928
Special revenue and special assessment obligations	1,726,599	16,531	(53,128)	1,690,002
Industrial and miscellaneous	1,016,796	7,728	(23,240)	1,001,284
Hybrid securities	14,231	698	(176)	14,753
Parent, subsidiaries and affiliates	110,885	2,029	-	112,914
Total fixed-maturity investments	4,056,686	33,846	(118,239)	3,972,293
Investments in unaffiliated common stock	105,292	13,600	-	118,892
Total fixed-maturity investments and stock	$ 4,161,978	$ 47,446	$ (118,239)	$ 4,091,185

The table above excludes unrealized losses on NAIC rated 3 through 6 securities that were carried at fair value where the fair value of the securities was lower than amortized cost. The Company has recorded unrealized losses on these securities to bring the book adjusted/carry value to fair value. The total fair value and unrealized loss for these securities as of December 31, 2013 was $14.3 million and $0.7 million, respectively.

Included in the tables above are fixed-maturity investments carried at book adjusted/carry value of $5.7 million and $5.6 million as of December 31, 2014 and 2013, respectively that were on deposit with various regulatory authorities to comply with insurance laws. The fair value of those fixed-maturity investments was $5.7 million as of December 31, 2014 and 2013.

The following table sets forth the distribution by contractual maturity of National's fixed-maturity investments at book adjusted/carry value and fair value at December 31, 2014. Contractual maturities may differ from expected maturities because borrowers may have the right to call or prepay obligations.

In thousands	Book Adjusted/ Carry Value	Fair Value
Due in one year or less	$ 259,795	$ 260,205
Due after one year through five years	898,113	903,363
Due after five years through ten years	788,173	798,091
Due after ten years through fifteen years	254,075	262,509
Due after fifteen years through twenty years	268,594	289,030
Due after twenty years	491,134	506,740
Mortgage-backed	1,203,622	1,215,755
Total fixed-maturity investments	$ 4,163,506	$ 4,235,693

The following tables set forth the gross unrealized losses of National's fixed-maturity and stock investments as of December 31, 2014 and 2013. The tables have segregated investments that have been in a continuous unrealized loss position for less than twelve months from those that have been in a continuous unrealized loss position for twelve months or longer.

	As of December 31, 2014					
	Less than 12 Months		12 Months or Longer		Total	
In thousands	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. governments	$ -	$ -	$ 263,970	$ (4,246)	$ 263,970	$ (4,246)
States, territories and possessions	4,571	(28)	131,100	(3,928)	135,671	(3,956)
Political subdivisions of states, territories and possessions	-	-	69,593	(968)	69,593	(968)
Special revenue and special assessment obligations	21,731	(248)	493,164	(9,950)	514,895	(10,198)
Industrial and miscellaneous	45,870	(253)	195,776	(3,227)	241,646	(3,480)
Hybrid securities	986	(14)	-	-	986	(14)
Total	$ 73,158	$ (543)	$ 1,153,603	$ (22,319)	$ 1,226,761	$ (22,862)

As of December 31, 2014, National's fixed-maturity and stock investment portfolios had gross unrealized losses of $22.9 million. There were 123 securities that were in an unrealized loss position for a continuous twelve-month period or longer with an aggregate unrealized loss position of $22.3 million. Among the 123 securities, the book value of 12 securities exceeded market value by more than 5%.

	As of December 31, 2013					
	Less than 12 Months		12 Months or Longer		Total	
In thousands	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. governments	$ 349,578	$ (10,052)	$ 68,074	$ (6,155)	$ 417,652	$ (16,207)
States, territories and possessions	254,763	(17,724)	18,955	(1,387)	273,718	(19,111)
Political subdivisions of states, territories and possessions	155,699	(6,051)	8,424	(326)	164,123	(6,377)
Special revenue and special assessment obligations	1,083,139	(48,531)	79,264	(4,597)	1,162,403	(53,128)
Industrial and miscellaneous	465,987	(13,853)	118,188	(9,387)	584,175	(23,240)
Hybrid securities	4,751	(176)	-	-	4,751	(176)
Total	$ 2,313,917	$ (96,387)	$ 292,905	$ (21,852)	$ 2,606,822	$ (118,239)

As of December 31, 2013, National's fixed-maturity and stock investment portfolios had gross unrealized losses of approximately $118 million. There were 36 securities that were in an unrealized loss position for a continuous twelve-month period or longer with an aggregate unrealized loss position of $21.9 million. Among the 36 securities, the book value of 25 securities exceeded market value by more than 5%.

The following tables set forth the gross unrealized losses of the Company's loan-backed and structured securities as of December 31, 2014 and 2013. The tables have segregated loan-backed and structured securities that have been in a continuous unrealized loss position for less than twelve months from those that have been in a continuous unrealized loss position for twelve months or longer.

In thousands	As of December 31, 2014		
The aggregate amount of unrealized losses:			
	Less than 12 Months	$	(157)
	12 Months or Longer	$	(7,021)
The aggregate related fair value of securities with unrealized losses:			
	Less than 12 Months	$	31,837
	12 Months or Longer	$	381,173

In thousands	As of December 31, 2013		
The aggregate amount of unrealized losses:			
	Less than 12 Months	$	(23,207)
	12 Months or Longer	$	(7,450)
The aggregate related fair value of securities with unrealized losses:			
	Less than 12 Months	$	715,391
	12 Months or Longer	$	117,507

National has evaluated whether the unrealized losses in its investment portfolio were other-than-temporary considering the circumstances that gave rise to the unrealized losses, along with National's ability and intent to hold these securities to maturity or until such time as to recover an amount equal to their amortized cost. See "Note 2. Summary of Significant Accounting Policies" for further information regarding the analysis performed in determining if a security is other-than-temporarily impaired.

Based on its evaluation, during 2014, National recognized an OTTI of $205 thousand on one commercial mortgage-backed security ("CMBS"). There was no OTTI recognized during 2013.

4. Investment Income and Gains and Losses

The following table presents National's net investment income for the years ended December 31, 2014 and 2013.

	Years Ended December 31,			
In thousands	**2014**		**2013**	
Fixed-maturity	$	120,553	$	96,531
Interest income on secured loan		-		41,032
Short-term investments		1,768		1,681
Other investments		1,958		643
Gross investment income	$	124,279	$	139,887
Investment expenses		6,464		6,613
Net investment income	$	117,815	$	133,274

Investment income is recorded as earned. All investment income due and accrued with amounts that are over 90 days past due are non-admitted. As of December 31, 2014 and 2013, there were no non-admitted assets for investment income due and accrued.

Net realized gains (losses) from fixed-maturity investment sales are primarily generated as a result of the ongoing management of the Company's investment portfolio. In 2014, net realized gains from the sale of fixed-maturity investments were $19 million compared with net realized gains of $30 million in 2013. The decrease was primarily due to lower gains generated on the sale of National's fixed income investments. The 2013 net realized gains on other investments of $10 million were primarily due to a sale of a common stock investment.

The following table presents net realized gains and losses for the years ended December 31, 2014 and 2013.

	Years Ended December 31,	
In thousands	**2014**	**2013**
Fixed-maturity:		
Gains	$ 20,049	$ 37,279
Losses	(1,293)	(7,746)
Net	18,756	29,533
Other investments:		
Gains	-	9,527
Net	-	9,527
Total net realized gains, before taxes	$ 18,756	$ 39,060

National recognized an OTTI of $205 thousand on one CMBS for the year ended December 31, 2014. There was no OTTI for the year ended December 31, 2013. Refer to "Note 3. Investments" and "Note 2. Summary of Significant Accounting Policies" for further information.

5. Fair Value of Financial Instruments

For financial instruments recorded at their carrying amount, the estimated fair value amounts of financial instruments shown in the following table have been determined by the Company using available market information and appropriate valuation methodologies. In certain instances, considerable judgment may be required to interpret market data in order to develop estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amount the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amount.

For assets and liabilities recorded on the balance sheet at fair value, SSAP No. 100 "Fair Value Measurements" establishes a disclosure hierarchy for inputs used in measuring fair value. Observable inputs are those the Company believes that market participants would use in pricing the asset or liability developed based on market data. Unobservable inputs are those that reflect the Company's beliefs about the assumptions market participants would use in pricing the asset or liability developed based on the best information available. The 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 National can access. Valuations are based on quoted prices that are readily and regularly available in an active market with significant trading volumes.

- 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.

Valuation Techniques

Valuation techniques for financial instruments measured at fair value are described below. These determinations were based on available market information and valuation methodologies. Considerable judgment is required to interpret market data to develop estimates and therefore, estimates may not necessarily be indicative of the amount the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. The Company's assets recorded at fair value have been categorized according to their fair value hierarchy based on the lowest level input that is significant to the fair value measurement in its entirety.

Fixed-maturity securities and Short-term investments - Fixed-maturity securities and short-term investments with an NAIC designation of 1 and 2 are carried at amortized cost while fixed-maturity securities and short-term investments with an NAIC designation of 3 through 6 are carried at the lower of amortized cost or fair value.

Fair value of fixed-maturity securities and short-term investments are generally provided by the NAIC SVO published market prices. If NAIC SVO published market prices are not available, the fair value is determined using an independent third-party pricing service which maximizes observable inputs, including price quotations of recent trades of same or similar securities. When observable price quotations are not available, fair value is determined based on cash flow models with yield curves, bond or single name credit default swap spreads and diversity scores as key inputs. These bonds are generally categorized in Level 2 of the fair value hierarchy; in instances where significant inputs are unobservable, they are categorized in Level 3 of the hierarchy.

Cash and cash equivalents, Accrued investment income, Receivable for securities and Payable for securities - The carrying amounts of these items are a reasonable estimate of their fair value due to the short-term nature and creditworthiness of these instruments.

Common stock - The fair value of common stock is based upon quoted market prices, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Other invested assets - National recorded its investment in its subsidiary, NREHA, within "Other invested assets" on its balance sheet. Investments in limited liability companies are reported using an equity method as defined in SSAP No. 97.

Securities purchased under agreements to resell and Securities sold under agreements to repurchase - The carrying amount of securities purchased under agreements to resell and securities sold under agreements to repurchase approximate their fair value.

Financial Guarantees - The fair value of financial guarantees, net of reinsurance 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 CDS spread and recovery rates 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 National's financial guarantees consists of deferred premium revenue and loss and LAE reserves, net of subrogation recoverable as reported on National's Statutory-Basis Statements of Admitted Assets, Liabilities and Capital and Surplus.

Fair Value Measurements

The following fair value hierarchy tables present information about the Company's assets reported on the balance sheets at fair value on a recurring basis as of December 31, 2014 and 2013. There were no liabilities measured at fair value for the years ended December 31, 2014 and 2013:

	Fair Value Measurements at Reporting Date			
In thousands	**(Level 1)**	**(Level 2)**	**(Level 3)**	**Balance as of December 31, 2014**
Assets at fair value				
Bonds:				
Special revenue and special assessment obligations	$ -	$ 822	$ -	$ 822
Industrial and miscellaneous	-	5,027	2,965	7,992
Hybrid Securities	-	1,003	-	1,003
Total bonds	-	6,852	2,965	9,817
Investment in unaffiliated common stock	-	127,200	-	127,200
Total assets as fair value	$ -	$ 134,052	$ 2,965	$ 137,017

	Fair Value Measurements at Reporting Date			
In thousands	**(Level 1)**	**(Level 2)**	**(Level 3)**	**Balance as of December 31, 2013**
Assets at fair value				
Bonds:				
U.S. Governments	$ -	$ 4,832	$ -	$ 4,832
Special revenue and special assessment obligations	-	955	-	955
Industrial and miscellaneous	-	5,601	2,929	8,530
Total bonds	-	11,388	2,929	14,317
Investment in unaffiliated common stock	-	118,892	-	118,892
Total assets as fair value	$ -	$ 130,280	$ 2,929	$ 133,209

There were no transfers into or out of Levels 1 and 2 during 2014 and 2013.

Level 3 Analysis

Level 3 assets were $3 million as of December 31, 2014 and 2013, and represented approximately 2% of total assets measured at fair value.

The following tables present information about changes in Level 3 assets measured at fair value on a recurring basis for the years ended December 31, 2014 and 2013. Gains and losses reported in these tables may include changes in fair value that are attributable to both observable and unobservable inputs.

Fair Value Measurements in Level 3 of the Fair Value Hierarchy for the Year Ended December 31, 2014

In thousands	Balance at 12/31/2013	Transfers into Level 3	Transfers out of Level 3	Total gains and (losses) included in Net Income	Total gains and (losses) included in Surplus	Purchases	Issuances	Sales	Settlements	Balance at 12/31/2014
Assets:										
Fixed-maturity investments										
Industrial and miscellaneous	$ 2,929	$ 2,436	$ (905)	$ 75	$ (281)	$ -	$ -	$ (1,276)	$ (13)	$ 2,965
Total assets	$ 2,929	$ 2,436	$ (905)	$ 75	$ (281)	$ -	$ -	$ (1,276)	$ (13)	$ 2,965

Fair Value Measurements in Level 3 of the Fair Value Hierarchy for the Year Ended December 31, 2013

In thousands	Balance at 12/31/2012	Transfers into Level 3	Transfers out of Level 3	Total gains and (losses) included in Net Income	Total gains and (losses) included in Surplus	Purchases	Issuances	Sales	Settlements	Balance at 12/31/2013
Assets:										
Fixed-maturity investments										
Industrial and miscellaneous	$ 16,424	$ 2,053	$ (11,553)	$ -	$ 108	$ -	$ -	$ -	$ (4,103)	$ 2,929
Hybrid securities	1,713	-	(1,713)	-	-	-	-	-	-	-
Total assets	$ 18,137	$ 2,053	$ (13,266)	$ -	$ 108	$ -	$ -	$ -	$ (4,103)	$ 2,929

For the year ended December 31, 2014 there were three transfers into Level 3 of $2.4 million and one transfer out of Level 3 of $0.9 million. For the year ended 2013, there were two transfers into Level 3 of $2 million and eight transfers out of Level 3 of $13 million. These transfers into and out of Level 3 were principally for securities where inputs, which are significant to their valuation, became unobservable or observable during the year. All Level 1, 2 and 3 designations are made at the end of each accounting period.

As of December 31, 2014 fixed-maturity securities carried at fair value primarily consist of a portfolio of collateralized debt obligations, corporate obligations and other asset backed securities.

The tables below reflect the fair value and admitted values of all assets and liabilities as of December 31, 2014 and 2013 that are financial instruments excluding those accounted for under the equity method. The fair values are also categorized into Levels 1, 2 and 3 of the fair value hierarchy as described above.

2014
In thousands

Type of Financial Instrument	Level 1	Level 2	Level 3	Fair Value	Admitted Value
Assets:					
Fixed-maturity securities	$ 428,519	$ 3,769,010	$ 38,164	$ 4,235,693	$ 4,163,506
Investment in unaffiliated common stock	-	127,200	-	127,200	127,200
Cash, cash equivalents and short-term investments	102,766	184,432	-	287,198	287,198
Securities purchased under agreements to resell	-	443,200	-	443,200	443,200
Other invested assets	-	11,349	-	11,349	11,176
Receivable for securities	-	21,255	-	21,255	21,255
Accrued investment income	-	27,810	-	27,810	27,810
Receivable from affiliates	-	440	-	440	440
Total assets	$ 531,285	$ 4,584,696	$ 38,164	$ 5,154,145	$ 5,081,785
Liabilities:					
Securities sold under agreements to repurchase	$ -	$ 443,200	$ -	$ 443,200	$ 443,200
Payable for securities	-	39,819	-	39,819	39,819
Payable to affiliates	-	1,959	-	1,959	1,959
Premium tax payable	-	9	-	9	9
Total liabilities	$ -	$ 484,987	$ -	$ 484,987	$ 484,987
Financial Guarantees:					
Net of reinsurance	$ -	$ -	$ 3,014,565	$ 3,014,565	$ 1,362,522

2013
In thousands

Type of Financial Instrument	Level 1	Level 2	Level 3	Fair Value	Admitted Value
Assets:					
Fixed-maturity securities	$ 297,968	$ 3,653,018	$ 21,307	$ 3,972,293	$ 4,056,686
Investment in unaffiliated common stock	-	118,892	-	118,892	118,892
Cash, cash equivalents and short-term investments	390,925	207,267	-	598,192	598,192
Securities purchased under agreements to resell	-	446,500	-	446,500	446,500
Other invested assets	-	9,678	-	9,678	10,345
Receivable for securities	-	612	-	612	612
Accrued investment income	-	29,373	-	29,373	29,373
Receivable from affiliates	-	11,496	-	11,496	11,496
Total assets	$ 688,893	$ 4,476,836	$ 21,307	$ 5,187,036	$ 5,272,096
Liabilities:					
Securities sold under agreements to repurchase	$ -	$ 446,500	$ -	$ 446,500	$ 446,500
Payable for securities	-	29,665	-	29,665	29,665
Payable to affiliates	-	461	-	461	461
Premium tax payable	-	1	-	1	1
Total liabilities	$ -	$ 476,627	$ -	$ 476,627	$ 476,627
Financial Guarantees:					
Net of reinsurance	$ -	$ -	$ 1,599,990	$ 1,599,990	$ 1,591,227

The carrying amounts of certain assets and liabilities were recorded in Level 1 of the fair value hierarchy as of December 31, 2013 and have been revised to reflect the appropriate classification in Level 2 of the fair value hierarchy.

6. Income Taxes

SSAP No. 101 "Income Taxes" provides for an admission calculation of deferred tax assets ("DTAs") specific to financial guarantors which state that if the reporting entity meets the minimum capital and reserve requirements for the state of domicile, they shall use the Realization Threshold Limitation Table when calculating the admission of DTAs. The financial guaranty entity table's threshold limitations are contingent upon the ratio of statutory capital excluding the admitted DTA to the required surplus and contingency reserve (the Aggregate Risk Limit). The Aggregate Risk Limit is the amount of aggregate capital that the NYSDFS requires to be maintained based on the risk characteristic and amount of insurance in force under NYIL.

The components of DTA's and deferred tax liabilities ("DTL's") are as follows:

DTA/DTL Components:

	12/31/2014			12/31/2013			Change		
In thousands	Ordinary	Capital	Total	Ordinary	Capital	Total	Ordinary	Capital	Total
Gross Deferred Tax Assets	$ 451,666	$ 15,404	$ 467,070	$ 500,396	$ 13,142	$ 513,538	$ (48,730)	$ 2,262	$ (46,468)
Statutory Valuation Allowance	-	-	-	-	-	-	-	-	-
Adjusted Gross Deferred Tax Assets	451,666	15,404	467,070	500,396	13,142	513,538	(48,730)	2,262	(46,468)
Gross Deferred Tax Liabilities	(215)	(13,800)	(14,015)	(283)	(10,555)	(10,838)	68	(3,245)	(3,177)
Net dta/(dtl) before admissibility test	451,451	1,604	453,055	500,113	2,587	502,700	(48,662)	(983)	(49,645)
Non-admitted deferred tax asset/(liability)	426,059	1,604	427,663	474,409	2,587	476,996	(48,350)	(983)	(49,333)
Net admitted DTAs	$ 25,392	$ -	$ 25,392	$ 25,704	$ -	$ 25,704	$ (312)	$ -	$ (312)

Admission calculation components:

	12/31/2014			12/31/2013			Change		
In thousands	Ordinary	Capital	Total	Ordinary	Capital	Total	Ordinary	Capital	Total
Admission calculation under 11.a. - 11.c.									
(a) Admitted pursuant to 11.a.	$ 22,367	$ -	$ 22,367	$ 21,984	$ -	$ 21,984	$ 383	$ -	$ 383
(b) Admitted pursuant to 11.b. (lessor of b.i. or b.ii.)	3,025	-	3,025	3,720	-	3,720	(695)	-	(695)
(c) Admitted pursuant to 11.b.i.	N/A	N/A	3,025	N/A	N/A	3,720	N/A	N/A	(695)
(d) Admitted pursuant to 11.b.ii.	N/A	N/A	343,057	N/A	N/A	322,003	N/A	N/A	21,054
(e) Admitted pursuant to 11.c.	215	13,800	14,015	283	10,555	10,838	(68)	3,245	3,177
(f) Total admitted under 11.a., 11.b., and 11.c.	$ 25,607	$ 13,800	$ 39,407	$ 25,987	$ 10,555	$ 36,542	$ (380)	$ 3,245	$ 2,865
(g) Deferred Tax Liabilities	(215)	(13,800)	(14,015)	(283)	(10,555)	(10,838)	68	(3,245)	(3,177)
Net admitted dta/(dtl) under 11.a., 11.b., and 11.c.	$ 25,392	$ -	$ 25,392	$ 25,704	$ -	$ 25,704	$ (312)	$ -	$ (312)
Threshold used in 11.b.									
(i) ExDTA Surplus/Policyholders and Contingency Reserves Ratio	N/A	N/A	267%	N/A	N/A	216%	N/A	N/A	51%

The Company has not implemented any tax planning strategies that would affect adjusted gross and net admitted deferred tax assets.

The Company has not entered into tax planning strategies involving reinsurance.

The Company has no unrecognized DTL for amounts described in SSAP No. 101, paragraph 7(d) and paragraph 31 of accounting principles for income taxes.

Current Tax and Change in Deferred Tax:

Current income tax incurred consists of the following major components:

In thousands	12/31/2014	12/31/2013
Current income taxes incurred		
Current federal income tax expense	$ 87,641	$ 94,426
Foreign Taxes	-	-
Subtotal	$ 87,641	$ 94,426
Tax on capital gains/(losses)	6,636	10,336
Other, including prior year (under)/over accrual	482	41,632
Federal and foreign income taxes incurred	$ 94,759	$ 146,394

The Company does not expect a significant increase in tax contingencies within the twelve month period following the balance sheet date. As of December 31, 2014, the Company does not have any significant uncertain tax positions.

The tax effects of temporary difference that give rise to significant portions of DTAs and DTLs are as follows:

DTAs Resulting from Book/Tax Differences in			
(in thousands)	**12/31/2014**	**12/31/2013**	**Change**
(a) Ordinary			
Contingency Reserve	$ 376,564	$ 410,209	$ (33,645)
Unearned Premium Reserve	48,128	58,729	(10,601)
Salvage and Subrogation	10,011	21,231	(11,220)
Building Impairment	8,412	7,286	1,126
Non-admitted Assets	6,160	464	5,696
Other	2,391	2,477	(86)
Gross Deferred Tax Assets - Ordinary	451,666	500,396	(48,730)
(b) Statutory Valuation Allowance (-)	-	-	-
(c) Non-admitted deferred tax assets (-)	(426,059)	(474,409)	48,350
(d) Net deferred tax asset/(liability)	$ 25,607	$ 25,987	$ (380)
(e) Capital			
Investments	12,352	10,162	2,190
Capital Loss Carryovers & OTTI	72	-	72
Land Impairment	2,980	2,980	-
Gross Deferred Tax Assets - Capital	15,404	13,142	2,262
(f) Statutory Valuation Allowance - Capital (-)	-	-	-
(g) Non-admitted deferred tax assets - Capital (-)	(1,604)	(2,587)	983
(h) Admitted Deferred Tax Assets - Capital	13,800	10,555	3,245
(i) Total Admitted Deferred Tax Assets	$ 39,407	$ 36,542	$ 2,865

DTLs Resulting from Book/Tax Differences in			
(in thousands)	**12/31/2014**	**12/31/2013**	**Change**
(a) Ordinary			
Salvage and Subrogation - 481(a) Adjustment	$ (189)	$ (283)	$ 94
Other	(26)	-	(26)
Ordinary Deferred Tax Liabilities	(215)	(283)	68
(b) Capital			
Investments	(6,495)	(6,027)	(468)
Tax effect of unrealized gains	(7,305)	(4,528)	(2,777)
Other	-	-	-
Capital Deferred Tax Liabilities	(13,800)	(10,555)	(3,245)
(c) Deferred Tax Liabilities	$ (14,015)	$ (10,838)	$ (3,177)
Net Deferred Tax Assets/(Liabilities)	**$ 25,392**	**$ 25,704**	**$ (312)**

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

In thousands	12/31/2014	12/31/2013	Change
Total deferred tax assets	$ 467,070	$ 513,538	$ (46,468)
Total deferred tax liabilities	(14,015)	(10,838)	(3,177)
Net deferred tax asset (liability)	$ 453,055	$ 502,700	(49,645)
Tax effect of unrealized gains/(losses)			2,777
Change in net deferred income tax [(expense)/benefit)]			$ (46,868)

Reconciliation of federal income tax rate to actual effective tax rate:

The provision for federal income taxes incurred is different from that which would be obtained by applying the statutory federal income tax rate to income before income taxes. The significant items causing this difference are as follows:

In thousands	Tax Effect	Effective Tax Rate
Income before taxes	$ 116,514	35%
National Real Estate Pre-tax	(489)	0%
Tax Exempt Interest (Net of Proration)	(2,477)	-1%
Change in non-admitted assets	(5,695)	-2%
Change in Contingency Reserve	33,645	10%
Other items	129	0%
Total statutory income taxes	$ 141,627	43%
Federal income tax incurred	94,759	28%
Change in net deferred income tax	46,868	14%
Total statutory income taxes	$ 141,627	43%

Carryforwards, recoverable taxes, and IRC § 6603 deposits:

At December 31, 2014, the Company did not have any net operating loss, capital loss, or minimum tax carry forwards.

National does not have any deposits admitted under Section 6603 of the Internal Revenue Code.

The taxes available for recoupment in the event of future net losses are as follows:

In thousands

Year	Ordinary	Capital	Total
2012	$ N/A	$ 40,277	$ 40,277
2013	94,576	10,668	105,244
2014	87,641	6,636	94,277
Total	$ 182,217	$ 57,581	$ 239,798

As of December 31, 2014, the Company's federal income tax return was consolidated with the following entities:

MBIA, Inc.
Capmac Holdings, Inc.
Cutwater Asset Management Corporation
Cutwater Investors Service Corporation
Cutwater Colorado Investor Services Corporation
MBIA Capital Corporation

MBIA Insurance Corporation
MBIA Investment Management Corporation
Municipal Issuers Service Corporation
National Public Finance Guarantee Corporation
National Public Finance Guarantee Holdings, Inc.
MBIA Services Corporation

National is included in the consolidated tax return of MBIA Inc. its Parent Company. The method of allocation between the companies is subject to written agreement, and is approved by the members of the consolidated group. National is included in the consolidated tax return of MBIA Inc. its Parent Company. The method of allocation between the companies is subject to written agreement, and is approved by the members of the consolidated group. The method of allocation between the members is generally based upon separate-company calculations as if each member filed a separate tax return.

7. Reconciliation of Statutory Accounting to GAAP-Basis Accounting

The accompanying statutory-basis financial statements have been prepared in conformity with NAIC SAP, which differs in some respects from accounting principles generally accepted in the United States of America ("GAAP"). The more significant of these differences are as follows:

- upfront premiums are earned on a SAP basis proportionate to the scheduled periodic maturity of principal and payment of interest ("debt service") to the original total principal and interest insured. Additionally, under SAP, installment premiums are earned on a straight-line basis over each installment period generally one year or less. Under GAAP, National recognizes and measures premium revenue over the period of the contract in proportion to the amount of insurance protection provided. Upfront and installment premium revenue is measured by applying a constant rate to the insured principal amount outstanding in a given period to recognize a proportionate share of the premium received or expected to be received on a financial guarantee insurance contract. Additionally, under GAAP, installment premiums receivable are recorded at the present value of the premiums due or expected to be collected over the period of the insurance contract using a discount rate which reflects the risk-free rate at the inception of the contract;

- under SAP, acquisition costs, (including ceding commission expense or income) are charged to operations as incurred rather than GAAP's requirement to defer and amortize the costs as the related premiums are earned;

- a contingency reserve is computed on the basis of statutory requirements and is not permitted under GAAP;

- loss reserves are reported net of insurance loss recoverables and are discounted using a rate equal to the yield-to-maturity of National's fixed-income portfolio, excluding cash and cash equivalents and other investments not intended to defease long-term liabilities. Under GAAP, loss reserves are discounted using a risk-free rate as of the measurement date and are reported net of the unearned premium revenue and gross of insurance recoverables which are reported as an asset;

- salvage and subrogation generally are recorded as a reduction to loss and LAE reserves for GAAP and statutory reporting. In certain instances under GAAP, the Company records salvage and subrogation, including insurance loss recoverables, as an asset. This would occur, for example, when the Company becomes entitled to the underlying collateral of an insured credit under salvage and subrogation rights as a result of a claim payment and the recovery of such salvage is reasonable and estimable;

- certain compensation, which may be in the form of fixed-maturity investments or other assets under SAP are recorded as a reduction in loss and LAE reserves; however under GAAP, compensation for claim payments are recorded based on where those types of assets are reflected on the balance sheet;

- assets and liabilities relating to reinsurance are reported on a net basis. Therefore, incurred losses and LAE are reported net of reinsurance recoverables and deferred premiums are reported net of prepaid reinsurance premium. Under GAAP, these reinsurance balances are required to be shown on a gross basis as an asset;

- certain assets, which consist primarily of deferred tax assets, leasehold improvements, furniture and equipment and prepaid expenses, described as "non-admitted," are excluded from the balance sheet and are charged directly to unassigned surplus under SAP. There were non-admitted assets of $445 million and $478 million at December 31, 2014 and 2013, respectively. Under GAAP, these amounts are typically reflected as assets;

- changes in net deferred income taxes are recognized as a separate component of gains and losses in surplus. Under GAAP, changes in National's net deferred income tax balances are either recognized as a component of net income or other comprehensive income depending on how the underlying pre-tax impact is reflected. Under SAP, the calculation of the valuation allowance on deferred tax assets is performed on a separate company basis, under GAAP a consolidated analysis is permitted;

- investments in bonds are generally carried at amortized cost under SAP. Accordingly, unrealized changes in fair value are not reflected in the statutory-based statements of income and changes in capital and surplus or the statutory statements of admitted assets, liabilities and capital and surplus. Bonds not qualified to be carried at amortized cost are carried at fair value as required by the NAIC with the differences between these values recorded directly to unassigned surplus net of adjustment for deferred federal income taxes, rather than recording the difference in unrealized gains and losses through shareholders' equity; unrealized gains and losses on common stocks are recorded directly to unassigned surplus net of an adjustment for deferred federal income taxes. Investments in subsidiaries and affiliates are valued pursuant to Section 1414 *Valuation of Investments* of the New York Insurance Statues and SSAP No. 97.

- under SAP, upon the transformation of National, investments were transferred from MBIA Corp. to National at fair market value, under GAAP these investments were transferred at book value;

- the statements of cash flows reconcile to cash and cash equivalents under GAAP rather than cash, cash equivalents, short-term investments and securities purchased under agreements to resell (parent). In addition, under SAP, cash flows from operations are reported consistent with the statement of income; and

- subsidiary financial data is not consolidated and the results of operations of subsidiary companies are charged or credited directly to surplus as part of unrealized capital gains and losses. Under GAAP, subsidiaries are consolidated.

The following is a reconciliation of statutory policyholders' surplus to shareholders' equity on a GAAP-basis for National:

	As of December 31,	
In thousands	**2014**	**2013**
Statutory policyholders' surplus	$ 2,190,410	$ 2,086,132
Premium revenue recognition	319,138	354,308
Deferral of acquisition costs	267,317	325,697
Investments including unrealized gains (losses)	128,829	13,196
Contingency reserve	1,075,897	1,172,026
Loss reserves	(53,260)	(159,522)
Deferred income taxes, net	(605,030)	(597,784)
Derivative assets and liabilities	(3,290)	(4,311)
Non-admitted assets and other items	440,117	492,879
GAAP-basis shareholders' equity	$ 3,760,128	$ 3,682,621

The following is a reconciliation of statutory net income to net income presented on a GAAP-basis for National:

	Years Ended December 31,	
In thousands	**2014**	**2013**
Statutory net income	$ 238,138	$ 255,949
Premium revenue recognition	(35,170)	(12,426)
Amortization of acquisition costs	(60,192)	(77,946)
Investments income including realized gains (losses)	(9,530)	(30,265)
Ceding commission expense	1,481	2,638
Losses incurred	98,099	(36,343)
Current income taxes	(18,303)	64,221
Other	2,631	(967)
GAAP-basis net income	$ 217,154	$ 164,861

8. Capital and Surplus and Dividend Restrictions

National is subject to insurance regulations and supervision of the State of New York (its state of incorporation) and all U.S. and non-U.S. jurisdictions in which it is licensed to conduct insurance business. The extent of insurance regulation and supervision varies by jurisdiction, but New York and most other jurisdictions have laws and regulations prescribing minimum standards of solvency and business conduct, which must be maintained by insurance companies. Among other things, these laws prescribe permitted classes and concentrations of investments and limit both the aggregate and individual securities risks that National may insure on a net basis based on the type of obligations insured. In addition, some insurance laws and regulations require the approval or filing of policy forms and rates. National is required to file detailed annual financial statements with the NYSDFS and similar supervisory agencies in other jurisdictions in which it is licensed. The operations and accounts of National are subject to examination by regulatory agencies at regular intervals.

As of December 31, 2014, National had 500,000 common shares authorized, issued and outstanding, with a par value of $30 per share.

National had no preferred stock outstanding as of December 31, 2014.

The 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 (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.

National had a positive earned surplus as of December 31, 2014, which provided National with dividend capacity. 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 Corp. 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. Following notice to the NYSDFS, National declared and paid a dividend of $220 million to its Parent Company in the fourth quarter of 2014.

As a result of the establishment of National, National exceeded as of the closing date certain single and aggregate risk limits under the NYIL. National obtained waivers from the NYSDFS of such limits. In connection with the waivers, National submitted a plan to the NYSDFS to achieve compliance with the applicable regulatory limits. Under the plan, National agreed not to write new financial guarantee insurance for certain issuers until it was in compliance with their single risk limits and agreed to take commercially reasonable steps, including considering reinsurance, the addition of capital and other risk mitigation strategies, in order to comply with the regulatory single and aggregate risk limits. As a condition to granting the waiver, the NYSDFS required that, in addition to complying with these plans, upon written notice from the NYSDFS, National would cease writing new financial guarantee insurance if it were not in compliance with the risk limitation requirements by December 31, 2009. National came into compliance with its aggregate risk limits in 2011 and has a de minimis number of single risk limits overages remaining.

National has no restrictions on unassigned surplus as of December 31, 2014 other than those mentioned above. National owns no common stock in affiliates or for special purposes as of December 31, 2014. National has not undergone a reorganization or quasi-reorganization during 2014.

The portion of unassigned funds (surplus) represented by cumulative net unrealized capital gains and losses is a net unrealized loss of $20.3 million. The deferred taxes generated by cumulative net unrealized capital gains and losses were $7.3 million. Additionally, the portion of unassigned funds (surplus) represented by non-admitted assets is $445 million.

9. Loss and Loss Adjustment Expense Reserves

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. National 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.

Certain local governments remain under financial and budgetary stress and a few 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 National’s insured transactions. National monitors and analyzes these situations closely; however, the overall extent and duration of such events are uncertain and the filing for protection under the United States Bankruptcy Code or entering state statutory proceedings does not result in a default or indicate that an ultimate loss will occur.

As of December 31, 2014, National had $98.9 billion of gross par outstanding on general obligations, of which $152 million was reflected on National’s Classified List. Capital appreciation bonds are reported at the par amount at the time of issuance of the insurance policy.

Total net loss and LAE was $88 million for the year ended December 31, 2014 compared with $69 million for the year ended December 31, 2013. For the year ended December 31, 2014, losses and LAE incurred related to reserves for Puerto Rico exposures and a gaming transaction, offset by decreases in reserves for certain general obligation bonds. For the year ended December 31, 2013, losses and LAE incurred related to general obligation bonds. Total loss and LAE reserves were in a contra-liability position of $13 million and $87 million as of December 31, 2014 and 2013, respectively.

National establishes new case basis reserves in accordance with the policy described in “Note 2. Summary of Significant Accounting Policies.”

National’s Portfolio Surveillance Division (“PSD”) monitors National’s outstanding insured obligations with the objective of minimizing losses. PSD meets this objective by identifying issuers that, because of deterioration in credit quality or changes in the economic, regulatory or political environment, are at a heightened risk of defaulting on debt service of obligations insured by National. In such cases, PSD works with the issuer, trustee, bond counsel, servicer, underwriter and other interested parties in an attempt to alleviate or remedy the problem and avoid defaults on debt service payments. PSD works closely with National’s Risk Management personnel and the applicable business unit to analyze insured obligation performance and credit risk parameters, both before and after an obligation is insured.

Once an obligation is insured, National typically requires the issuer, servicer (if applicable) and the trustee to furnish periodic financial and asset-related information, including audited financial statements, to PSD for review. PSD also monitors publicly available information related to insured obligations. Potential problems uncovered through this review such as poor financial results, low fund balances, covenant or trigger violations and trustee or servicer problems or other events that could have an adverse impact on the insured obligation, could result in an immediate surveillance review and an evaluation of possible remedial actions. PSD also monitors and evaluates the impact on issuers of general economic conditions, current and proposed legislation and regulations, as well as state and municipal finances and budget developments.

The frequency and extent of PSD's monitoring is based on the criteria and categories described below. Insured obligations that are judged to merit more frequent and extensive monitoring or remediation activities due to a deterioration in the underlying credit quality of the insured obligation or the occurrence of adverse events related to the underlying credit of the issuer are assigned to a surveillance category ("Caution List-Low," "Caution List-Medium," "Caution List-High," or "Classified List") depending on the extent of credit deterioration or the nature of the adverse events. PSD monitors insured obligations assigned to a surveillance category more frequently and, if needed, develops a remediation plan to address any credit deterioration.

National does not establish any case basis reserves for insured obligations that are assigned to "Caution List-Low," "Caution List-Medium," or "Caution List-High." However, LAE reserves are established for any expense that has been incurred, but not yet paid. In the event National expects to pay a claim with respect to an insured transaction, it places the insured transaction on its "Classified List" and establishes a case basis reserve. The following provides a description of each surveillance category:

> "Caution List – Low" - Includes issuers where debt service protection is adequate under current and anticipated circumstances. However, debt service protection and other measures of credit support and stability may have declined since the transaction was underwritten and the issuer is less able to withstand further adverse events. Transactions in this category generally require more frequent monitoring than transactions that do not appear within a surveillance category. PSD subjects issuers in this category to heightened scrutiny.

> "Caution List – Medium" - Includes issuers where debt service protection is adequate under current and anticipated circumstances, although adverse trends have developed and are more pronounced than for "Caution List – Low." Issuers in this category may have breached one or more covenants or triggers. These issuers are more closely monitored by PSD but generally take remedial action on their own.

> "Caution List – High" - Includes issuers where more proactive remedial action is needed but where no defaults on debt service payments are expected. Issuers in this category exhibit more significant weaknesses, such as low debt service coverage, reduced or insufficient collateral protection or inadequate liquidity, which could lead to debt service defaults in the future. Issuers in this category may have breached one or more covenants or triggers and have not taken conclusive remedial action. Therefore, PSD adopts a remediation plan and takes more proactive remedial actions.

> "Classified List" - Includes all insured obligations where National has paid a claim or where a claim payment is expected. It also includes insured obligations where a significant LAE payment has been made, or is expected to be made, to mitigate a claim payment. This may include property improvements, bond purchases and commutation payments. Generally, PSD is actively remediating these credits where possible, including restructurings through legal proceedings, usually with the assistance of specialist counsel and advisors.

Discount Rate

Loss reserves are discounted on a non-tabular basis by applying a discount rate equal to the yield-to-maturity of National's fixed-income investment portfolio, excluding cash, cash equivalents and other investments not intended to defease long-term liabilities. LAE reserves are reported net of reinsurance and are not discounted. The discount rates used at December 31, 2014 and 2013 were 2.90% and 3.14%, respectively. The amount of non-tabular discount as of December 31, 2014 was a negative $283 million compared with a negative $75 million as of December 31, 2013.

Loss and LAE Activity

The following tables provide information about the financial guarantees and related claim liability included in each of National's surveillance categories as of December 31, 2014 and 2013:

	Surveillance Categories - 2014				
$ in millions	**Caution List Low**	**Caution List Medium**	**Caution List High**	**Classified List**	**Total**
Number of policies	30	92	3	43	168
Number of issues (1)	12	2	2	10	26
Remaining weighted average contract period (in years)	6.9	17.0	10.6	8.9	10.6
Gross insured contractual payments outstanding(2):					
Principal	$ 790	$ 918	$ 118	$ 1,624	$ 3,450
Interest	314	773	64	820	1,971
Total	$ 1,104	$ 1,691	$ 182	$ 2,444	$ 5,421
Gross claim liability	$ -	$ -	$ -	$ 80	$ 80
Less:					
Gross potential recoveries	-	-	-	376	376
Discount, net (3)	-	-	-	(283)	(283)
Net claim liability (recoverable)	$ -	$ -	$ -	$ (13)	$ (13)
Net unearned premium reserve	$ 6	$ 20	$ 7	$ 25	$ 58
Reinsurance recoverable	$ -	$ -	$ -	$ -	$ -

(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 National.
(3) - Represents discount related to Gross Claim Liability and Gross Potential Recoveries.

	Surveillance Categories - 2013				
$ in millions	**Caution List Low**	**Caution List Medium**	**Caution List High**	**Classified List**	**Total**
Number of policies	64	2	5	35	106
Number of issues (1)	14	2	4	13	33
Remaining weighted average contract period (in years)	12.9	3.0	11.5	14.4	13.2
Gross insured contractual payments outstanding(2):					
Principal	$ 3,176	$ 7	$ 40	$ 695	$ 3,918
Interest	2,726	2	25	943	3,696
Total	$ 5,902	$ 9	$ 65	$ 1,638	$ 7,614
Gross claim liability	$ -	$ -	$ -	$ 193	$ 193
Less:					
Gross potential recoveries	-	-	-	355	355
Discount, net (3)	-	-	-	(75)	(75)
Net claim liability (recoverable)	$ -	$ -	$ -	$ (87)	$ (87)
Net unearned premium reserve	$ 34	$ 0	$ 0	$ 21	$ 55
Reinsurance recoverable	$ -	$ -	$ -	$ -	$ -

(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 National.
(3) - Represents discount related to Gross Claim Liability and Gross Potential Recoveries.

A summary of the components of the liability for loss and LAE reserves are shown in the following table as of December 31, 2014 and 2013:

In thousands	As of December 31, 2014	As of December 31, 2013
Gross loss and LAE reserves, January 1	$ (86,739)	$ (109,044)
Less: Reinsurance recoverable	-	-
Net loss and LAE reserves, January 1	(86,739)	(109,044)
Plus: Incurred losses and LAE related to:		
Current year	65,837	62,645
Prior years	22,369	6,016
Total incurred losses and LAE	88,206	68,661
Less: Paid losses and LAE related to:		
Current year	1,968	6,116
Prior years	12,039	40,240
Total paid losses and LAE	14,007	46,356
Net loss and LAE reserves, December 31	(12,540)	(86,739)
Add: Reinsurance recoverable	-	-
Gross loss and LAE reserves, December 31	$ (12,540)	$ (86,739)

The following tables present changes in National's loss and LAE reserve as of December 31, 2014 and 2013. Changes in the loss reserve attributable to the accretion of the claim liability discount, changes in discount rate, changes in the timing and amounts of estimated payments and recoveries and changes in assumptions are recorded in "Losses incurred" in National's Statements of Income. LAE reserves are reported net of reinsurance and are not discounted. Changes in LAE reserves are recorded in "Loss adjustment expenses incurred" in National's Statements of Income. As of December 31, 2014 and 2013, the rates used to discount the claim liability were 2.90% and 3.14%, respectively.

In millions

Loss and LAE Reserve as of December 31, 2013	Loss Payments	Accretion of Claim Liability Discount	Changes in Discount Rate	Changes in Assumptions	Changes in LAE Reserves	Other (1)	Reinsurance	Loss and LAE Reserve as of December 31, 2014
$ (87)	$ (3)	$ (3)	$ (21)	$ 96	$ 1	$ 4	$ 0	$ (13)

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

In millions

Loss and LAE Reserve as of December 31, 2012	Loss Payments	Accretion of Claim Liability Discount	Changes in Discount Rate	Changes in Assumptions	Changes in LAE Reserves	Other (1)	Reinsurance	Loss and LAE Reserve as of December 31, 2013
$ (109)	$ (71)	$ (2)	$ (3)	$ 60	$ 54	$ (16)	$ -	$ (87)

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

10. Insurance in Force

National's insurance in force represents the aggregate amount of the insured principal of, and interest or other amounts owing on insured obligations. National's ultimate exposure to credit loss in the event of nonperformance by the issuer of the insured obligation is represented by the insurance in force in the tables that follow. Substantially all insurance in force is from the quota share reinsurance agreement with MBIA Corp. and the novation of the FGIC U.S. public finance portfolio to 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. 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. The creditworthiness of each issuer of an insured obligation is evaluated prior to the issuance of insurance, and each insured obligation must comply with National's underwriting guidelines. Further, the payments to be made by the issuer on 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.

National maintains underwriting guidelines based on those aspects of credit quality that it deems important for each category of obligation considered for insurance.

As of December 31, 2014, insurance in force had an expected maturity range of 1-42 years. The distribution of insurance in force by geographic location as of December 31, 2014 and 2013 respectively, is presented in the following table:

	As of December 31,			
In billions	2014		2013	
Geographic Location	Insurance in Force	% of Insurance in Force	Insurance in Force	% of Insurance in Force
California	$ 73.5	20.3%	$ 88.4	19.8%
New York	29.2	8.1%	37.4	8.4%
Illinois	25.4	7.0%	29.6	6.6%
Florida	24.1	6.7%	29.2	6.6%
Texas	21.1	5.8%	28.0	6.3%
New Jersey	16.8	4.7%	20.2	4.5%
Michigan	12.3	3.4%	15.3	3.4%
Puerto Rico	10.1	2.8%	10.9	2.5%
Pennsylvania	9.3	2.6%	11.8	2.6%
Washington	9.1	2.5%	11.5	2.6%
Subtotal	230.9	63.9%	282.3	63.3%
Nationally diversified	7.3	2.0%	7.9	1.8%
Other states	123.4	34.1%	155.5	34.9%
Total	$ 361.6	100.0%	$ 445.7	100.0%

The insurance in force by type of bond is presented in the following table:

In billions	As of December 31, 2014			As of December 31, 2013		
Bond Type						
General obligations	$	122.8	34.0%	$	153.5	34.4%
General obligations - lease		27.9	7.7%		34.1	7.7%
Municipal utilities		60.5	16.7%		78.0	17.5%
Tax-Backed		53.6	14.8%		66.1	14.8%
Transportation		38.4	10.6%		46.2	10.4%
Higher education		19.5	5.4%		24.1	5.4%
Health care		8.4	2.3%		9.5	2.1%
Military housing		18.4	5.1%		19.2	4.3%
Investor-owned utilities (1)		6.1	1.7%		7.2	1.6%
Municipal housing		3.6	1.0%		4.8	1.1%
Other (2)		2.4	0.7%		3.0	0.7%
Total	$	361.6	100.0%	$	445.7	100.0%

(1) - Includes investor owned utilities, industrial development and pollution control revenue bonds.
(2) - Includes student loans, certain non-profit enterprises and stadium related financing.

Ceded Exposure

Reinsurance enables National 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 National under rating agency models and the overall value of the reinsurance to National is reduced. National generally retains the right to reassume the business ceded to reinsurers under certain circumstances, including a reinsurer's rating downgrade below specified thresholds.

The aggregate amount of insurance in force ceded by National to reinsurers under reinsurance agreements was $7.1 billion and $7.5 billion as of December 31, 2014 and 2013, respectively. Under National's reinsurance agreement with MBIA Corp., if a reinsurer of MBIA Corp. is unable to pay claims ceded by MBIA Corp., National will assume liability for such ceded claim payments. As of December 31, 2014, the total amount of insurance in force for which National would be liable in the event that the reinsurers of MBIA Corp. were unable to meet their obligations is $2.4 billion.

National 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 December 31, 2014, the total amount available under these letters of credit and trust arrangements was $27 million.

Premium Summary

The components of net premiums written and earned, including premiums assumed from and ceded to other insurers and reinsurers are set forth in the following table:

	Years Ended December 31,			
	2014		2013	
In thousands	Written	Earned	Written	Earned
Direct	$ 6,476	$ 84,011	$ 1	$ 36,724
Assumed	6,733	232,416	12,054	338,086
Gross	13,209	316,427	12,055	374,810
Ceded	(0)	(0)	(0)	(1)
Net	$ 13,209	$ 316,427	$ 12,055	$ 374,809

Premiums written for the year ended December 31, 2014 were amounts related to new policy issuance and amounts assumed from MBIA Corp. Premiums written for the year ended December 31, 2013 were primarily amounts assumed from MBIA Corp.

Ceding commissions received from reinsurers, before deferrals and net of returned ceding commissions, were an expense of $1 million and $3 million in 2014 and 2013, respectively.

The maximum amount of return commission, which would have been due reinsurers if all reinsurance contracts were canceled with the return of the unearned premium reserve, would be income of $225 million and $274 million as of December 31, 2014 and 2013, respectively. The direct unearned premium reserve at December 31, 2014 and 2013 was $354 million and $432 million, respectively.

11. Information Concerning Parent, Subsidiary and Affiliates

National is a wholly owned subsidiary of National Holdings, which is domiciled in the State of Delaware. All outstanding common shares of National Holdings are owned by its parent company, MBIA Inc., a holding company domiciled in the State of Connecticut. During the fourth quarters of 2014 and 2013, National declared and paid dividends of $220 million and $214 million, respectively, to its Parent Company National owns no shares directly or indirectly of an upstream intermediate entity or its Parent Company. Additionally, National does not have an investment in a foreign subsidiary. In 2014, 51% of National’s written premiums arise from the quota share reinsurance agreement with MBIA Corp.

On February 2, 2010, National established NREHA and on March 1, 2010 contributed certain real estate for purposes of conducting National’s business and leasing to certain affiliates. In 2014 and 2013, NREHA recorded impairment charges of $3 million and $29 million, respectively, on its Armonk, New York facility. The carrying amount of the facility was adjusted to its fair market value, which was estimated based on an independent third-party appraisal. National recorded its investment in NREHA using an equity method as described in “Note 2. Summary of Significant Accounting Policies” and as such the impairment charge is reported within “Other invested assets” on National’s statement of admitted assets, liabilities and capital and surplus for the years ended December 31, 2014 and 2013. In the fourth quarter of 2013, National approved and initiated a plan to actively market the Armonk, New York facility for sale.

MBIA Services Corporation (“MSC”) (formerly known as Optinuity Alliance Resources), created in the first quarter of 2010, provides support services such as management, legal, accounting, treasury and information technology, among others, to MBIA Inc. and other subsidiaries including National on a fee-for-service basis. The service fees charged to National by MSC and other affiliates were $19 million and $18 million, respectively, for the years ended December 31, 2014 and 2013.

National is a party to the MBIA Tax Sharing Agreement. National made several tax payments to MBIA Inc. in 2014, totaling $79 million. For further details refer to “Note 6. Income Taxes”.

National’s investment portfolio is managed by Cutwater Investors Services Corp. (“Cutwater-CISC”), which in 2014 was a wholly-owned subsidiary of MBIA Inc. Cutwater-CISC, provides fixed-income investment management services for MBIA Inc. and its affiliates, as well as third-party institutional clients. For the years ended December 31, 2014 and 2013, Cutwater-CISC charged fees of $6 million and $7 million, respectively, to National based on the size of its investment portfolio. During the fourth quarter of 2014, MBIA Inc. entered into an agreement to sell Cutwater-CISC to a subsidiary of The Bank of New York Mellon Corporation. This transaction was effective January 1, 2015. In connection with the sale, MBIA Inc. and its affiliates entered into an agreement for Cutwater to manage its proprietary investment assets for the next several years.

In the first quarter of 2009, National entered into an agreement with MBIA Inc. whereby National held securities under agreements to resell and under an agreement to repurchase $443 million and $447 million as of December 31, 2014 and 2013, respectively. These agreements reset on a quarterly basis. The interest income and expense related to these agreements were $2 million and $1 million, respectively, for the year ended December 31, 2014 and $3 million and $2 million, respectively, for the year ended December 31, 2013.

As of December 31, 2014 and 2013, there were $0.4 million and $10 million, respectively, of receivables from affiliates included in other assets. As of December 31, 2014 and 2013, there was $0.3 million and $0.5 million, respectively, of payables to MBIA Inc. included in other liabilities. The terms of the settlement agreement require that these amounts be settled within 90 days.

National had no loans outstanding to any executive officers or directors in 2014 and 2013.

12. Retirement Plans and Deferred Compensation

National participates in its parent company's pension plan, which covers substantially all employees. The pension plan is a qualified non-contributory defined contribution plan to which National contributes 10% of each eligible employee's annual compensation. Annual compensation for determining such contributions consists of base salary, bonus and commissions, as applicable. Pension benefits vest over a five-year period with 20% vested after two years, 60% vested after three years, 80% vested after four years and 100% vested after five years. The Company funds the annual pension contribution by the following February of each applicable year. Pension expense related to the qualified pension plan for the year ended December 31, 2014 and 2013 was $834 thousand and $498 thousand, respectively.

National's parent company has a qualified profit sharing/401(k) plan in which it participates. The plan is a voluntary contributory plan that allows eligible employees to defer compensation for federal income tax purposes under Section 401(k) of the Internal Revenue Code of 1986, as amended. Employees may contribute, through payroll deductions, up to 25% of eligible compensation. National matches employee contributions up to the first 5% of such compensation and are made in the form of cash, whereby participants may direct the match to an investment of their choice. The benefit of National's contributions vest over a five-year period with 20% vested after two years, 60% vested after three years, 80% vested after four years and 100% vested after five years. Generally, a participating employee is entitled to distributions from the plan upon termination of employment, retirement, death or disability. Participants who qualify for distribution may receive a single lump sum, transfer assets to another qualified plan or individual retirement account, or receive a series of specified installment payments. Profit sharing/401(k) expense related to the qualified profit-sharing/401(k) plan for the year ended December 31, 2014 and 2013 was $334 thousand and $252 thousand, respectively.

In addition to the above two plans, National also participates in its parent company's non-qualified deferred compensation plan. Contributions to the above plans that exceed limitations established by federal regulations are then contributed to the non-qualified deferred compensation plan. The non-qualified pension expense for the years ended December 31, 2014 and 2013 was $457 thousand and $255 thousand, respectively. The non-qualified profit-sharing/401(k) expense for the years ended December 31, 2014 and 2013 was $178 thousand and $165 thousand, respectively.

National participates in its parent company's 2005 Omnibus Incentive Plan (the "Omnibus Plan"). The Omnibus Plan may grant any type of award including stock options, performance shares, performance units, restricted stock, restricted stock units and dividend equivalents. Following the effective date of the Omnibus Plan, no new options or awards were granted under any of the prior plans authorized by the MBIA Inc. shareholders.

The stock option component of the Omnibus Plan enables key employees to acquire shares of MBIA Inc. common stock. The stock option grants, which may be awarded every year, provide the right to purchase shares of MBIA Inc. common stock at the fair value of the stock on the date of grant. Options are exercisable as specified at the time of grant depending on the level of the recipient (generally four or five years) and expire either seven or ten years from the date of grant (or shorter if specified or following termination of employment).

Under the restricted stock component of the Omnibus Plan, certain employees are granted restricted shares of MBIA Inc.'s common stock. These awards have a restriction period lasting three, four or five years depending on the type of award, after which time the awards fully vest. During the vesting period these shares may not be sold. Restricted stock may be granted to all employees.

MBIA Inc. maintains voluntary retirement benefits, which provide certain benefits to all of National's eligible employees upon retirement. A description of these benefits is included in MBIA Inc.'s proxy statement. One of the components of the retirement program, for those employees that are retirement eligible, is to continue to vest all performance-based stock options and restricted share awards beyond the retirement date in accordance with the original vesting terms and to immediately vest all outstanding time-based stock options and restricted share grants.

MBIA Inc. valued all stock options granted using an option-pricing model. The value is recognized as an expense over the period in which the options vest. For the years ended December 31, 2014 and 2013, National had fully expensed its proportionate share of compensation cost for employee stock options in prior years and therefore had no 2014 or 2013 expense. National's proportionate share of compensation cost related to the restricted stock program for the years ended December 31, 2014 and 2013 was $560 thousand and $670 thousand, respectively.

13. Premium Revenue

National has not recorded unearned premium related to future installment payments nor has it recorded premiums receivable on installment contracts at December 31, 2014. The following table presents a roll forward of National's undiscounted premiums receivable for the year ended December 31, 2014 as if all installment premium contracts were received on an upfront basis.

In thousands			Adjustments			
Premiums Receivable as of December 31, 2013	Premium Payments Received	Premiums from New Business Written	Changes in Expected Term of Policies	Other	Premiums Receivable as of December 31, 2014	Reinsurance Premiums Payable as of December 31, 2014
$ 332,171	$ (20,968)	$ 6,475	$ (6,076)	$ (4,418)	$ 307,184	$ -

The following table presents the undiscounted future amount of premiums expected to be collected and the period in which those collections are expected to occur:

In thousands		**Expected Collection of Premiums**
Three months ended:		
March 31, 2015	$	1,822
June 30, 2015		3,761
September 30, 2015		3,695
December 31, 2015		4,362
Twelve months ended:		
December 31, 2016		13,862
December 31, 2017		13,630
December 31, 2018		13,298
December 31, 2019		13,091
Five years ended:		
December 31, 2024		60,647
December 31, 2029		54,023
December 31, 2034		47,016
December 31, 2039 and thereafter		77,977
Total	$	307,184

The following table presents the unearned premium revenue balance, gross of reinsurance, and the future gross expected premiums earned revenue as of and for the periods presented. The amounts reflected on the financial statements are net of reinsurance.

Expected Future Premium Earnings

In thousands	Unearned Premium Revenue	Upfront	Installments	Estimated Earnings of Future Premium Collections	Total Expected Future Premium Earnings
December 31, 2014	$ 1,375,079				
Three months ended:					
March 31, 2015	1,345,314	26,376	3,389	505	30,270
June 30, 2015	1,318,717	24,193	2,404	1,358	27,955
September 30, 2015	1,280,718	36,365	1,634	2,299	40,298
December 31, 2015	1,253,208	27,070	440	3,239	30,749
Twelve months ended:					
December 31, 2016	1,152,213	99,947	1,048	13,667	114,662
December 31, 2017	1,065,762	85,672	779	13,760	100,211
December 31, 2018	987,696	77,281	785	13,432	91,498
December 31, 2019	909,876	77,114	706	13,182	91,002
Five years ended:					
December 31, 2024	591,146	315,162	3,568	61,282	380,012
December 31, 2029	331,390	256,734	3,022	54,402	314,158
December 31, 2034	155,204	173,455	2,731	47,917	224,103
December 31, 2039 and thereafter	-	146,665	8,539	82,141	237,345
Total		$ 1,346,034	$ 29,045	$ 307,184	$ 1,682,263

14. Contingencies and Commitments

In the normal course of operating its business, National may be involved in various legal proceedings. Additionally, MBIA Inc. together with its subsidiaries may be involved in various legal proceedings that directly or indirectly impact National.

National and MBIA Corp. have received subpoenas or informal inquiries from a variety of regulators, regarding a variety of subjects. National and MBIA Corp. have cooperated fully with each of these regulators and have or are in the process of satisfying all such requests. National and MBIA Corp. may receive additional inquiries from these and other regulators and expect to provide additional information to such regulators regarding their inquiries in the future.

On July 23, 2008, the City of Los Angeles filed a complaint in the Superior Court of the State of California, County of Los Angeles, against a number of financial guarantee insurers, including MBIA. At the same time and subsequently, additional complaints against MBIA and nearly all of the same co-defendants were filed by various municipal entities and quasi-municipal entities, mostly in California. These cases are part of a coordination proceeding in Superior Court, San Francisco County, before Judge Richard A. Kramer, referred to as the Ambac Bond Insurance Cases. In August of 2011, the plaintiffs filed amended versions of their respective complaints. The claims allege violation of California's antitrust laws through maintaining a dual credit rating scale that misstated the credit default risk of certain issuers, thereby creating market demand for bond insurance. The plaintiffs also allege that the individual bond insurers participated in risky financial transactions in other lines of business that damaged each bond insurer's financial condition, and failure to adequately disclose the impact of those transactions on their financial condition. The plaintiffs also assert common law claims of breach of contract and fraud. The non-municipal plaintiffs also allege a California unfair competition cause of action. An appeal of the dismissal of the plaintiff's antitrust claim under California's Cartwright Act is pending. An appeal is also pending of the March 26, 2014 decision granting in part the Bond Insurer defendants' motions for reimbursement of legal fees incurred in connection with the motion to strike pursuant to California's Anti-SLAPP stature.

On July 23, 2008, the City of Los Angeles filed a separate complaint in the Superior Court, County of Los Angeles, naming as defendants MBIA and other financial institutions, and alleging fraud and violations of California's antitrust laws through bid-rigging in the sale of guaranteed investment contracts and what plaintiffs call "municipal derivatives" to municipal bond issuers. The case was removed to federal court and transferred by order dated November 26, 2008 to the Southern District of New York for inclusion in the multidistrict litigation, Municipal Derivatives Antitrust Litigation, M.D.L. No. 1950. Complaints making the same allegations against MBIA and nearly all of the same co-defendants were then, or subsequently, filed by municipal entities and quasi-municipal entities, mostly in California, and three not-for-profit retirement community operators. These cases have all been added to the multidistrict litigation. The plaintiffs in all of the cases assert federal and either California or New York state antitrust claims. As of May 31, 2011, MBIA has answered all of the existing complaints.

National and Assured Guaranty Municipal Corp. commenced an adversary proceeding against the City of Detroit and certain individuals employees/managers in the City of Detroit's chapter 9 case. The amended complaint sought a declaratory judgment that the City of Detroit and its employees comply with Michigan law in the collection, segregation and use of ad valorem tax proceeds pledged to repay several series of unlimited tax general obligation bonds as well as declaratory relief with respect to National's and Assured Guaranty Municipal Corp.'s rights and interests in the ad valorem tax proceeds. In April of 2014, National reached a settlement with the City of Detroit regarding its enhanced Unlimited Tax General Obligation bonds, which was approved when the City of Detroit's Eighth Amended Plan went effective on December 10, 2014.

On January 30, 2013, MBIA Insurance Corp. and National filed a petition in Texas state court seeking an order requiring the Harris County-Houston Sports Authority to impose higher taxes as well as damages for other alleged breaches of contract. On December 30, 2014, the litigation was resolved in connection with a refinancing transaction.

MBIA Inc. and National are defending against the aforementioned actions in which they are a defendant and expect ultimately to prevail on the merits. There is no assurance, however, that they will prevail in these actions. Adverse rulings in these actions could have a material adverse effect on National'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, National 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 National, threatened, to which National is a party.

Headquarters Lease Agreement

In September of 2014, National moved its headquarters to Purchase, New York, for which National had previously entered into a lease agreement as part of the Company's cost reduction measures that included the plan to sell the Armonk, New York facility. The initial lease term expires in 2030 with the option to terminate the lease in 2025 upon the payment of a termination amount. At the end of the initial lease term, National has the option to extend the term of the lease for two additional terms of five years at a fixed annual rent based on the fair market rent at the time of any extension. The total future minimum lease payments over the initial lease term are $42 million. National received a lease incentive amount of $6 million from the property owner to fund certain leasehold improvements. The total future minimum lease payments include annual rent escalation amounts and a free rent period and exclude the lease incentive amount. The lease agreement has been classified as an operating lease, and operating rent expense has been recognized on a straight-line basis since the second quarter of 2014.

15. Subsequent Events

Subsequent events have been considered through March 2, 2015, the date upon which the audited statutory financial statements were available to be issued.

Refer to "Note 14. Contingencies and Commitments" for information about legal proceedings that commenced after December 31, 2014.