MGIC INVESTMENT CORP
Form 10-Q
August 10, 2015

FORM 10-Q
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2015
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______ to ______
Commission file number 1-10816

MGIC INVESTMENT CORPORATION
(Exact name of registrant as specified in its charter)

WISCONSIN	39-1486475
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
250 E. KILBOURN AVENUE MILWAUKEE, WISCONSIN (Address of principal executive offices)	53202 (Zip Code)

(414) 347-6480
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES NO

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

Large accelerated filer	Accelerated filer	Non-accelerated filer	Smaller reporting company	(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

CLASS OF STOCK	PAR VALUE	DATE	NUMBER OF SHARES
Common stock	$1.00	07/31/15	339,638,670

Forward Looking and Other Statements

All statements in this report that address events, developments or results that we expect or anticipate may occur in the future are “forward looking statements.” Forward looking statements consist of statements that relate to matters other than historical fact. In most cases, forward looking statements may be identified by words such as “believe,” “anticipate” or “expect,” or words of similar import. The risk factors referred to in “Forward Looking Statements and Risk Factors – Location of Risk Factors” in Management’s Discussion and Analysis of Financial Condition and Results of Operations below, may cause our actual results to differ materially from the results contemplated by forward looking statements that we may make. We are not undertaking any obligation to update any forward looking statements or other statements we may make in this document even though these statements may be affected by events or circumstances occurring after the forward looking statements or other statements were made. Therefore no reader of this document should rely on these statements being current as of any time other than the time at which this document was filed with the Securities and Exchange Commission.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	June 30, 2015	December 31, 2014
ASSETS	(In thousands)	
Investment Portfolio (notes 7 and 8):		
Securities, available-for-sale, at fair value:		
Fixed maturities (amortized cost, 2015 - $4,586,317; 2014 - $4,602,514)	$4,549,047	$4,609,614
Equity securities	3,063	3,055
Total investment portfolio	4,552,110	4,612,669
Cash and cash equivalents	215,770	197,882
Restricted cash and cash equivalents (note 1)	-	17,212
Accrued investment income	34,561	30,518
Prepaid reinsurance premiums	58,085	47,623
Reinsurance recoverable on loss reserves	53,456	57,841
Reinsurance recoverable on paid losses	5,918	6,424
Premiums receivable	52,468	57,442
Home office and equipment, net	28,925	28,693
Deferred insurance policy acquisition costs	14,160	12,240
Profit commission receivable (note 4)	142,457	91,500
Other assets	88,872	106,390
Total assets	$5,246,782	$5,266,434
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities:		
Loss reserves (note 12)	$2,110,761	$2,396,807
Premium deficiency reserve (note 13)	-	23,751
Unearned premiums	244,288	203,414
Senior notes (note 3)	61,941	61,918
Convertible senior notes (note 3)	845,000	845,000
Convertible junior debentures (note 3)	389,522	389,522
Other liabilities	356,986	309,119
Total liabilities	4,008,498	4,229,531
Contingencies (note 5)		
Shareholders' equity (note 14):		
Common stock (one dollar par value, shares authorized 1,000,000; shares issued 2015 - 340,079; 2014 - 340,047; shares outstanding 2015 - 339,639; 2014 - 338,560)	340,079	340,047
Paid-in capital	1,664,931	1,663,592
Treasury stock (shares at cost 2015 - 440; 2014 - 1,487)	(3,362)	(32,937)
Accumulated other comprehensive loss, net of tax (note 9)	(128,140)	(81,341)
Retained deficit	(635,224)	(852,458)
Total shareholders' equity	1,238,284	1,036,903
Total liabilities and shareholders' equity	$5,246,782	$5,266,434

See accompanying notes to consolidated financial statements.

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands, except per share data)			
Revenues:				
Premiums written:				
Direct	$261,404	$241,249	$526,816	$485,438
Assumed	308	430	646	881
Ceded (note 4)	(34,937)	(28,294)	(66,231)	(54,914)
Net premiums written	226,775	213,385	461,231	431,405
Increase in unearned premiums, net	(13,267)	(5,899)	(30,435)	(9,658)
Net premiums earned	213,508	207,486	430,796	421,747
Investment income, net of expenses	25,756	21,180	49,876	41,336
Net realized investment gains (losses):				
Total other-than-temporary impairment losses	-	-	-	-
Portion of losses recognized in comprehensive income, before taxes	-	-	-	-
Net impairment losses recognized in earnings	-	-	-	-
Other realized investment gains	166	522	26,493	291
Net realized investment gains	166	522	26,493	291
Other revenue	3,699	2,048	6,179	2,944
Total revenues	243,129	231,236	513,344	466,318
Losses and expenses:				
Losses incurred, net (note 12)	90,238	141,141	172,023	263,749
Change in premium deficiency reserve (note 13)	(17,333)	(7,833)	(23,751)	(13,006)
Amortization of deferred policy acquisition costs	2,046	1,676	3,803	3,095
Other underwriting and operating expenses, net	35,829	32,238	75,097	70,219
Interest expense	17,373	17,374	34,735	34,913
Total losses and expenses	128,153	184,596	261,907	358,970
Income before tax	114,976	46,640	251,437	107,348
Provision for income taxes (note 11)	1,322	1,118	4,707	1,844
Net income	$113,654	$45,522	$246,730	$105,504
Income per share (note 6)				
Basic	$0.33	$0.13	$0.73	$0.31
Diluted	$0.28	$0.12	$0.60	$0.27
Weighted average common shares outstanding - basic (note 6)	339,705	338,626	339,406	338,419
Weighted average common shares outstanding - diluted (note 6)	439,148	413,481	439,221	413,374

See accompanying notes to consolidated financial statements.

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands)			
Net income	$113,654	$45,522	$246,730	$105,504
Other comprehensive (loss) income, net of tax (note 9):				
Change in unrealized investment gains and losses (note 7)	(63,646)	44,501	(44,083)	84,099
Benefit plan adjustments	(392)	(1,980)	(1,092)	(3,466)
Foreign currency translation adjustment	390	587	(1,624)	1,840
Other comprehensive (loss) income, net of tax	(63,648)	43,108	(46,799)	82,473
Comprehensive income	$50,006	$88,630	$199,931	$187,977

See accompanying notes to consolidated financial statements

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Unaudited)

	Six Months Ended June 30,	
	2015	2014
	(In thousands)	
Common stock		
Balance, beginning of period	$340,047	$340,047
Net common stock issued under share-based compensation plans	32	-
Balance, end of period	340,079	340,047
Paid-in capital		
Balance, beginning of period	1,663,592	1,661,269
Net common stock issued under share-based compensation plans	(32)	-
Reissuance of treasury stock, net	(7,181)	(6,680)
Tax benefit from share-based compensation	2,568	-
Equity compensation	5,984	4,072
Balance, end of period	1,664,931	1,658,661
Treasury stock		
Balance, beginning of period	(32,937)	(64,435)
Reissuance of treasury stock, net	29,575	31,498
Balance, end of period	(3,362)	(32,937)
Accumulated other comprehensive income (loss)		
Balance, beginning of period	(81,341)	(117,726)
Other comprehensive (loss) income	(46,799)	82,473
Balance, end of period	(128,140)	(35,253)
Retained earnings (deficit)		
Balance, beginning of period	(852,458)	(1,074,617)
Net income	246,730	105,504
Reissuance of treasury stock, net	(29,496)	(29,790)
Balance, end of period	(635,224)	(998,903)
Total shareholders' equity	$1,238,284	$931,615

See accompanying notes to consolidated financial statements.

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended June 30,	
	2015	2014
	(In thousands)	
Cash flows from operating activities:		
Net income	$246,730	$105,504
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	23,938	26,869
Deferred tax (benefit) expense	(13)	243
Realized investment gains, net	(26,493)	(291)
Loss on repurchases of senior notes	-	837
Excess tax benefits related to share-based compensation	(2,568)	-
Other	23,690	(8,292)
Change in certain assets and liabilities:		
Accrued investment income	(4,043)	2,630
Prepaid insurance premium	(10,462)	(4,018)
Reinsurance recoverable on loss reserves	4,385	6,322
Reinsurance recoverable on paid losses	506	2,908
Premium receivable	4,974	9,367
Deferred insurance policy acquisition costs	(1,920)	(955)
Profit commission receivable	(50,957)	(44,697)
Real estate	4,663	2,476
Loss reserves	(286,046)	(385,807)
Premium deficiency reserve	(23,751)	(13,006)
Unearned premiums	40,874	13,721
Return premium accrual	(3,500)	7,800
Income taxes payable - current	102	(752)
Net cash used in operating activities	(59,891)	(279,141)
Cash flows from investing activities:		
Purchases of investments:		
Fixed maturities	(1,499,319)	(1,054,567)
Equity securities	(39)	(40)
Proceeds from sales of fixed maturities	1,218,688	718,938
Proceeds from maturity of fixed maturities	298,618	649,468
Net increase (decrease) in payable for securities	41,762	(4)
Net decrease in restricted cash	17,212	237
Additions to property and equipment	(1,711)	(3,216)
Net cash provided by investing activities	75,211	310,816
Cash flows from financing activities:		
Repayment of long-term debt	-	(21,767)
Excess tax benefits related to share-based compensation	2,568	-
Net cash provided by (used in) financing activities	2,568	(21,767)
Net increase in cash and cash equivalents	17,888	9,908
Cash and cash equivalents at beginning of period	197,882	332,692

Cash and cash equivalents at end of period	$215,770	$342,600

See accompanying notes to consolidated financial statements.

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2015
(Unaudited)

Note 1 – Nature of Business and Basis of Presentation

MGIC Investment Corporation is a holding company which, through Mortgage Guaranty Insurance Corporation ("MGIC"), MGIC Indemnity Corporation (“MIC”) and several other subsidiaries, is principally engaged in the mortgage insurance business. We provide mortgage insurance to lenders throughout the United States and to government sponsored entities (“GSEs”) to protect against loss from defaults on low down payment residential mortgage loans.

The accompanying unaudited consolidated financial statements of MGIC Investment Corporation and its wholly-owned subsidiaries have been prepared in accordance with the instructions to Form 10-Q as prescribed by the Securities and Exchange Commission (“SEC”) for interim reporting and do not include all of the other information and disclosures required by accounting principles generally accepted in the United States of America (“GAAP”). These statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2014 included in our Annual Report on Form 10-K. As used below, “we,” “our” and “us” refer to MGIC Investment Corporation’s consolidated operations or to MGIC Investment Corporation, as the context requires.

In the opinion of management the accompanying financial statements include all adjustments, consisting primarily of normal recurring accruals, necessary to fairly state our financial position and results of operations for the periods indicated. The results of operations for the interim period may not be indicative of the results that may be expected for the year ending December 31, 2015.

Capital - GSEs

Since 2008, substantially all of our insurance written has been for loans sold to Fannie Mae and Freddie Mac (the “GSEs”). In April 2015, the GSEs each released revised private mortgage insurer eligibility requirements (the “PMIERs”) that become effective December 31, 2015. The PMIERs include revised financial requirements for mortgage insurers (the “GSE Financial Requirements”) under which a mortgage insurer’s “Available Assets” (generally only the most liquid assets of an insurer) must meet or exceed “Minimum Required Assets” (which are based on an insurer’s book and are calculated from tables of factors with several risk dimensions and are subject to a floor amount).

We expect that MGIC will be in compliance with the PMIERs, including the GSE Financial Requirements, when they become effective. This expectation is based on our interpretation of the GSE Financial Requirements and assumes that the risk in force and assets of MGIC’s MIC subsidiary will be repatriated to MGIC and that we will receive substantially all of the benefit available under the PMIERs for our existing reinsurance agreement, upon the effectiveness of its restructure, which has been agreed between MGIC and the reinsurers, subject to final documentation. Fannie Mae and the Office of the Commissioner of Insurance of the State of Wisconsin (“OCI”) have each approved the restructured transaction; however, its effectiveness remains subject to approval by Freddie Mac. Although it has not yet been approved, Freddie Mac has not raised material objections to the restructured transaction.

If additional Available Assets are required, we believe that a portion of our holding company's $463 million of cash and investments at June 30, 2015, may be available for future contribution to MGIC.

Factors that may negatively impact MGIC's ability to comply with the GSE Financial Requirements before their effective date include the following:

- Freddie Mac may not approve our restructured reinsurance agreement or allow the amount of benefit we expect under the GSE Financial Requirements.

- We may not obtain regulatory authorization to transfer assets from MIC to MGIC to the extent we are assuming because regulators project higher losses than we project or require a level of capital be maintained in MIC higher than we are assuming.

- MGIC may not receive additional capital contributions from our holding company due to competing demands on the holding company resources, including for repayment of debt.

- Our future operating results may be negatively impacted by the matters discussed in the rest of these footnotes. Such matters could decrease our revenues, increase our losses or require the use of assets, thereby increasing our shortfall in Available Assets.

There can be no assurance that the GSEs will not make the GSE Financial Requirements more onerous in the future; in this regard, the PMIERs provide that the tables of factors that determine Minimum Required Assets will be updated every two years and may be updated more frequently to reflect changes in macroeconomic conditions or loan performance. The GSEs will provide notice 180 days prior to the effective date of table updates. In addition, the GSEs may amend the PMIERs at any time. If MGIC ceases to be eligible to insure loans purchased by one or both of the GSEs, it would significantly reduce the volume of our new business writings.

While on an overall basis, the amount of Available Assets we must hold in order to continue to insure GSE loans has increased under the PMIERs over what state regulation currently provides, reinsurance is one option we have to mitigate the effect of PMIERs on our returns. In this regard, see the first bullet point above.

See additional disclosure regarding statutory capital in Note 16 – "Statutory Capital."

Reclassifications

Certain reclassifications have been made in the accompanying financial statements to 2014 amounts to conform to 2015 presentation. For the six months ended June 30, 2014 cash used for additions to property and equipment was previously presented as "Other" within cash flows from operations and is currently presented separately as "Additions to property and equipment" within cash flows from investing activities as of June 30, 2015. This revision is not material to amounts previously reported or disclosed by us in prior periods.

Restricted cash and cash equivalents

During the second quarter of 2013, approximately $60.3 million was placed in escrow in connection with the two agreements we entered into to resolve our dispute with Countrywide Home Loans, Inc. ("CHL") and its affiliate, Bank of America, N.A., as successor to Countrywide Home Loans Servicing LP ("BANA" and collectively with CHL, "Countrywide") regarding rescissions. In the fourth quarter of 2013, approximately $42.9 million was released from escrow in connection with the BANA agreement. In the first quarter of 2015, the remaining escrow funds were disbursed to us pursuant to the amended and restated settlement agreement and release entered into with CHL on March 2, 2015. See additional discussion of these settlement agreements in Note 5 – "Litigation and Contingencies."

Subsequent events

We have considered subsequent events through the date of this filing.

Note 2 – New Accounting Pronouncements

Revenue from Contracts with Customers

In May 2014, the FASB issued guidance to clarify the principles for recognizing revenue. While insurance contracts are not within the scope of this updated guidance, our fee income related to contract underwriting and other fee-based services provided to lenders will be subject to this guidance. The updated guidance requires an entity to recognize revenue as performance obligations are met, in order to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration the entity is entitled to receive for those goods or services. The guidance also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts. The guidance is effective for reporting periods beginning after December 15, 2017 with early adoption for reporting periods beginning after December 15, 2016 permitted. We are currently evaluating the impact of this update, but it is not expected to have a significant impact on our consolidated financial statements and disclosures.

Presentation of Debt Issuance Costs

In April 2015, the FASB amended existing guidance related to the presentation of debt issuance costs. The new standard requires the presentation of debt issuance costs in the balance sheet as a deduction from the carrying amount of the related debt liability instead of a deferred charge. It is effective for annual reporting periods beginning after December 15, 2015, but early adoption is permitted. The adoption of this guidance is not expected to have a significant impact on our consolidated financial statements.

Note 3 – Debt

Long-term debt as of June 30, 2015 and December 31, 2014 consists of the following obligations.

	June 30, 2015	December 31, 2014
	(In millions)	
Senior Notes, interest at 5.375% per annum, due November 2015	$61.9	$61.9
Convertible Senior Notes, interest at 5% per annum, due May 2017 (1)	345.0	345.0
Convertible Senior Notes, interest at 2% per annum, due April 2020 (2) (3)	500.0	500.0
Convertible Junior Subordinated Debentures, interest at 9% per annum, due April 2063 (4)	389.5	389.5
Total debt	1,296.4	1,296.4
Less current portion of debt	(61.9)	(61.9)
Total long-term debt	$1,234.5	$1,234.5

(1) Convertible at any time prior to maturity at the holder's option, at an initial conversion rate, which is subject to adjustment, of 74.4186 shares per $1,000 principal amount, representing an initial conversion price of approximately $13.44 per share.

(2) Prior to January 1, 2020, the 2% Convertible Senior Notes are convertible only upon satisfaction of one or more conditions. One such condition is that during any calendar quarter commencing after March 31, 2014, the last reported sale price of our common stock for each of at least 20 trading days during the 30 consecutive trading days ending on, and including, the last trading day of the immediately preceding calendar quarter be greater than or equal to 130% of the applicable conversion price on each applicable trading day. The 2% Notes are convertible at an initial conversion rate, which is subject to adjustment, of 143.8332 shares per $1,000 principal amount, representing an initial conversion price of approximately $6.95 per share. 130% of such conversion price is $9.03. On or after January 1, 2020, holders may convert their notes irrespective of satisfaction of the conditions. Our common stock price was greater than or equal to 130% of the applicable conversion price for each of at least 20 trading days during the 30 consecutive trading days ending on, and including, June 30, 2015.

(3) Prior to April 10, 2017, the notes will not be redeemable. On any business day on or after April 10, 2017 we may redeem for cash all or part of the notes, at our option, at a redemption rate equal to 100% of the principal amount of the notes being redeemed, plus any accrued and unpaid interest, if the closing sale price of our common stock exceeds 130% of the then prevailing conversion price of the notes for each of at least 20 of the 30 consecutive trading days preceding notice of the redemption.

(4) Convertible at any time prior to maturity at the holder's option, at an initial conversion rate, which is subject to adjustment, of 74.0741 shares per $1,000 principal amount, representing an initial conversion price of approximately $13.50 per share. If a holder elects to convert their debentures, deferred interest owed on the debentures being converted is also converted into shares of our common stock. The conversion rate for any deferred interest is based on the average price that our shares traded at during a 5-day period immediately prior to the election to convert. In lieu of issuing shares of common stock upon conversion of the debentures, we may, at our option, make a cash payment to converting holders for all or some of the shares of our common stock otherwise issuable upon conversion.

Interest payments on our existing debt obligations appear below.

	Six months ended June 30,	
	2015	2014
	(In millions)	
Senior Notes, interest at 5.375% per annum, due November 2015	$1.7	$2.0
Convertible Senior Notes, interest at 5% per annum, due May 2017	8.6	8.6
Convertible Senior Notes, interest at 2% per annum, due April 2020	5.0	5.0
Convertible Junior Subordinated Debentures, interest at 9% per annum, due April 2063	17.5	17.5
Total interest payments	$32.8	$33.1

The Senior Notes, Convertible Senior Notes and Convertible Junior Subordinated Debentures are obligations of our holding company, MGIC Investment Corporation, and not of its subsidiaries. At June 30, 2015, we had approximately $463 million in cash and investments at our holding company. The net unrealized gains on our holding company investment portfolio were approximately $1.5 million at June 30, 2015. The modified duration of the holding company investment portfolio, excluding cash and cash equivalents, was 2.7 years at June 30, 2015.

Note 4 – Reinsurance

A summary of our quota share reinsurance agreements, excluding captive agreements, appears below.

	Six months ended June 30,	
	2015	2014
	(In thousands)	
Ceded premiums written, net of profit commission	$58,055	$44,689
Ceded premiums earned, net of profit commission	47,567	40,594
Ceded losses incurred	6,060	5,658
Ceding commissions (1)	21,803	17,877
Ceded unearned premiums	57,842	39,946

(1) Ceding commissions are reported within Other underwriting and operating expenses, net on the consolidated statements of operations.

As of June 30, 2015 and December 31, 2014, we have accrued a profit commission receivable of $142.5 million and $91.5 million, respectively. This receivable may further increase through the term of the agreement, but the ultimate amount of the profit commission will depend on the ultimate level of premiums earned net of ceding commissions and losses incurred under the agreement. A commutation of our existing reinsurance agreement would result in any unearned premium being returned to us, a related return of ceding commission to the reinsurers and an adjustment to the profit commission. Profit commissions are recorded as a reduction to our ceded premiums. We do not expect a commutation to materially affect our results from operations. The anticipated restructuring of the agreement will effectively commute our existing agreement and any profit commission would be paid to us upon such commutation. Recoverables under the existing agreement are supported by trust funds or letters of credit.

In the past, MGIC also obtained captive reinsurance. In a captive reinsurance arrangement, the reinsurer is affiliated with the lender for whom MGIC provides mortgage insurance. As part of our settlement with the Consumer Financial Protection Bureau ("CFPB") in 2013 and with the Minnesota Department of Commerce (the "MN Department") in June 2015, discussed in Note 5 – "Litigation and Contingencies", MGIC has agreed to not enter into any new captive reinsurance agreement or reinsure any new loans under any existing captive reinsurance agreement for a period of ten years subsequent to the respective settlements. In accordance with the CFPB settlement, all of our active captive arrangements were placed into run-off. In addition, at the time PMIERs become effective on December 31, 2015 the GSEs will not approve any future reinsurance or risk sharing transaction with a mortgage enterprise or an affiliate of a mortgage enterprise.

Captive agreements were generally written on an annual book of business and each captive reinsurer is required to maintain a separate trust account to support its combined reinsured risk on all annual books. MGIC is the sole beneficiary of the trusts, and the trust accounts are made up of capital deposits by the captive reinsurers, premium deposits by MGIC, and investment income earned. These amounts are held in the trust account and are available to pay reinsured losses. The reinsurance recoverable on loss reserves related to captive agreements was $38 million at June 30, 2015 which was supported by $163 million of trust assets, while at December 31, 2014, the reinsurance recoverable on loss reserves related to captive agreements was $45 million, which was supported by $198 million of trust assets.

Note 5 – Litigation and Contingencies

Before paying a claim, we review the loan and servicing files to determine the appropriateness of the claim amount. All of our insurance policies provide that we can reduce or deny a claim if the servicer did not comply with its obligations under our insurance policy, including the requirement to mitigate our loss by performing reasonable loss mitigation efforts or, for example, diligently pursuing a foreclosure or bankruptcy relief in a timely manner. We call such reduction of claims submitted to us "curtailments." In 2014 and the first half of 2015, curtailments reduced our average claim paid by approximately 6.7% and 7.4%, respectively. After we pay a claim, servicers and insureds sometimes object to our curtailments and other adjustments. We review these objections if they are sent to us within 90 days after the claim was paid.

When reviewing the loan file associated with a claim, we may determine that we have the right to rescind coverage on the loan. In recent quarters, approximately 5% of claims received in a quarter have been resolved by rescissions, down from the peak of approximately 28% in the first half of 2009. We estimate rescissions mitigated our incurred losses by approximately $2.5 billion in 2009 and $0.2 billion in 2010 and have not significantly mitigated our incurred losses since then. Our loss reserving methodology incorporates our estimates of future rescissions and reversals of rescissions. Historically, reversals of rescissions have been immaterial. A variance between ultimate actual rescission and reversal rates and our estimates, as a result of the outcome of litigation, settlements or other factors, could materially affect our losses.

If the insured disputes our right to rescind coverage, we generally engage in discussions in an attempt to settle the dispute. As part of those discussions, we may voluntarily suspend rescissions we believe may be part of a settlement. Certain settlements require GSE approval. The GSEs consented to our settlement agreements with Countrywide, as discussed below, but there is no guarantee they will approve others. We have reached and implemented settlement agreements that do not require GSE approval, but they have not been material in the aggregate.

If we are unable to reach a settlement, the outcome of a dispute ultimately would be determined by legal proceedings. Under our policies in effect prior to October 1, 2014, legal proceedings disputing our right to rescind coverage may be brought up to three years after the lender has obtained title to the property (typically through a foreclosure) or the property was sold in a sale that we approved, whichever is applicable, and under our master policy effective October 1, 2014, such proceedings may be brought up to two years from the date of the notice of rescission. In a few jurisdictions there is a longer time to bring such proceedings.

Until a liability associated with a settlement agreement or litigation becomes probable and can be reasonably estimated, we consider our claim payment or rescission resolved for financial reporting purposes even though discussions and legal proceedings have been initiated and are ongoing. Under ASC 450-20, an estimated loss from such discussions and proceedings is accrued for only if we determine that the loss is probable and can be reasonably estimated.

In December 2009, we entered into legal proceedings with Countrywide Home Loans, Inc. ("CHL") and its affiliate, Bank of America, N.A., as successor to Countrywide Home Loans Servicing LP ("BANA" and collectively with CHL, "Countrywide") in which Countrywide alleged that MGIC denied valid mortgage insurance claims. (In our SEC reports, we refer to insurance rescissions and denials of claims collectively as "rescissions" and variations of that term.)

In April 2013, MGIC entered into separate settlement agreements with CHL and BANA, pursuant to which the parties agreed to settle the Countrywide litigation as it relates to MGIC's rescission practices (as amended from time to time, the "Agreements"). The Agreement with BANA covers loans purchased by the GSEs. That original Agreement was implemented beginning in November 2013 and we resolved all related suspended rescissions in November and December 2013 by paying the associated claim or processing the rescission.

On March 2, 2015, the parties to the Agreement with CHL amended and restated that Agreement. The Agreement with CHL covers loans that were purchased by non-GSE investors, including securitization trusts. The original Agreement addressed rescission and denial rights; the amended and restated Agreement also addresses curtailment rights. Implementation of that Agreement occurred in June 2015 with respect to loans for which consent to the Agreement was received.

The estimated impact of the Agreements has been recorded in our financial statements. The pending arbitration proceedings concerning the loans covered by the Agreements have been dismissed, the mutual releases regarding loans for which consent was received have become effective and the litigation between the parties regarding loans covered by the Agreements has been dismissed. Consent was received for approximately 89% of the dollar amount of exposure on loans covered by the Agreement with CHL; the holders of loans that did not consent retain their rights to assert claims with respect to such loans.

The estimated impact of other probable settlements has also been recorded in our financial statements. The estimated impact that we recorded for other probable settlements is our best estimate of our loss from these matters. We estimate that as of June 30, 2015, the maximum exposure above the best estimate provision we recorded is $122 million. If we are not able to implement the other settlements we consider probable, we intend to defend MGIC vigorously against any related legal proceedings.

The flow policies at issue with Countrywide are in the same form as the flow policies that we used with all of our customers during the period covered by the Agreements, and the bulk policies at issue vary from one another, but are generally similar to those used in the majority of our Wall Street bulk transactions.

We are involved in discussions and consensual proceedings with insureds with respect to our claims paying practices. In addition, holders of loans that did not consent to the Agreement with CHL may bring legal proceedings against MGIC with respect to such loans. Although it is reasonably possible that when these discussions or proceedings are completed we will not prevail in all cases, we are unable to make a reasonable estimate or range of estimates of the potential liability. We estimate the maximum exposure associated with these discussions and proceedings to be approximately $218 million, although we believe we will ultimately resolve these matters for significantly less than this amount.

The estimates of our maximum exposure referred to above do not include interest or consequential or exemplary damages.

Consumers continue to bring lawsuits against home mortgage lenders and settlement service providers. Mortgage insurers, including MGIC, have been involved in litigation alleging violations of the anti-referral fee provisions of the Real Estate Settlement Procedures Act, which is commonly known as RESPA, and the notice provisions of the Fair Credit Reporting Act, which is commonly known as FCRA. MGIC’s settlement of class action litigation against it under RESPA became final in October 2003. MGIC settled the named plaintiffs’ claims in litigation against it under FCRA in December 2004, following denial of class certification in June 2004. Since December 2006, class action litigation has been brought against a number of large lenders alleging that their captive mortgage reinsurance arrangements violated RESPA. Beginning in December 2011, MGIC, together with various mortgage lenders and other mortgage insurers, was named as a defendant in twelve lawsuits, alleged to be class actions, filed in various U.S. District Courts. The complaints in all of the cases alleged various causes of action related to the captive mortgage reinsurance arrangements of the mortgage lenders, including that the lenders’ captive reinsurers received excessive premiums in relation to the risk assumed by those captives, thereby violating RESPA. As of the end of the first quarter of 2015, MGIC has been dismissed from all twelve cases. There can be no assurance that we will not be subject to further litigation under RESPA (or FCRA) or that the outcome of any such litigation would not have a material adverse effect on us.

In 2013, the U.S. District Court for the Southern District of Florida approved a settlement with the CFPB that resolved a federal investigation of MGIC's participation in captive reinsurance arrangements in the mortgage insurance industry. The settlement concluded the investigation with respect to MGIC without the CFPB or the court making any findings of wrongdoing. As part of the settlement, MGIC agreed that it would not enter into any new captive reinsurance agreement or reinsure any new loans under any existing captive reinsurance agreement for a period of ten years. MGIC had voluntarily suspended most of its captive arrangements in 2008 in response to market conditions and GSE requests. In connection with the settlement, MGIC paid a civil penalty of $2.65 million and the court issued an injunction prohibiting MGIC from violating any provisions of RESPA.

We received requests from the MN Department beginning in February 2006 regarding captive mortgage reinsurance and certain other matters in response to which MGIC has provided information on several occasions. In June 2015, MGIC executed a Consent Order with the MN Department that resolved the MN Department's investigation of captive reinsurance matters without making any findings of wrongdoing. The Consent Order provides, among other things, that MGIC is prohibited from entering into any new captive reinsurance agreement or reinsuring any new loans under any existing captive reinsurance agreement for a period of ten years.

We also received a request in June 2005 from the New York Department of Financial Services for information regarding captive mortgage reinsurance arrangements and other types of arrangements in which lenders receive compensation.

Various regulators, including the CFPB, state insurance commissioners and state attorneys general may bring actions seeking various forms of relief in connection with alleged violations of RESPA. The insurance law provisions of many states prohibit paying for the referral of insurance business and provide various mechanisms to enforce this prohibition. While we believe our practices are in conformity with applicable laws and regulations, it is not possible to predict the eventual scope, duration or outcome of any such reviews or investigations nor is it possible to predict their effect on us or the mortgage insurance industry.

We are subject to comprehensive, detailed regulation by state insurance departments. These regulations are principally designed for the protection of our insured policyholders, rather than for the benefit of investors. Although their scope varies, state insurance laws generally grant broad supervisory powers to agencies or officials to examine insurance companies and enforce rules or exercise discretion affecting almost every significant aspect of the insurance business. State insurance regulatory authorities could take actions, including changes in capital requirements, that could have a material adverse effect on us. In addition, the CFPB may issue additional rules or regulations, which may materially affect our business.

In December 2013, the U.S. Treasury Department's Federal Insurance Office released a report that calls for federal standards and oversight for mortgage insurers to be developed and implemented. It is uncertain what form the standards and oversight will take and when they will become effective.

A non-insurance subsidiary of our holding company is a shareholder of the corporation that operates the Mortgage Electronic Registration System ("MERS"). Our subsidiary, as a shareholder of MERS, had been named as a defendant (along with MERS and its other shareholders) in eight lawsuits asserting various causes of action arising from allegedly improper recording and foreclosure activities by MERS. As of June 5, 2015, all of these lawsuits have been dismissed without any further opportunity to appeal.

In addition to the matters described above, we are involved in other legal proceedings in the ordinary course of business. In our opinion, based on the facts known at this time, the ultimate resolution of these ordinary course legal proceedings will not have a material adverse effect on our financial position or results of operations.

Through a non-insurance subsidiary, we utilize our underwriting skills to provide an outsourced underwriting service to our customers known as contract underwriting. As part of the contract underwriting activities, that subsidiary is responsible for the quality of the underwriting decisions in accordance with the terms of the contract underwriting agreements with customers. That subsidiary may be required to provide certain remedies to its customers if certain standards relating to the quality of our underwriting work are not met, and we have an established reserve for such future obligations. Claims for remedies may be made a number of years after the underwriting work was performed. Beginning in the second half of 2009, our subsidiary experienced an increase in claims for contract underwriting remedies, which continued throughout 2012. The underwriting remedy expense for 2014 and the first half of 2015 was approximately $4 million and $1 million, respectively, but may increase in the future.

See Note 11 – "Income Taxes" for a description of federal income tax contingencies.

Note 6 – Earnings per Share

Basic earnings per share ("EPS") is calculated by dividing net income by the weighted average number of common shares outstanding during the reporting period. Diluted EPS includes the components of basic EPS and also gives effect to dilutive common equivalent shares outstanding during the reporting period. We calculate diluted EPS using the treasury stock method for unvested restricted stock, and the if-converted method for convertible debt instruments. For unvested restricted stock, assumed proceeds under the treasury stock method would include unamortized compensation expense and windfall tax benefits or shortfalls. The determination of potentially issuable shares from our convertible debt instruments does not consider satisfaction of the conversion requirements and the shares are included in the determination of diluted EPS as of the beginning of the period, if dilutive. In addition, interest expense, net of tax, related to dilutive convertible debt instruments is added back to earnings in calculating diluted EPS.

The following table reconciles the numerators and denominators used to calculate basic and diluted EPS and also indicates the number of antidilutive securities.

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
	(In thousands, except per share data and as otherwise noted)			
Basic earnings per share:				
Net income	$113,654	$45,522	$246,730	$105,504
Weighted average common shares outstanding	339,705	338,626	339,406	338,419
Basic income per share	$0.33	$0.13	$0.73	$0.31
Diluted earnings per share:				
Net income	$113,654	$45,522	$246,730	$105,504
Interest expense, net of tax:				
2% Convertible Senior Notes due 2020	3,049	3,049	6,098	6,098
5% Convertible Senior Notes due 2017	4,692	-	9,384	-
Diluted income available to common shareholders	$121,395	$48,571	$262,212	$111,602
Weighted average shares - basic	339,705	338,626	339,406	338,419
Effect of dilutive securities:				
Unvested restricted stock units	1,831	2,913	2,203	3,013
2% Convertible Senior Notes due 2020	71,942	71,942	71,942	71,942
5% Convertible Senior Notes due 2017	25,670	-	25,670	-
Weighted average shares - diluted	439,148	413,481	439,221	413,374
Diluted income per share	$0.28	$0.12	$0.60	$0.27
Antidilutive securities (in millions)	28.9	54.5	28.9	54.5

Note 7 – Investments

The amortized cost, gross unrealized gains and losses and fair value of the investment portfolio at June 30, 2015 and December 31, 2014 are shown below.

June 30, 2015	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses (1)	Fair Value
	(In thousands)			
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$130,388	$ 1,959	$ (2,791)	$129,556
Obligations of U.S. states and political subdivisions	1,307,313	10,460	(10,913)	1,306,860
Corporate debt securities	2,292,817	6,538	(32,409)	2,266,946
Asset-backed securities	199,763	537	(33)	200,267
Residential mortgage-backed securities	297,207	265	(10,451)	287,021
Commercial mortgage-backed securities	263,967	336	(2,635)	261,668
Collateralized loan obligations	61,341	-	(658)	60,683
Debt securities issued by foreign sovereign governments	33,521	2,676	(151)	36,046
Total debt securities	4,586,317	22,771	(60,041)	4,549,047
Equity securities	3,042	36	(15)	3,063
Total investment portfolio	$4,589,359	$ 22,807	$ (60,056)	$4,552,110

December 31, 2014	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses (1)	Fair Value
	(In thousands)			
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$349,153	$ 2,752	$ (5,130)	$346,775
Obligations of U.S. states and political subdivisions	844,942	12,961	(2,761)	855,142
Corporate debt securities	2,418,991	16,325	(10,035)	2,425,281
Asset-backed securities	286,260	535	(140)	286,655
Residential mortgage-backed securities	329,983	254	(9,000)	321,237
Commercial mortgage-backed securities	276,215	1,221	(2,158)	275,278
Collateralized loan obligations	61,340	-	(1,264)	60,076
Debt securities issued by foreign sovereign governments	35,630	3,540	-	39,170
Total debt securities	4,602,514	37,588	(30,488)	4,609,614
Equity securities	3,003	61	(9)	3,055
Total investment portfolio	$4,605,517	$ 37,649	$ (30,497)	$4,612,669

(1) At June 30, 2015 and December 31, 2014, there were no other-than-temporary impairment losses recorded in other comprehensive income.

Our foreign investments primarily consist of the investment portfolio supporting our Australian domiciled subsidiary. This portfolio is comprised of Australian government and semi government securities, representing 86% of the market value of our foreign investments with the remainder invested in corporate securities and cash equivalents with allocations of 10% and 4%, respectively. Eighty-five percent of the Australian portfolio is rated AAA, by one or more of Moody's, Standard & Poor's and Fitch Ratings, and the remaining 15% is rated AA.

The amortized cost and fair values of debt securities at June 30, 2015, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Because most asset-backed and mortgage-backed securities and collateralized loan obligations provide for periodic payments throughout their lives, they are listed below in separate categories.

June 30, 2015	Amortized Cost	Fair Value
	(In thousands)	
Due in one year or less	$271,482	$272,149
Due after one year through five years	1,612,642	1,619,983
Due after five years through ten years	1,140,771	1,115,794
Due after ten years	739,144	731,482
	$3,764,039	$3,739,408
Asset-backed securities	199,763	200,267
Residential mortgage-backed securities	297,207	287,021
Commercial mortgage-backed securities	263,967	261,668
Collateralized loan obligations	61,341	60,683
Total at June 30, 2015	$4,586,317	$4,549,047

At June 30, 2015 and December 31, 2014, the investment portfolio had gross unrealized losses of $60.1 million and $30.5 million, respectively. For those securities in an unrealized loss position, the length of time the securities were in such a position, as measured by their month-end fair values, is as follows:

June 30, 2015	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or Greater Fair Value	12 Months or Greater Unrealized Losses	Total Fair Value	Total Unrealized Losses
	(In thousands)					
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$82,100	$ 1,096	$15,284	$ 1,695	$97,384	$ 2,791
Obligations of U.S. states and political subdivisions	525,293	9,733	51,076	1,180	576,369	10,913
Corporate debt securities	1,198,025	28,926	147,131	3,483	1,345,156	32,409
Asset-backed securities	46,789	21	7,696	12	54,485	33
Residential mortgage-backed securities	55,302	364	214,206	10,087	269,508	10,451
Commercial mortgage-backed securities	164,137	1,688	71,721	947	235,858	2,635
Collateralized loan obligations	-	-	60,683	658	60,683	658
Foreign government securities	2,446	151	-	-	2,446	151
Equity securities	351	6	173	9	524	15
Total	$2,074,443	$ 41,985	$567,970	$ 18,071	$2,642,413	$ 60,056

December 31, 2014	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or Greater Fair Value	12 Months or Greater Unrealized Losses	Total Fair Value	Total Unrealized Losses
	(In thousands)					
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$58,166	$ 138	$232,351	$ 4,992	$290,517	$ 5,130
Obligations of U.S. states and political subdivisions	166,408	1,066	114,465	1,695	280,873	2,761
Corporate debt securities	816,555	5,259	243,208	4,776	1,059,763	10,035
Asset-backed securities	54,491	80	11,895	60	66,386	140
Residential mortgage-backed securities	24,168	34	263,002	8,966	287,170	9,000
Commercial mortgage-backed securities	89,301	810	110,652	1,348	199,953	2,158
Collateralized loan obligations	-	-	60,076	1,264	60,076	1,264
Equity securities	167	1	235	8	402	9
Total	$1,209,256	$ 7,388	$1,035,884	$ 23,109	$2,245,140	$ 30,497

The unrealized losses in all categories of our investments at June 30, 2015 and December 31, 2014 were primarily caused by the difference in interest rates at each respective period, compared to interest rates at the time of purchase. There were 532 and 423 securities in an unrealized loss position at June 30, 2015 and December 31, 2014, respectively.

During each of the three and six months ended June 30, 2015 and 2014 there were no other-than-temporary impairments ("OTTI") recognized. The net realized investment gains (losses) on the investment portfolio are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands)			
Realized investment gains (losses) on investments:				
Fixed maturities	$161	$360	$26,485	$126
Equity securities	5	162	8	165
Net realized investment gains	$166	$522	$26,493	$291

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In thousands)			
Realized investment gains (losses) on investments:				
Gains on sales	$785	$1,307	$27,991	$2,112
Losses on sales	(619)	(785)	(1,498)	(1,821)
Net realized investment gains	$166	$522	$26,493	$291

Note 8 – Fair Value Measurements

In accordance with fair value guidance, we applied the following fair value hierarchy in order to measure fair value for assets and liabilities:

Level 1 – Quoted prices for identical instruments in active markets that we can access. Financial assets utilizing Level 1 inputs primarily include U.S. Treasury securities, equity securities, and Australian government and semi government securities.

Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and inputs, other than quoted prices, that are observable in the marketplace for the financial instrument. The observable inputs are used in valuation models to calculate the fair value of the financial instruments. Financial assets utilizing Level 2 inputs primarily include obligations of U.S. government corporations and agencies and certain municipal and corporate bonds.

Level 3 – Valuations derived from valuation techniques in which one or more significant inputs or value drivers are unobservable. Level 3 inputs reflect our own assumptions about the assumptions a market participant would use in pricing an asset or liability. Financial assets utilizing Level 3 inputs primarily include certain state premium tax credit investments. The state premium tax credit investments have an average maturity of less than 4 years, credit ratings of AA+ or higher, and their balance reflects their remaining scheduled payments discounted at an average annual rate of 7.2%. Our non-financial assets that are classified as Level 3 securities consist of real estate acquired through claim settlement. The fair value of real estate acquired is the lower of our acquisition cost or a percentage of the appraised value. The percentage applied to the appraised value is based upon our historical sales experience adjusted for current trends.

To determine the fair value of securities available-for-sale in Level 1 and Level 2 of the fair value hierarchy, independent pricing sources have been utilized. One price is provided per security based on observable market data. To ensure securities are appropriately classified in the fair value hierarchy, we review the pricing techniques and methodologies of the independent pricing sources and believe that their policies adequately consider market activity, either based on specific transactions for the issue valued or based on modeling of securities with similar credit quality, duration, yield and structure that were recently traded. A variety of inputs are utilized by the independent pricing sources including benchmark yields, reported trades, non-binding broker/dealer quotes, issuer spreads, two sided markets, benchmark securities, bids, offers and reference data including data published in market research publications. Inputs may be weighted differently for any security, and not all inputs are used for each security evaluation. Market indicators, industry and economic events are also considered. This information is evaluated using a multidimensional pricing model. Quality controls are performed by the independent pricing sources throughout this process, which include reviewing tolerance reports, trading information and data changes, and directional moves compared to market moves. This model combines all inputs to arrive at a value assigned to each security. In addition, on a quarterly basis, we perform quality controls over values received from the pricing sources which include reviewing tolerance reports, trading information and data changes, and directional moves compared to market moves. We have not made any adjustments to the prices obtained from the independent pricing sources.

Fair value measurements for assets measured at fair value included the following as of June 30, 2015 and December 31, 2014:

June 30, 2015	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$129,556	$26,271	$103,285	$ -
Obligations of U.S. states and political subdivisions	1,306,860	-	1,305,226	1,634
Corporate debt securities	2,266,946	-	2,266,946	-
Asset-backed securities	200,267	-	200,267	-
Residential mortgage-backed securities	287,021	-	287,021	-
Commercial mortgage-backed securities	261,668	-	261,668	-
Collateralized loan obligations	60,683	-	60,683	-
Debt securities issued by foreign sovereign governments	36,046	36,046	-	-
Total debt securities	4,549,047	62,317	4,485,096	1,634
Equity securities	3,063	2,742	-	321
Total investment portfolio	$4,552,110	$65,059	$4,485,096	$ 1,955
Real estate acquired (1)	$7,995	$-	$-	$ 7,995

December 31, 2014	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$346,775	$188,824	$157,951	$ -
Obligations of U.S. states and political subdivisions	855,142	-	853,296	1,846
Corporate debt securities	2,425,281	-	2,425,281	-
Asset-backed securities	286,655	-	286,655	-
Residential mortgage-backed securities	321,237	-	321,237	-
Commercial mortgage-backed securities	275,278	-	275,278	-
Collateralized loan obligations	60,076	-	60,076	-
Debt securities issued by foreign sovereign governments	39,170	39,170	-	-
Total debt securities	4,609,614	227,994	4,379,774	1,846
Equity securities	3,055	2,734	-	321
Total investment portfolio	$4,612,669	$230,728	$4,379,774	$ 2,167
Real estate acquired (1)	$12,658	$-	$-	$ 12,658

(1) Real estate acquired through claim settlement, which is held for sale, is reported in Other assets on the consolidated balance sheets.

There were no transfers of securities between Level 1 and Level 2 during the first six months of 2015.

For assets measured at fair value using significant unobservable inputs (Level 3), a reconciliation of the beginning and ending balances for the three and six months ended June 30, 2015 and 2014 is as follows:

	Debt Securities	Equity Securities	Total Investments	Real Estate Acquired
	(In thousands)			
Balance at March 31, 2015	$1,791	$ 321	$ 2,112	$ 10,897
Total realized/unrealized gains (losses):				
Included in earnings and reported as losses incurred, net	-	-	-	31
Purchases	-	-	-	5,917
Sales	(157)	-	(157)	(8,850)
Transfers into Level 3	-	-	-	-
Transfers out of Level 3	-	-	-	-
Balance at June 30, 2015	$1,634	$ 321	$ 1,955	$ 7,995
Amount of total losses included in earnings for the three months ended June 30, 2015 attributable to the change in unrealized losses on assets still held at June 30, 2015	$-	$ -	$ -	$ -

	Debt Securities	Equity Securities	Total Investments	Real Estate Acquired
	(In thousands)			
Balance at December 31, 2014	$1,846	$ 321	$ 2,167	$12,658
Total realized/unrealized gains (losses):				
Included in earnings and reported as losses incurred, net	-	-	-	(472)
Purchases	7	-	7	16,714
Sales	(219)	-	(219)	(20,905)
Transfers into Level 3	-	-	-	-
Transfers out of Level 3	-	-	-	-
Balance at June 30, 2015	$1,634	$ 321	$ 1,955	$7,995
Amount of total losses included in earnings for the six months ended June 30, 2015 attributable to the change in unrealized losses on assets still held at June 30, 2015	$-	$ -	$ -	$-

	Debt Securities	Equity Securities	Total Investments	Real Estate Acquired
	(In thousands)			
Balance at March 31, 2014	$2,378	$ 321	$ 2,699	$11,137
Total realized/unrealized gains (losses):				
Included in earnings and reported as losses incurred, net	-	-	-	(1,157)
Purchases	-	-	-	11,367
Sales	(147)	-	(147)	(10,543)
Transfers into Level 3	-	-	-	-
Transfers out of Level 3	-	-	-	-
Balance at June 30, 2014	$2,231	$ 321	$ 2,552	$10,804
Amount of total losses included in earnings for the three months ended June 30, 2014 attributable to the change in unrealized losses on assets still held at June 30, 2014	$-	$ -	$ -	$-

	Debt Securities	Equity Securities	Total Investments	Real Estate Acquired
	(In thousands)			
Balance at December 31, 2013	$2,423	$ 321	$ 2,744	$13,280
Total realized/unrealized gains (losses):				
Included in earnings and reported as losses incurred, net	-	-	-	(2,316)
Purchases	30	-	30	19,377
Sales	(222)	-	(222)	(19,537)
Transfers into Level 3	-	-	-	-
Transfers out of Level 3	-	-	-	-
Balance at June 30, 2014	$2,231	$ 321	$ 2,552	$10,804
Amount of total losses included in earnings for the six months ended June 30, 2014 attributable to the change in unrealized losses on assets still held at June 30, 2014	$-	$ -	$ -	$-

Authoritative guidance over disclosures about the fair value of financial instruments requires additional disclosure for financial instruments not measured at fair value. Certain financial instruments, including insurance contracts, are excluded from these fair value disclosure requirements. The carrying values of cash and cash equivalents (Level 1) and accrued investment income (Level 2) approximated their fair values.

Additional fair value disclosures related to our investment portfolio are included in Note 7 – "Investments."

We incur financial liabilities in the normal course of our business. The following tables present the carrying value and fair value of our financial liabilities disclosed, but not carried, at fair value at June 30, 2015 and December 31, 2014, and the level within the fair value hierarchy at which such liabilities are measured on a recurring basis.

June 30, 2015	Par Value	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)				
Financial liabilities:					
Senior Notes	$61,953	$62,689	$ -	$62,689	$ -
Convertible Senior Notes due 2017	345,000	394,521	-	394,521	-
Convertible Senior Notes due 2020	500,000	837,125	-	837,125	-
Convertible Junior Subordinated Debentures	389,522	512,186	-	512,186	-
Total Debt	$1,296,475	$1,806,521	$ -	$1,806,521	$ -

December 31, 2014	Par Value	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)				
Financial liabilities:					
Senior Notes	$61,953	$63,618	$ -	$63,618	$ -
Convertible Senior Notes due 2017	345,000	387,997	-	387,997	-
Convertible Senior Notes due 2020	500,000	735,075	-	735,075	-
Convertible Junior Subordinated Debentures	389,522	500,201	-	500,201	-
Total Debt	$1,296,475	$1,686,891	$ -	$1,686,891	$ -

The fair values of our Senior Notes, Convertible Senior Notes and Debentures were determined using available pricing for these debentures or similar instruments and are considered Level 2 securities.

Note 9 – Other Comprehensive Income

The pretax components of our other comprehensive income (loss) and the related income tax (expense) benefit for the three and six months ended June 30, 2015 and 2014 are included in the tables below.

	Three Months Ended June 30, 2015	2014
	(In thousands)	
Net unrealized holding (losses) gains arising during the period	$(64,118)	$44,818
Income tax benefit (expense)	22,362	(15,634)
Valuation allowance	(21,890)	15,317
Net of taxes	(63,646)	44,501
Net changes in benefit plan assets and obligations	(392)	(1,980)
Income tax benefit	137	693
Valuation allowance	(137)	(693)
Net of taxes	(392)	(1,980)
Net changes in unrealized foreign currency translation adjustment	598	904
Income tax expense	(208)	(317)
Net of taxes	390	587
Total other comprehensive income (loss)	(63,912)	43,742
Total income tax benefit (expense), net of valuation allowance	264	(634)
Total other comprehensive income (loss), net of tax	$(63,648)	$43,108

	Six Months Ended June 30, 2015	2014
	(In thousands)	
Net unrealized holding (losses) gains arising during the period	$(44,397)	$84,479
Income tax benefit (expense)	15,486	(29,505)
Valuation allowance	(15,172)	29,125
Net of taxes	(44,083)	84,099
Net changes in benefit plan assets and obligations	(1,092)	(3,466)
Income tax benefit	382	1,213
Valuation allowance	(382)	(1,213)
Net of taxes	(1,092)	(3,466)
Net changes in unrealized foreign currency translation adjustment	(2,504)	2,835
Income tax benefit (expense)	880	(995)
Net of taxes	(1,624)	1,840
Total other comprehensive income (loss)	(47,993)	83,848
Total income tax benefit (expense), net of valuation allowance	1,194	(1,375)
Total other comprehensive income (loss), net of tax	$(46,799)	$82,473

The pretax and related income tax (expense) benefit components of the amounts reclassified from our accumulated other comprehensive income to our consolidated statements of operations for the three and six months ended June 30, 2015 and 2014 are included in the tables below.

	Three Months Ended June 30,	
	2015	2014
	(In thousands)	
Reclassification adjustment for net realized gains (losses) included in net income	$477	$(1,896)
Income tax (expense) benefit	(161)	669
Valuation allowance	122	(699)
Net of taxes	438	(1,926)
Reclassification adjustment related to benefit plan assets and obligations	392	1,980
Income tax expense	(137)	(693)
Valuation allowance	137	693
Net of taxes	392	1,980
Total reclassifications	869	84
Total income tax expense, net of valuation allowance	(39)	(30)
Total reclassifications, net of tax	$830	$54

	Six Months Ended June 30,	
	2015	2014
	(In thousands)	
Reclassification adjustment for net realized gains (losses) included in net income	$11,711	$(4,885)
Income tax (expense) benefit	(4,092)	1,715
Valuation allowance	4,048	(1,745)
Net of taxes	11,667	(4,915)
Reclassification adjustment related to benefit plan assets and obligations	1,092	3,466
Income tax expense	(382)	(1,213)
Valuation allowance	382	1,213
Net of taxes	1,092	3,466
Total reclassifications	12,803	(1,419)
Total income tax expense, net of valuation allowance	(44)	(30)
Total reclassifications, net of tax	$12,759	$(1,449)

See Note 11 – “Income Taxes” for a discussion of the valuation allowance.

Changes in our accumulated other comprehensive loss (“AOCL”), including amounts reclassified from other comprehensive income (loss), for the six months ended June 30, 2015 are included in the table below.

	Six Months Ended June 30, 2015			
	Unrealized gains and losses on available-for-sale securities	Defined benefit plans	Foreign currency translation	Total accumulated other comprehensive income
	(In thousands)			
Balance at December 31, 2014, net of tax	$(57,551)	$(28,938)	$ 5,148	$ (81,341)
Other comprehensive loss before reclassifications	(32,416)	-	(1,624)	$ (34,040)
Less: Amounts reclassified from AOCL	11,667 (1)	1,092 (2)	-	$ 12,759
Balance at June 30, 2015, net of tax	$(101,634)	$(30,030)	$ 3,524	$ (128,140)

(1) Increases Net realized investment gains on the Consolidated Statements of Operations.
(2) Decreases Other underwriting and operating expenses, net on the Consolidated Statements of Operations.

Note 10 – Benefit Plans

The following table provides the components of net periodic benefit cost for the pension, supplemental executive retirement and other postretirement benefit plans:

	Three Months Ended June 30,			
	Pension and Supplemental Executive Retirement Plans		Other Postretirement Benefits	
	2015	2014	2015	2014
	(In thousands)			
Service cost	$2,680	$2,203	$214	$152
Interest cost	4,016	3,985	171	144
Expected return on plan assets	(5,259)	(5,257)	(1,247)	(1,163)
Recognized net actuarial loss (gain)	1,533	250	(53)	(144)
Amortization of prior service cost	(211)	(423)	(1,663)	(1,662)
Net periodic benefit cost (benefit)	$2,759	$758	$(2,578)	$(2,673)

	Six Months Ended June 30,			
	Pension and Supplemental Executive Retirement Plans		Other Postretirement Benefits	
	2015	2014	2015	2014
	(In thousands)			
Service cost	$5,128	$4,283	$416	$329
Interest cost	7,924	7,994	349	327
Expected return on plan assets	(10,554)	(10,515)	(2,495)	(2,324)
Recognized net actuarial loss (gain)	2,742	541	(88)	(217)
Amortization of prior service cost	(422)	(465)	(3,325)	(3,325)
Net periodic benefit cost (benefit)	$4,818	$1,838	$(5,143)	$(5,210)

We currently intend to make a contribution of $17 million to our qualified pension plan and supplemental executive retirement plan in 2015.

Note 11 – Income Taxes

Valuation Allowance

We review the need to maintain the deferred tax asset valuation allowance on a quarterly basis. We analyze several factors, among which are the severity and frequency of operating losses, our capacity for the carryback or carryforward of any losses, the existence and current level of taxable operating income, operating results, on a three year cumulative basis, the expected occurrence of future income or loss, the expiration dates of the carryforwards, the cyclical nature of our operating results, and available tax planning strategies. Based on our analysis, we continue to reduce our benefit from income tax through the recognition of a valuation allowance.

It is reasonably possible that the valuation allowance will be reversed in the foreseeable future. Specifically, if we continue to recognize meaningful levels of sustainable pre-tax income, it is likely that the valuation allowance will be reversed in 2015. Currently, our analysis of the severity of previous operating losses shows, on a three year cumulative basis, a loss from operations, adjusted for permanent tax differences, which is considered to be unfavorable evidence with respect to the realization of deferred tax assets and is difficult to overcome with projections of future results. As a result of this analysis, and consideration of other factors, we concluded that it was appropriate to maintain the valuation allowance at this time. In the period in which the valuation allowance is reversed, we would recognize a tax benefit which will increase our earnings for that period. In future years with taxable income, after the valuation allowance has been reversed and until such time as our net operating loss carryforwards are exhausted or expired, our provision for income tax would substantially exceed the amount of cash tax payments.

The effect of the change in valuation allowance on the provision for income taxes was as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
	(In thousands)			
Provision for income tax	$39,991	$17,172	$87,874	$40,292
Change in valuation allowance	(38,669)	(16,054)	(83,167)	(38,448)
Provision for income taxes	$1,322	$1,118	$4,707	$1,844

The change in the valuation allowance that was included in other comprehensive income for the three months ended June 30, 2015 and 2014 was an increase of $22.0 million and a decrease of $14.6 million, respectively. The change in the valuation allowance that was included in other comprehensive income for the six months ended June 30, 2015 and 2014 was an increase of $15.6 million and a decrease of $27.9 million, respectively. The total valuation allowance as of June 30, 2015 and December 31, 2014 was $834.7 million and $902.3 million, respectively.

We have approximately $2.2 billion of net operating loss carryforwards on a regular tax basis and $1.3 billion of net operating loss carryforwards for computing the alternative minimum tax as of June 30, 2015. Any unutilized carryforwards are scheduled to expire at the end of tax years 2029 through 2033.

Tax Contingencies

As previously disclosed, the Internal Revenue Service ("IRS") completed examinations of our federal income tax returns for the years 2000 through 2007 and issued proposed assessments for taxes, interest and penalties related to our treatment of the flow-through income and loss from an investment in a portfolio of residual interests of Real Estate Mortgage Investment Conduits ("REMICs"). The IRS indicated that it did not believe that, for various reasons, we had established sufficient tax basis in the REMIC residual interests to deduct the losses from taxable income. We appealed these assessments within the IRS and in August 2010, we reached a tentative settlement agreement with the IRS which was not finalized.

On September 10, 2014, we received Notices of Deficiency (commonly referred to as "90 day letters") covering the 2000-2007 tax years. The Notices of Deficiency reflect taxes and penalties related to the REMIC matters of $197.5 million and at June 30, 2015, there would also be interest related to these matters of approximately $175.5 million. In 2007, we made a payment of $65.2 million to the United States Department of the Treasury which will reduce any amounts we would ultimately owe. The Notices of Deficiency also reflect additional amounts due of $261.4 million, which are primarily associated with the disallowance of the carryback of the 2009 net operating loss to the 2004-2007 tax years. We believe the IRS included the carryback adjustments as a precaution to keep open the statute of limitations on collection of the tax that was refunded when this loss was carried back, and not because the IRS actually intends to disallow the carryback permanently.

We filed a petition with the U.S. Tax Court contesting most of the IRS' proposed adjustments reflected in the Notices of Deficiency and the IRS has filed an answer to our petition which continues to assert their claim. Litigation to resolve our dispute with the IRS could be lengthy and costly in terms of legal fees and related expenses. We can provide no assurance regarding the outcome of any such litigation or whether a compromised settlement with the IRS will ultimately be reached and finalized. Depending on the outcome of this matter, additional state income taxes and state interest may become due when a final resolution is reached. As of June 30, 2015, those state taxes and interest would approximate $48.1 million. In addition, there could also be state tax penalties. Our total amount of unrecognized tax benefits as of June 30, 2015 is $106.7 million, which represents the tax benefits generated by the REMIC portfolio included in our tax returns that we have not taken benefit for in our financial statements, including any related interest. We continue to believe that our previously recorded tax provisions and liabilities are appropriate. However, we would need to make appropriate adjustments, which could be material, to our tax provision and liabilities if our view of the probability of success in this matter changes, and the ultimate resolution of this matter could have a material negative impact on our effective tax rate, results of operations, cash flows, available assets and statutory capital. In this regard, see Note 1 – "Nature of Business – Capital-GSEs."

In October 2014, we received a Revenue Agent's Report from the IRS related to the examination of our federal income tax returns for the years 2011 and 2012. The result of the examination had no material effect on the financial statements.

The total amount of the unrecognized tax benefits, related to our aforementioned REMIC issue that would affect our effective tax rate is $94.1 million, after taking into account the effect of NOL carrybacks. We recognize interest accrued and penalties related to unrecognized tax benefits in income taxes. As of June 30, 2015 and December 31, 2014, we had accrued $27.4 million and $26.9 million, respectively, for the payment of interest.

Note 12 – Loss Reserves

We establish reserves to recognize the estimated liability for losses and loss adjustment expenses ("LAE") related to defaults on insured mortgage loans. Loss reserves are established by estimating the number of loans in our inventory of delinquent loans that will result in a claim payment, which is referred to as the claim rate, and further estimating the amount of the claim payment, which is referred to as claim severity.

Estimation of losses is inherently judgmental. The conditions that affect the claim rate and claim severity include the current and future state of the domestic economy, including unemployment, and the current and future strength of local housing markets. The actual amount of the claim payments may be substantially different than our loss reserve estimates. Our estimates could be adversely affected by several factors, including a deterioration of regional or national economic conditions, including unemployment, leading to a reduction in borrower income and thus their ability to make mortgage payments, and a drop in housing values which may affect borrower willingness to continue to make mortgage payments when the value of the home is below the mortgage balance. Changes to our estimates could result in a material impact to our results of operations and capital position, even in a stable economic environment.

The following table provides a reconciliation of beginning and ending loss reserves for the six months ended June 30, 2015 and 2014:

	Six months ended June 30,	
	2015	2014
	(In thousands)	
Reserve at beginning of period	$2,396,807	$3,061,401
Less reinsurance recoverable	57,841	64,085
Net reserve at beginning of period	2,338,966	2,997,316