

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**FORM 10-Q**

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(Mark One)

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

**1934**

For the quarterly period ended March 31, 2014

OR

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

**1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-11356

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**Radian Group Inc.**

(Exact name of registrant as specified in its charter)

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**Delaware**

(State or other jurisdiction of incorporation or organization)

**23-2691170**

(I.R.S. Employer Identification No.)

**1601 Market Street, Philadelphia, PA**

(Address of principal executive offices)

**19103**

(Zip Code)

**(215) 231-1000**

(Registrant's telephone number, including area code)

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

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

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

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

(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

**APPLICABLE ONLY TO CORPORATE ISSUERS:**

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 173,171,885 shares of common stock, \$0.001 par value per share, outstanding on April 29, 2014.

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### Cautionary Note Regarding Forward Looking Statements—Safe Harbor Provisions

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” within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934 and the United States (“U.S.”) Private Securities Litigation Reform Act of 1995. In most cases, forward-looking statements may be identified by words such as “anticipate,” “may,” “will,” “could,” “should,” “would,” “expect,” “intend,” “plan,” “goal,” “contemplate,” “believe,” “estimate,” “predict,” “project,” “potential,” “continue,” “seek,” “strategy,” “future,” “likely” or the negative or other variations on these words and other similar expressions. These statements, which may include, without limitation, projections regarding our future performance and financial condition, are made on the basis of management’s current views and assumptions with respect to future events. Any forward-looking statement is not a guarantee of future performance and actual results could differ materially from those contained in the forward-looking statement. These statements speak only as of the date they were made, and we undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. We operate in a changing environment. New risks emerge from time to time and it is not possible for us to predict all risks that may affect us. The forward-looking statements, as well as our prospects as a whole, are subject to risks and uncertainties that could cause actual results to differ materially from those set forth in the forward-looking statements including:

- changes in general economic and political conditions, including unemployment rates, changes in the U.S. housing and mortgage credit markets (including declines in home prices and property values), the performance of the U.S. or global economies, the amount of liquidity in the capital or credit markets, changes or volatility in interest rates or consumer confidence and changes in credit spreads, all of which may be impacted by, among other things, legislative activity or inactivity, actual or threatened downgrades of U.S. government credit ratings, or actual or threatened defaults on U.S. government obligations;
- changes in the way customers, investors, regulators or legislators perceive the strength of private mortgage insurers or financial guaranty providers, in particular in light of the fact that certain of our former competitors have ceased writing new insurance business and have been placed under supervision or receivership by insurance regulators;
- catastrophic events, municipal and sovereign or sub-sovereign bankruptcy filings or other economic changes in geographic regions where our mortgage insurance exposure is more concentrated or where we have financial guaranty exposure;
- our ability to maintain sufficient holding company liquidity to meet our short- and long-term liquidity needs;
- a reduction in, or prolonged period of depressed levels of, home mortgage originations due to reduced liquidity in the lending market, tighter underwriting standards, or general reduced housing demand in the U.S., which may be exacerbated by regulations impacting home mortgage originations, including requirements established under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”);
- our ability to maintain an adequate risk-to-capital position, minimum policyholder position and other surplus requirements for Radian Guaranty Inc. (“Radian Guaranty”), our principal mortgage insurance subsidiary, and an adequate minimum policyholder position and surplus for our insurance subsidiaries that provide reinsurance or capital support to Radian Guaranty;
- our ability to continue to effectively mitigate our mortgage insurance and financial guaranty losses;
- a more rapid than expected decrease in the levels of mortgage insurance rescissions and claim denials, which have reduced our paid losses and resulted in a significant reduction in our loss reserves, including a decrease in net rescissions or denials resulting from an increase in the number of successful challenges to previously rescinded policies or claim denials (including as part of one or more settlements of disputed rescissions or denials), or by Fannie Mae or Freddie Mac (the “Government-Sponsored Enterprises” or the “GSEs”) intervening in or otherwise limiting our loss mitigation practices, including settlements of disputes regarding loss mitigation activities;
- the negative impact that our loss mitigation activities may have on our relationships with our customers and potential customers, including the potential loss of current or future business and the heightened risk of disputes and litigation;

- the need, in the event that we are unsuccessful in defending our loss mitigation activities, to increase our loss reserves for, and reassume risk on, rescinded or cancelled loans or denied claims, and to pay additional claims, including amounts previously curtailed;
- any disruption in the servicing of mortgages covered by our insurance policies, as well as poor servicer performance;
- adverse changes in the severity or frequency of losses associated with certain products that we formerly offered (and which remain a small part of our insured portfolio) that are riskier than traditional mortgage insurance or financial guaranty insurance policies;
- a substantial decrease in the persistency rates of our mortgage insurance policies, which has the effect of reducing our premium income on our monthly premium policies and could decrease the profitability of our mortgage insurance business;
- heightened competition for our mortgage insurance business from others such as the Federal Housing Administration, the U.S. Department of Veterans Affairs and other private mortgage insurers, including with respect to other private mortgage insurers, those that have been assigned higher ratings than we have, that may have access to greater amounts of capital than we do, that are less dependent on capital support from their subsidiaries than we are or that are new entrants to the industry, and therefore, are not burdened by legacy obligations;
- changes in requirements for Radian Guaranty to remain an eligible insurer to the GSEs (which are expected to be released in draft form for public comment as early as the second quarter of 2014, and to become effective following an implementation period), which may include, among other items, more onerous risk-to-capital ratio requirements, capital requirements based on a variety of risk characteristics and measures of credit quality and a limitation on the amount of capital credit available for Radian Guaranty's equity in its subsidiaries, including capital attributable to our financial guaranty business; the form of the new eligibility requirements and the timeframe for their implementation remain uncertain, and we cannot give any assurances as to their potential impact on us;
- changes in the charters or business practices of, or rules or regulations applicable to, the GSEs;
- changes to the current system of housing finance, including the possibility of a new system in which private mortgage insurers are not required or their products are significantly limited in effect or scope;
- the effect of the Dodd-Frank Act on the financial services industry in general, and on our mortgage insurance and financial guaranty businesses in particular, including whether and to what extent loans with private mortgage insurance may be considered "qualified residential mortgages" for purposes of the Dodd-Frank Act securitization provisions;
- the application of existing federal or state laws and regulations, or changes in these laws and regulations or the way they are interpreted, including, without limitation: (i) the resolution of existing, or the possibility of additional, lawsuits or investigations (including in particular investigations and litigation relating to captive reinsurance arrangements under the Real Estate Settlement Procedures Act of 1974); (ii) changes to the Mortgage Guaranty Insurers Model Act (the "Model Act") being considered by the National Association of Insurance Commissioners ("NAIC") that could include more stringent capital and other requirements for Radian Guaranty in states that adopt the new Model Act in the future; and (iii) legislative and regulatory changes (a) impacting the demand for private mortgage insurance, (b) limiting or restricting the products we may offer or increasing the amount of capital we are required to hold, (c) affecting the form in which we execute credit protection, or (d) otherwise impacting our existing businesses or future prospects;
- the amount and timing of potential payments or adjustments associated with federal or other tax examinations, including adjustments proposed by the Internal Revenue Service resulting from the examination of our 2000 through 2007 tax years, which we are currently contesting;
- the possibility that we may fail to estimate accurately the likelihood, magnitude and timing of losses in connection with establishing loss reserves for our mortgage insurance or financial guaranty businesses, or to estimate accurately the fair value amounts of derivative instruments in determining gains and losses on these instruments;

- volatility in our earnings caused by changes in the fair value of our assets and liabilities carried at fair value, including our derivative instruments, substantially all of our investment portfolio and certain of our long-term incentive compensation awards;
- our ability to realize some or all of the tax benefits associated with our gross deferred tax assets, which will depend, in part, on our ability to generate sufficient sustainable taxable income in future periods;
- changes in accounting principles generally accepted in the United States of America or statutory accounting principles, rules and guidance, or their interpretation;
- legal and other limitations on amounts we may receive from our subsidiaries as dividends or through our tax- and expense-sharing arrangements with our subsidiaries; and
- our pending acquisition of Clayton Holdings LLC (“Clayton”), including: the potential to not fully realize the benefits anticipated from the acquisition, or to not realize such benefits during the anticipated time frame, including as a result of a loss of customers and/or employees; the potential inability to successfully integrate Clayton’s business with our business or the inability to complete such integration during the anticipated time frame; the inability or decision to not complete the acquisition, or to not complete the acquisition on a timely basis; the potential distraction of management time and attention; the risk that we are not able to finance the acquisition as anticipated, or that, if the financing efforts are successful, we are not able to utilize the funds raised efficiently in the event that we do not complete the acquisition.

For more information regarding these risks and uncertainties as well as certain additional risks that we face, you should refer to the Risk Factors detailed in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2013, Item 1A of Part II of this Quarterly Report on Form 10-Q and subsequent reports and registration statements filed from time to time with the U.S. Securities and Exchange Commission. We caution you not to place undue reliance on these forward-looking statements, which are current only as of the date on which we issued this report.

PART I

Radian Group Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	March 31, 2014	December 31, 2013
<b>(\$ in thousands, except share and per share amounts)</b>		
<b>ASSETS</b>		
Investments		
Fixed-maturities held to maturity—at amortized cost (fair value \$50 and \$351)	\$ 50	\$ 358
Fixed-maturities available for sale—at fair value (amortized cost \$212,734 and \$120,385)	213,989	120,553
Equity securities available for sale—at fair value (cost \$78,106 and \$78,106)	137,920	135,168
Trading securities—at fair value	2,728,976	3,117,429
Short-term investments—at fair value	1,649,228	1,429,228
Other invested assets—including variable interest entity (“VIE”) assets at fair value of \$81,635 and \$81,000)	128,416	128,421
Total investments	4,858,579	4,931,157
Cash	20,963	23,858
Restricted cash	22,366	22,527
Deferred policy acquisition costs	63,708	66,926
Accrued investment income	27,690	30,264
Accounts and notes receivable	75,072	75,106
Property and equipment, at cost (less accumulated depreciation of \$102,436 and \$101,625)	12,482	10,516
Derivative assets	14,466	16,642
Deferred income taxes, net	—	17,902
Reinsurance recoverables	31,033	46,846
Other assets (including VIE other assets of \$92,594 and \$92,023)	402,626	379,947
Total assets	\$ 5,528,985	\$ 5,621,691
<b>LIABILITIES AND STOCKHOLDERS’ EQUITY</b>		
Unearned premiums	\$ 774,788	\$ 768,871
Reserve for losses and loss adjustment expenses (“LAE”)	1,923,711	2,185,421
Long-term debt	938,390	930,072
VIE debt—at fair value	95,580	94,645
Derivative liabilities (including VIE derivative liabilities of \$47,769 and \$68,457)	257,717	307,185
Other liabilities (including VIE accounts payable of \$190 and \$254)	392,216	395,852
Total liabilities	4,382,402	4,682,046
Commitments and Contingencies (Note 15)		
Equity component of currently redeemable convertible senior notes (Note 10)	91,016	—
Stockholders’ equity		
Common stock: par value \$.001 per share; 485,000,000 shares authorized at March 31, 2014 and December 31, 2013; 190,712,673 and 190,636,972 shares issued at March 31, 2014 and December 31, 2013, respectively; 173,166,892 and 173,099,515 shares outstanding at March 31, 2014 and December 31, 2013, respectively	191	191
Treasury stock, at cost: 17,545,781 and 17,537,457 shares at March 31, 2014 and December 31, 2013, respectively	(892,937)	(892,807)
Additional paid-in capital	2,256,436	2,347,104
Retained deficit	(349,467)	(552,226)
Accumulated other comprehensive income	41,344	37,383
Total stockholders’ equity	1,055,567	939,645
Total liabilities and stockholders’ equity	\$ 5,528,985	\$ 5,621,691

See Notes to Unaudited Condensed Consolidated Financial Statements.

**Radian Group Inc.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)**

<b>(\$ in thousands, except per share amounts)</b>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Revenues:</b>		
Premiums written—insurance:		
Direct	\$ 229,322	\$ 245,467
Assumed	473	(10,397)
Ceded	(16,089)	(27,885)
Net premiums written	213,706	207,185
Increase in unearned premiums	(8,041)	(14,597)
Net premiums earned—insurance	205,665	192,588
Net investment income	24,229	26,873
Net gains (losses) on investments	64,451	(5,505)
Change in fair value of derivative instruments	50,086	(167,670)
Net gains (losses) on other financial instruments	698	(5,675)
Other income	1,127	1,771
Total revenues	346,256	42,382
<b>Expenses:</b>		
Provision for losses	54,809	132,059
Change in premium deficiency reserve (“PDR”)	466	(629)
Policy acquisition costs	8,614	17,195
Other operating expenses	59,909	80,100
Interest expense	19,927	15,881
Total expenses	143,725	244,606
Equity in net (loss) income of affiliates	(13)	1
Pretax income (loss)	202,518	(202,223)
Income tax benefit	(241)	(14,723)
Net income (loss)	\$ 202,759	\$ (187,500)
Basic net income (loss) per share	\$ 1.17	\$ (1.30)
Diluted net income (loss) per share	\$ 0.94	\$ (1.30)
Weighted-average number of common shares outstanding—basic	173,165	144,355
Weighted-average number of common and common equivalent shares outstanding—diluted	222,668	144,355
Dividends per share	\$ 0.0025	\$ 0.0025

See Notes to Unaudited Condensed Consolidated Financial Statements.



**Radian Group Inc.**

**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)**

<u>(In thousands)</u>	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
Net income (loss)	<u>\$ 202,759</u>	<u>\$ (187,500)</u>
Other comprehensive income, net of tax (see Note 11):		
Unrealized gains on investments:		
Unrealized holding gains arising during the period	4,485	7,466
Less: Reclassification adjustment for net gains included in net income (loss)	524	21
Net unrealized gains on investments	<u>3,961</u>	<u>7,445</u>
Other comprehensive income	<u>3,961</u>	<u>7,445</u>
Comprehensive income (loss)	<u>\$ 206,720</u>	<u>\$ (180,055)</u>

See Notes to Unaudited Condensed Consolidated Financial Statements.

**Radian Group Inc.**

**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN COMMON STOCKHOLDERS' EQUITY (UNAUDITED)**

<u>(In thousands)</u>	Common Stock		Treasury Stock		Additional Paid-in Capital		Retained Deficit		Accumulated Other Comprehensive Income		Total	
BALANCE, JANUARY 1, 2013	\$	151	\$	(892,094)	\$	1,967,414	\$	(355,241)	\$	16,095	\$	736,325
Net loss		—		—		—		(187,500)		—		(187,500)
Net unrealized gain on investments, net of tax		—		—		—		—		7,445		7,445
Issuance of common stock - stock offering		39		—		299,503		—		—		299,542
Issuance of common stock under benefit plans		—		—		271		—		—		271
Issuance of common stock under incentive plans		—		—		62		—		—		62
Amortization of restricted stock		—		—		208		—		—		208
Issuance of convertible debt		—		—		77,026		—		—		77,026
Stock-based compensation expense, net		—		—		(1,999)		—		—		(1,999)
Dividends declared		—		—		(334)		—		—		(334)
<b>BALANCE, MARCH 31, 2013</b>	<b>\$</b>	<b>190</b>	<b>\$</b>	<b>(892,094)</b>	<b>\$</b>	<b>2,342,151</b>	<b>\$</b>	<b>(542,741)</b>	<b>\$</b>	<b>23,540</b>	<b>\$</b>	<b>931,046</b>
BALANCE, JANUARY 1, 2014	\$	191	\$	(892,807)	\$	2,347,104	\$	(552,226)	\$	37,383	\$	939,645
Net income		—		—		—		202,759		—		202,759
Net unrealized gain on investments, net of tax		—		—		—		—		3,961		3,961
Repurchases of common stock under incentive plans		—		(130)		—		—		—		(130)
Issuance of common stock under benefit plans		—		—		458		—		—		458
Issuance of common stock under incentive plans		—		—		13		—		—		13
Amortization of restricted stock		—		—		459		—		—		459
Stock-based compensation expense, net		—		—		(149)		—		—		(149)
Reclassification to equity component of currently redeemable convertible senior notes		—		—		(91,016)		—		—		(91,016)
Dividends declared		—		—		(433)		—		—		(433)
<b>BALANCE, MARCH 31, 2014</b>	<b>\$</b>	<b>191</b>	<b>\$</b>	<b>(892,937)</b>	<b>\$</b>	<b>2,256,436</b>	<b>\$</b>	<b>(349,467)</b>	<b>\$</b>	<b>41,344</b>	<b>\$</b>	<b>1,055,567</b>

See Notes to Unaudited Condensed Consolidated Financial Statements.

**Radian Group Inc.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

<u>(In thousands)</u>	Three Months Ended March 31,	
	2014	2013
Cash flows used in operating activities	\$ (137,010)	\$ (165,971)
<b>Cash flows from investing activities:</b>		
Proceeds from sales of fixed-maturity investments available for sale	13,230	1,102
Proceeds from sales of trading securities	444,967	380,030
Proceeds from redemptions of fixed-maturity investments available for sale	1,540	2,035
Proceeds from redemptions of fixed-maturity investments held to maturity	300	255
Purchases of fixed-maturity investments available for sale	(103,506)	—
Purchases of trading securities	—	(232,538)
Purchases of short-term investments, net	(219,943)	(589,799)
Sales of other assets, net	640	2,005
Purchases of property and equipment, net	(2,776)	(362)
Net cash provided by (used in) investing activities	134,452	(437,272)
<b>Cash flows from financing activities:</b>		
Dividends paid	(433)	(334)
Proceeds/payments related to issuance or exchange of debt, net	—	381,165
Redemption of long-term debt	—	(79,372)
Issuance of common stock	—	299,542
Excess tax benefits from stock-based awards	89	50
Net cash (used in) provided by financing activities	(344)	601,051
Effect of exchange rate changes on cash	7	(29)
Decrease in cash	(2,895)	(2,221)
Cash, beginning of period	23,858	31,555
Cash, end of period	\$ 20,963	\$ 29,334
<b>Supplemental disclosures of cash flow information:</b>		
Income taxes paid (received)	\$ 1,508	\$ (1,983)
Interest paid	\$ 4,520	\$ 3,630

See Notes to Unaudited Condensed Consolidated Financial Statements.

## **Radian Group Inc.**

### **Notes to Unaudited Condensed Consolidated Financial Statements**

#### **1. Condensed Consolidated Financial Statements—Basis of Presentation and Business Overview**

Our condensed consolidated financial statements include the accounts of Radian Group Inc. and its subsidiaries. We refer to Radian Group Inc. together with its consolidated subsidiaries as “Radian,” the “Company,” “we,” “us” or “our,” unless the context requires otherwise. We generally refer to Radian Group Inc. alone, without its consolidated subsidiaries, as “Radian Group.”

Our condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and include the accounts of all wholly-owned subsidiaries. Companies in which we, or one of our subsidiaries, exercise significant influence (generally ownership interests ranging from 20% to 50%), are accounted for in accordance with the equity method of accounting. VIEs for which we are the primary beneficiary are consolidated, as described in Note 5. All intercompany accounts and transactions, and intercompany profits and losses, have been eliminated. We have condensed or omitted certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with GAAP pursuant to the instructions set forth in Article 10 of Regulation S-X of the United States (“U.S.”) Securities and Exchange Commission.

The financial information presented for interim periods is unaudited; however, such information reflects all adjustments that are, in the opinion of management, necessary for the fair statement of the financial position, results of operations, comprehensive income and cash flows for the interim periods presented. Such adjustments are of a normal recurring nature. These interim financial statements should be read in conjunction with the audited financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013 (the “2013 Form 10-K”). The results of operations for interim periods are not necessarily indicative of results to be expected for the full year or for any other period. The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. While the amounts included in our condensed consolidated financial statements include our best estimates and assumptions, actual results may vary materially.

In July 2013, the Financial Accounting Standards Board (“FASB”) issued an update to the accounting standard regarding income taxes. This update provides guidance concerning the balance sheet presentation of an unrecognized tax benefit when a net operating loss carryforward or a tax credit carryforward (the “Carryforwards”) is available. This accounting standard requires an entity to net its liability related to unrecognized tax benefits against the related deferred tax assets for the Carryforwards. A gross presentation will be required when the Carryforwards are not available under the tax law of the applicable jurisdiction or when the Carryforwards would not be used by the entity to settle any additional income taxes resulting from disallowance of the uncertain tax position. This update is effective for fiscal years and interim periods within such years beginning after December 15, 2013. We adopted this update in the first quarter of 2014. As a result of our implementation of this new FASB guidance, our March 31, 2014 condensed consolidated balance sheet reflects a full valuation allowance against our deferred tax assets (“DTAs”) as our remaining DTA was reduced by the reclassification of our liability for unrecognized tax benefits. The adoption of this update did not affect the recognition or measurement of uncertain tax positions and did not have a significant impact on our consolidated financial statements or disclosures. See Note 12 for additional information.

#### **Business Overview**

We are a credit enhancement company with a primary strategic focus on domestic, residential mortgage insurance on first-lien mortgage loans (“first-liens”). We have two operating business segments—mortgage insurance and financial guaranty.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

***Mortgage Insurance***

Our mortgage insurance segment provides credit-related insurance coverage, principally through private mortgage insurance, and risk management services to mortgage lending institutions. We provide these products and services mainly through our wholly-owned subsidiary, Radian Guaranty Inc. (“Radian Guaranty”). Private mortgage insurance protects mortgage lenders from all or a portion of default-related losses on residential mortgage loans made to home buyers who generally make down payments of less than 20% of the home’s purchase price. Private mortgage insurance also facilitates the sale of these mortgage loans in the secondary mortgage market, most of which are sold to Freddie Mac and Fannie Mae. We refer to Freddie Mac and Fannie Mae together as “Government-Sponsored Enterprises” or “GSEs.”

Our mortgage insurance segment offers primary mortgage insurance coverage on residential first-liens. At March 31, 2014, primary insurance on first-liens comprised approximately 96.0% of our \$42.1 billion total direct risk in force (“RIF”). In the past, we also wrote pool insurance, which at March 31, 2014, comprised approximately 3.8% of our total direct RIF. Additionally, we offered other forms of credit enhancement on residential mortgage assets. These products included mortgage insurance on second-lien mortgages (“second-lien”), credit enhancement on net interest margin securities (“NIMS”), and primary mortgage insurance on international mortgages (collectively, we refer to the risk associated with these transactions as “non-traditional”). Our non-traditional RIF was \$93.0 million as of March 31, 2014, representing less than 1% of our total direct RIF.

***Financial Guaranty***

Our financial guaranty segment has provided direct insurance and reinsurance on credit-based risks through Radian Asset Assurance Inc. (“Radian Asset Assurance”), our principal financial guaranty subsidiary. Radian Asset Assurance is a wholly-owned subsidiary of Radian Guaranty, which has allowed our financial guaranty business to serve as an important source of capital for Radian Guaranty and our mortgage insurance business. We have provided financial guaranty credit protection in several forms, including through the issuance of financial guaranty policies, by insuring the obligations under one or more credit default swaps (“CDS”) and through the reinsurance of both types of obligations. While we discontinued writing new financial guaranty business in 2008, we continue to provide financial guaranty insurance on our existing portfolio consisting primarily of public finance and structured finance insured transactions. We have continued to reduce our financial guaranty exposures in order to mitigate uncertainty, maximize the ultimate capital and liquidity available for our mortgage insurance business and accelerate access to that capital and liquidity through transactions such as risk commutations, ceded reinsurance, discounted insured bond purchases and transaction settlements and terminations.

***Business Conditions***

As a seller of credit protection, our results are subject to macroeconomic conditions and specific events that impact the origination environment and the credit performance of our underlying insured assets. The financial crisis and the downturn in the housing and related credit markets that began in 2007 has had a significant negative impact on the operating environment and results of operations for both of our business segments. This was characterized by a decrease in mortgage originations, a broad decline in home prices, mortgage servicing and foreclosure delays, and ongoing deterioration in the credit performance of mortgage and other assets originated prior to 2009, together with macroeconomic factors such as high unemployment, limited employment growth, limited economic growth and a lack of meaningful liquidity in many sectors of the capital markets. More recently, we have experienced a period of economic recovery and the operating environment for our businesses has improved. Our results of operations have continued to improve as the negative impact from losses on the mortgage insurance we wrote during the poor underwriting years of 2005 through 2008 (we refer to this portion of our mortgage insurance portfolio, together with business written prior to 2005, as our “legacy portfolio”) has been reduced and we continue to write insurance on higher credit quality loans. As of March 31, 2014, our legacy portfolio had been reduced to approximately 38% of our total primary RIF, while insurance on loans written after 2008 constituted approximately 62% of our primary RIF.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Although the U.S. economy and certain housing markets remain weak compared to historical standards, home prices have been appreciating on a broad basis throughout the U.S., foreclosure activity has declined and the credit quality of recent mortgage market originations continues to be significantly better than the credit quality of our legacy portfolio. In addition, although the economic recovery has been sluggish, there are signs of a broader recovery in the U.S. economy, including importantly, a reduction in unemployment rates. As a consequence of these and other factors, in the first quarter of 2014 we have experienced improvement in our results of operations, driven primarily by a significant reduction in our incurred losses as a result of an 18.4% decline in new primary mortgage insurance defaults compared to the first quarter of 2013 and by other positive default and claim developments.

Currently, our business strategy is primarily focused on: (1) growing our mortgage insurance business by writing insurance on high-quality mortgages in the U.S.; (2) pursuing other potential alternatives for providing credit-related services to the mortgage finance market, such as expanding our presence in the mortgage finance market through our agreement to acquire Clayton Holdings, LLC (“Clayton”) referred to below; (3) continuing to manage losses in our legacy mortgage insurance and financial guaranty portfolios; (4) continuing to reduce our legacy mortgage insurance and financial guaranty exposures; and (5) continuing to effectively manage our capital and liquidity positions.

Our businesses also are significantly impacted by, and our future success may be dependent upon, legislative and regulatory developments impacting the housing finance industry. The Federal Housing Administration (“FHA”) remains our primary competitor outside of the private mortgage insurance industry. The GSEs’ current federal charters generally prohibit them from purchasing any mortgage with a loan amount that exceeds 80% of a home’s value, unless that mortgage is insured by a qualified mortgage insurer, or the mortgage seller retains at least a 10% participation in the loan or agrees to repurchase the loan in the event of a default. As a result, high loan-to-value (“LTV”) mortgages purchased by the GSEs generally are insured with private mortgage insurance. Changes in the charters or business practices of the GSEs, including the introduction of alternatives to private mortgage insurance as a condition to purchasing high-LTV loans, could reduce the number of mortgages they purchase that are insured by us and consequently diminish our franchise value.

The GSEs are in the process of revising their eligibility requirements for mortgage insurers. We expect the GSEs to release the new requirements for public comment as early as the second quarter of 2014 and for these new requirements to become effective following an implementation period. Among other changes, the new GSE eligibility requirements are expected to contain new capital adequacy standards for private mortgage insurers that are more onerous than the capital requirements that are currently in effect, including potentially: (i) a risk-to-capital ratio (defined below) below Radian Guaranty’s 19.2 to 1 risk-to-capital ratio as of March 31, 2014; (ii) capital requirements based on a variety of risk characteristics and measures of credit quality; and (iii) a limitation on the amount of capital credit available for subsidiary capital (including Radian Guaranty’s capital that is attributable to its ownership of Radian Asset Assurance). The form of the new eligibility requirements and the timeframe for their implementation remain uncertain. If the new GSE eligibility requirements include more onerous capital requirements, including any one or more of the potential requirements referenced above, we may need to provide additional capital support to, or arrange additional capital relief for, Radian Guaranty, including potentially, entering into new reinsurance arrangements, increasing the amount of capital contributions from our available holding company funds or seeking to raise funds in private or public capital transactions.

Under state insurance regulations, Radian Guaranty is required to maintain minimum surplus levels and, in certain states, a minimum ratio of statutory capital relative to the level of net RIF, or “risk-to-capital.” Sixteen states (the “RBC States”) currently impose a statutory or regulatory risk-based capital requirement (the “Statutory RBC Requirement”). The most common Statutory RBC Requirement is that a mortgage insurer’s risk-to-capital ratio may not exceed 25 to 1. In certain of the RBC States there is a Statutory RBC Requirement that the mortgage insurer must maintain a minimum policyholder position, which is calculated based on both risk and surplus levels (the “MPP Requirement”). The statutory capital requirements for the non-RBC States are de minimis (ranging from \$1 million to \$5 million); however, the insurance laws of these states generally grant broad supervisory powers to state agencies or officials to enforce rules or exercise discretion affecting almost every significant aspect of the insurance business, including the power to revoke or restrict an insurance company’s ability to write new business. Unless an RBC State grants a waiver or other form of relief, if a mortgage insurer is not in compliance with the Statutory RBC Requirement of such state, that mortgage insurer may be prohibited from writing new mortgage insurance business in that state. Radian Guaranty’s domiciliary state, Pennsylvania, is not one of the RBC States. As of March 31, 2014, Radian Guaranty was in compliance with all applicable Statutory RBC Requirements.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

***Capital and Liquidity***

Since the financial crisis that began in 2007, we have engaged in a number of strategic actions and initiatives in response to the negative economic and market conditions impacting our businesses. These actions include the following:

- We significantly tightened our mortgage insurance underwriting standards to focus primarily on insuring high credit quality first-liens originated in the U.S. and we ceased writing mortgage insurance on non-traditional and other inherently riskier products.
- We expanded our claims management and loss mitigation efforts to better manage losses in the weak housing market and high default and claim environment.
- We discontinued writing new financial guaranty business and Radian Group contributed its ownership interest in Radian Asset Assurance to Radian Guaranty. Although this structure makes the capital adequacy of our mortgage insurance business dependent, to a significant degree, on the successful run-off of our financial guaranty business, the structure has provided Radian Guaranty with substantial regulatory capital and, through dividends from Radian Asset Assurance, has increased liquidity at Radian Guaranty.
- We reduced our legacy mortgage insurance portfolio, non-traditional mortgage insurance RIF and our financial guaranty portfolio through risk commutations, discounted security purchases, ceded reinsurance, discounted insured bond purchases and transaction settlements and terminations.

Additionally, consistent with our strategy, we are currently pursuing the following initiative:

- Since Radian Asset Assurance ceased writing new business in June 2008, Radian Asset Assurance has reduced its aggregate net par exposure by approximately 80% to \$22.7 billion as of March 31, 2014. This reduction included large declines in many of the riskier segments of Radian Asset Assurance's insured portfolio. In light of this risk reduction and the significant level of capital, including \$1.2 billion of statutory surplus remaining at Radian Asset Assurance, Radian Asset Assurance submitted a request to the New York State Department of Financial Services ("NYSDFS") seeking permission to pay an extraordinary dividend to Radian Guaranty. The NYSDFS currently is considering this request and there can be no assurance if and when such request will be granted in whole or in part, and if granted, that it will not be subject to material conditions.

On May 6, 2014, Radian Group entered into a Unit Purchase Agreement (the "Purchase Agreement") to purchase all of the outstanding equity interests in Clayton for aggregate cash consideration of \$305 million. In connection with the acquisition, we plan to raise the aggregate cash consideration by seeking financing through the issuance of debt and equity. See Note 17 for additional information.

Radian Group currently has immediately available, either directly or through an unregulated subsidiary, unrestricted cash and liquid investments of approximately \$615 million. This amount excludes certain additional cash and liquid investments that have been advanced from our subsidiaries for corporate expenses and interest payments. Substantially all of Radian Group's obligations to pay corporate expenses and interest payments on outstanding debt are reimbursed to Radian Group through the expense-sharing arrangements currently in place with its subsidiaries. Currently, we expect to maintain Radian Guaranty's risk-to-capital ratio at or below 20 to 1. However, we expect this target level may change upon the modification of GSE eligibility requirements or future changes in applicable regulatory requirements.

**2. Segment Reporting**

Our mortgage insurance and financial guaranty segments are strategic business units that are managed separately. We allocate corporate income and expenses to our mortgage insurance and financial guaranty segments based on either an allocated percentage of time spent on each segment or internally allocated capital, which is based on the relative GAAP equity of each segment. We allocate corporate cash and investments to our segments based on internally allocated capital. The results for each segment for each reporting period can cause significant volatility in internally allocated capital based on relative GAAP equity, which can impact the allocations of income and expenses to our segments.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

*Adjusted Pretax Operating Income (Loss)*

Our senior management, including our Chief Executive Officer (our chief operating decision maker), uses adjusted pretax operating income (loss) as our primary measure to facilitate evaluation of the fundamental financial performance of the Company's business segments and to allocate resources to the segments. Adjusted pretax operating income (loss) is defined as pretax income (loss) excluding the effects of net gains (losses) on investments and other financial instruments and net impairment losses recognized in earnings. It also excludes gains and losses related to changes in fair value estimates on insured credit derivatives and includes the impact of changes in the present value of insurance claims and recoveries on insured credit derivatives, based on our ongoing insurance loss monitoring, as well as premiums earned on insured credit derivatives. Management's use of this measure as its primary measure to evaluate segment performance began with the quarter ended March 31, 2014. Accordingly, for comparison purposes, we also present the applicable measures from the corresponding period of 2013 on a basis consistent with the current year presentation.

Although adjusted pretax operating income (loss) excludes certain items that have occurred in the past and are expected to occur in the future, the excluded items represent those that are: (1) not viewed as part of the operating performance of our primary activities; or (2) not expected to result in an economic impact equal to the amount reflected in pretax income (loss). These adjustments, along with the reasons for their treatment, are described below.

- (1) *Change in fair value of derivative instruments*. Gains and losses related to changes in the fair value of insured credit derivatives are subject to significant fluctuation based on changes in interest rates, credit spreads (of both the underlying collateral as well as our credit spread), credit ratings and other market, asset-class and transaction-specific conditions and factors that may be unrelated or only indirectly related to our obligation to pay future claims. With the exception of the estimated present value of net credit (losses) recoveries incurred and net premiums earned on derivatives, discussed in items 2 and 3 below, we believe these gains and losses will reverse over time and consequently these changes are not expected to result in economic gains or losses. Therefore, these gains and losses are excluded from our calculation of adjusted pretax operating income (loss).
- (2) *Estimated present value of net credit (losses) recoveries incurred*. The change in present value of insurance claims we expect to pay or recover on insured credit derivatives represents the amount of the change in credit derivatives from item 1 above, that we expect to result in an economic loss or recovery based on our ongoing loss monitoring analytics. Therefore, this item is expected to have an economic impact and is included in our calculation of adjusted pretax operating income (loss). Also included in this item is the expected recovery of miscellaneous operating expenses associated with our consolidated VIEs.
- (3) *Net premiums earned on derivatives*. The net premiums earned on insured credit derivatives are classified as part of the change in fair value of derivative instruments discussed in item 1 above. However, since net premiums earned on derivatives are considered part of our fundamental operating activities, these premiums are included in our calculation of adjusted pretax operating income (loss).
- (4) *Net gains (losses) on investments and other financial instruments*. The recognition of realized investment gains or losses can vary significantly across periods as the activity is highly discretionary based on the timing of individual securities sales due to such factors as market opportunities, our tax and capital profile and overall market cycles. Unrealized investment gains and losses arise primarily from changes in the market value of our investments that are classified as trading. These valuation adjustments may not necessarily result in economic gains or losses. We do not view them to be indicative of our fundamental operating activities. Trends in the profitability of our fundamental operating activities can be more clearly identified without the fluctuations of these realized and unrealized gains or losses. Therefore, these items are excluded from our calculation of adjusted pretax operating income (loss).
- (5) *Net impairment losses recognized in earnings*. The recognition of net impairment losses on investments can vary significantly in both size and timing, depending on market credit cycles. We do not view them to be indicative of our fundamental operating activities. Therefore, these losses are excluded from our calculation of adjusted pretax operating income (loss).



**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Summarized financial information concerning our operating segments as of and for the periods indicated, is as follows:

<u>(In thousands)</u>	Three Months Ended March 31, 2014		
	Mortgage Insurance	Financial Guaranty	Total
Net premiums written—insurance	\$ 212,953	\$ 753	\$ 213,706
Net premiums earned—insurance	\$ 198,762	\$ 6,903	\$ 205,665
Net premiums earned on derivatives	—	3,445	3,445
Net investment income	14,021	10,208	24,229
Other income	1,057	70	1,127
Total revenues	213,840	20,626	234,466
Provision for losses	49,159	5,650	54,809
Estimated present value of net credit losses (recoveries) incurred	139	(501)	(362)
Change in PDR	466	—	466
Policy acquisition costs	7,017	1,597	8,614
Other operating expenses	50,358	9,551	59,909
Interest expense	5,372	14,555	19,927
Total expenses	112,511	30,852	143,363
Equity in net loss of affiliates	—	(13)	(13)
Adjusted pretax operating income (loss)	\$ 101,329	\$ (10,239)	\$ 91,090
Cash and investments	\$ 2,735,809	\$ 2,166,099	\$ 4,901,908
Deferred policy acquisition costs	27,870	35,838	63,708
Total assets	3,136,537	2,392,448	5,528,985
Unearned premiums	580,453	194,335	774,788
Reserve for losses and LAE	1,893,960	29,751	1,923,711
VIE debt	3,144	92,436	95,580
Derivative liabilities	—	257,717	257,717
New Insurance Written (“NIW”) (in millions)	\$ 6,808		

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**Three Months Ended March 31, 2013**

<b>(In thousands)</b>	<b>Mortgage Insurance</b>	<b>Financial Guaranty</b>	<b>Total</b>
Net premiums written—insurance	\$ 217,286	\$ (10,101)	\$ 207,185
Net premiums earned—insurance	\$ 182,992	\$ 9,596	\$ 192,588
Net premiums earned on derivatives	—	4,992	4,992
Net investment income	15,102	11,771	26,873
Other income	1,712	59	1,771
Total revenues	199,806	26,418	226,224
Provision for losses	131,956	103	132,059
Estimated present value of net credit recoveries incurred	(299)	(2,845)	(3,144)
Change in PDR	(629)	—	(629)
Policy acquisition costs	11,732	5,463	17,195
Other operating expenses	65,780	14,320	80,100
Interest expense	2,669	13,212	15,881
Total expenses	211,209	30,253	241,462
Equity in net income of affiliates	—	1	1
Adjusted pretax operating loss	\$ (11,403)	\$ (3,834)	\$ (15,237)
Cash and investments	\$ 3,186,871	\$ 2,486,017	\$ 5,672,888
Deferred policy acquisition costs	29,920	44,681	74,601
Total assets	3,663,552	2,707,397	6,370,949
Unearned premiums	428,574	245,275	673,849
Reserve for losses and LAE	2,894,500	24,573	2,919,073
VIE debt	11,062	96,339	107,401
Derivative liabilities	—	430,898	430,898
NIW (in millions)	\$ 10,906		

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The reconciliation of adjusted pretax operating income (loss) to consolidated pretax income (loss) and consolidated net income (loss) is as follows:

	Three Months Ended March 31,	
	2014	2013
Adjusted pretax operating income (loss):		
Mortgage insurance	\$ 101,329	\$ (11,403)
Financial guaranty	(10,239)	(3,834)
Total adjusted pretax operating income (loss)	<u>\$ 91,090</u>	<u>\$ (15,237)</u>
Change in fair value of derivative instruments	50,086	(167,670)
Less: Estimated present value of net credit recoveries incurred	362	3,144
Less: Net premiums earned on derivatives	3,445	4,992
Change in fair value of derivative instruments expected to reverse over time	<u>46,279</u>	<u>(175,806)</u>
Net gains (losses) on investments	64,451	(5,505)
Net gains (losses) on other financial instruments	698	(5,675)
Consolidated pretax income (loss)	<u>202,518</u>	<u>(202,223)</u>
Income tax benefit	(241)	(14,723)
Consolidated net income (loss)	<u>\$ 202,759</u>	<u>\$ (187,500)</u>

On a consolidated basis, “adjusted pretax operating income (loss)” is a measure not determined in accordance with GAAP. Total adjusted pretax operating income (loss) is not a measure of total profitability, and therefore should not be viewed as a substitute for GAAP pretax income (loss). Our definition of adjusted pretax operating income (loss) may not be comparable to similarly-named measures reported by other companies.

### 3. Derivative Instruments

We provide a significant portion of our credit protection within our financial guaranty segment in the form of CDS, which are accounted for as derivatives. Derivative instruments are recorded at fair value and changes in fair value are recorded as such in the condensed consolidated statement of operations. All of our derivative instruments are recognized in our condensed consolidated balance sheets as either derivative assets or derivative liabilities. In many of our CDS transactions, primarily our corporate collateralized debt obligations (“CDOs”), we are required to make payments to our counterparty above a specified level of subordination, upon the occurrence of credit events related to the borrowings or bankruptcy of obligors contained within pools of corporate obligations or, in the case of pools of mortgage or other asset-backed obligations, upon the occurrence of credit events related to the specific obligations in the pool. When we provide a CDS as credit protection on a specific obligation, we generally guarantee the full and timely payment of principal and interest when due on such obligation. These derivatives have various maturity dates, but the majority of the net par outstanding of our remaining insured CDS transactions, including all of our corporate CDOs, mature within four years.

We recorded premiums and origination costs related to our CDS and certain other derivative contracts in change in fair value of derivative instruments and policy acquisition costs, respectively, on our condensed consolidated statements of operations. Our classification of these contracts is the same whether we are a direct insurer or we reinsure these contracts.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following table sets forth our gross unrealized gains and gross unrealized losses on derivative assets and liabilities as of the dates indicated. Certain contracts are in an asset position because the net present value of the contractual premium we receive exceeds the net present value of our estimate of the expected future premiums that a financial guarantor of similar credit quality to us would charge to provide the same credit protection, assuming a transfer of our obligation to such financial guarantor as of the measurement date.

<u>(In thousands)</u>	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
<b>Balance Sheets</b>		
Derivative assets:		
Financial Guaranty credit derivative assets	\$ 5,638	\$ 6,323
Fixed-maturity derivative assets	8,828	10,319
Total derivative assets	<u>14,466</u>	<u>16,642</u>
Derivative liabilities:		
Financial Guaranty credit derivative liabilities	209,948	238,728
Financial Guaranty VIE derivative liabilities	47,769	68,457
Total derivative liabilities	<u>257,717</u>	<u>307,185</u>
Total derivative liabilities, net	<u>\$ 243,251</u>	<u>\$ 290,543</u>

The notional value of our derivative contracts at March 31, 2014 and December 31, 2013 was \$11.4 billion and \$12.3 billion, respectively.

The components of the gains (losses) included in change in fair value of derivative instruments are as follows:

<u>(In thousands)</u>	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
<b>Statements of Operations</b>		
Net premiums earned—derivatives	\$ 3,445	\$ 4,992
Financial Guaranty credit derivatives	28,016	(175,724)
Financial Guaranty VIE derivatives	20,117	3,062
Other derivatives	(1,492)	—
Change in fair value of derivative instruments	<u>\$ 50,086</u>	<u>\$ (167,670)</u>

The valuation of derivative instruments may result in significant volatility from period to period in gains and losses as reported on our condensed consolidated statements of operations. Generally, these gains and losses result, in part, from changes in corporate credit or asset-backed spreads and changes in the market's perception of the creditworthiness of any: (i) underlying corporate entities; (ii) assets underlying asset-backed securities ("ABS"); or (iii) primary obligors of obligations for which we provide second-to-pay credit protection. Additionally, when determining the fair value of our liabilities, we are required to incorporate into the fair value of those liabilities an adjustment that reflects our own non-performance risk, and consequently, changes in the market's perception of our non-performance risk can also result in gains and losses on our derivative instruments. Any incurred gains or losses (which include any claim payments) on our financial guaranty contracts that are accounted for as derivatives are recognized as a change in fair value of derivative instruments. Because our fair value determinations for derivative and other financial instruments are based on assumptions and estimates that are inherently subject to risk and uncertainty, the fair value amounts could vary significantly from period to period. See Note 4 for information on the fair value of our financial instruments.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following table shows selected information about our derivative contracts:

(\$ in thousands)	March 31, 2014		
	Number of Contracts	Par/ Notional Exposure	Total Net Asset (Liability)
<b>Product</b>			
Corporate CDOs	17	\$ 6,957,838	\$ (2,457)
Non-Corporate CDOs and other derivative transactions:			
Trust preferred securities (“TruPs”)	13	956,989	(30,202)
CDOs of commercial mortgage-backed securities (“CMBS”)	3	1,381,000	(56,312)
Other:			
Structured finance	4	500,950	(75,691)
Public finance	21	1,278,666	(31,096)
Total Non-Corporate CDOs and other derivative transactions	41	4,117,605	(193,301)
Assumed financial guaranty credit derivatives:			
Structured finance	26	156,168	(8,151)
Public finance	4	90,197	(401)
Total Assumed	30	246,365	(8,552)
Financial Guaranty VIE derivative liabilities (1)	1	78,575	(47,769)
Other (2)	1	—	8,828
<b>Grand Total</b>	90	\$ 11,400,383	\$ (243,251)

(1) Represents the fair value of a CDS included in a VIE that we have consolidated.

(2) Represents derivative assets related to other purchased derivatives for which we do not have loss exposure that exceeds our net asset amount.

#### 4. Fair Value of Financial Instruments

Certain assets and liabilities are recorded at fair value. These include: available for sale securities, trading securities, VIE debt, derivative instruments, and certain other assets. All derivative instruments are recognized in our condensed consolidated balance sheets as either derivative assets or derivative liabilities. All changes in fair value of trading securities, VIE debt, derivative instruments, and certain other assets are included in our condensed consolidated statements of operations. All changes in the fair value of available for sale securities are recorded in accumulated other comprehensive income (loss).

Our estimated fair value measurements are intended to reflect the assumptions market participants would use in pricing an asset or liability based on the best information available. Assumptions include the risks inherent in a particular valuation technique (such as a pricing model) and the risks inherent in the inputs to the model. Changes in economic conditions and capital market conditions, including but not limited to, credit spread changes, benchmark interest rate changes, market volatility and changes in the value of underlying collateral or of any third-party guaranty or insurance, could cause actual results to differ materially from our estimated fair value measurements. We define fair value as the current amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In the event that our investments or derivative contracts were sold, commuted, terminated or settled with a counterparty or transferred in a forced liquidation, the amounts received or paid may be materially different from those determined in accordance with the accounting standard regarding fair value measurements. Differences may also arise between our recorded fair value and the settlement or termination value with a counterparty based upon consideration of information that may not be available to another market participant. Those differences, which may be material, are recorded as realized gains/(losses) in our condensed consolidated statements of operations in the period in which the transaction occurs. There were no significant changes to our fair value methodologies during the three months ended March 31, 2014.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

When determining the fair value of our liabilities, we are required to incorporate into the fair value of those liabilities an adjustment that reflects our own non-performance risk. Our five-year CDS spread is an observable quantitative measure of our non-performance risk and is used by typical market participants to determine the likelihood of our default; the CDS spread actually used in the valuation of specific fair value liabilities is typically based on the remaining term of the insured obligation. Assuming all other factors are held constant, as our CDS spread tightens or widens, it has the effect of increasing or decreasing, respectively, the fair value of our liabilities with a corresponding impact on our results of operations.

In accordance with GAAP, we established a three-level valuation hierarchy for disclosure of fair value measurements based on the transparency of inputs to the valuation of an asset or liability as of the measurement date. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level I measurements) and the lowest priority to unobservable inputs (Level III measurements). The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the measurement in its entirety. The three levels of the fair value hierarchy are described below:

- Level I — Unadjusted quoted prices for identical assets or liabilities in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level II — Prices or valuations based on observable inputs other than quoted prices in active markets for identical assets and liabilities; and
- Level III — Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable. Level III inputs are used to measure fair value only to the extent that observable inputs are not available.

The level of market activity used to determine the fair value hierarchy is based on the availability of observable inputs market participants would use to price an asset or a liability, including market value price observations. We provide a qualitative description of the valuation techniques and inputs used for Level II recurring and non-recurring fair value measurements in our audited annual financial statements as of December 31, 2013. For a complete understanding of those valuation techniques and inputs used as of March 31, 2014, these unaudited condensed consolidated financial statements should be read in conjunction with the audited annual financial statements and notes thereto included in our 2013 Form 10-K.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following is a list of those assets and liabilities that are measured at fair value by hierarchy level as of March 31, 2014:

<u>(In millions)</u>	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
<b>Assets and Liabilities at Fair Value</b>				
Investment Portfolio:				
U.S. government and agency securities	\$ 980.0	\$ 370.9	\$ —	\$ 1,350.9
State and municipal obligations	—	619.0	19.1	638.1
Money market instruments	639.5	—	—	639.5
Corporate bonds and notes	—	1,026.0	—	1,026.0
Residential mortgage-backed securities (“RMBS”)	—	282.4	—	282.4
CMBS	—	282.6	—	282.6
Other ABS	—	234.4	—	234.4
Foreign government and agency securities	—	46.7	—	46.7
Equity securities (1)	130.0	96.4	0.4	226.8
Other investments (2)	—	2.2	82.1	84.3
<b>Total Investments at Fair Value (3)</b>	<b>1,749.5</b>	<b>2,960.6</b>	<b>101.6</b>	<b>4,811.7</b>
Derivative assets	—	8.8	5.6	14.4
Other assets (4)	—	—	92.5	92.5
<b>Total Assets at Fair Value</b>	<b>\$ 1,749.5</b>	<b>\$ 2,969.4</b>	<b>\$ 199.7</b>	<b>\$ 4,918.6</b>
Derivative liabilities	\$ —	\$ —	\$ 257.7	\$ 257.7
VIE debt (5)	—	—	95.6	95.6
<b>Total Liabilities at Fair Value</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 353.3</b>	<b>\$ 353.3</b>

- (1) Comprising broadly diversified domestic equity mutual funds included within Level I and various preferred and common stocks invested across numerous companies and industries included within Levels II and III.
- (2) Comprising TruPs (\$0.6 million) and short-term certificates of deposit (“CDs”) (\$1.6 million) included within Level II and lottery annuities (\$0.3 million), TruPs (\$0.2 million), and a guaranteed investment contract held by a consolidated VIE (\$81.6 million) within Level III.
- (3) Does not include fixed-maturities held to maturity (\$0.1 million) and certain other invested assets (\$46.8 million), primarily invested in limited partnerships, accounted for as cost-method investments and not measured at fair value.
- (4) Primarily comprising manufactured housing loan collateral related to two consolidated financial guaranty VIEs.
- (5) Comprising consolidated debt related to NIMS VIEs (\$3.1 million) and financial guaranty VIEs (\$92.5 million).

At March 31, 2014, our total Level III assets were approximately 4.1% of total assets measured at fair value and total Level III liabilities accounted for 100% of total liabilities measured at fair value. Realized and unrealized gains and losses on Level III assets and liabilities in the rollforward represent gains and losses for the periods in which they were classified as Level III.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following is a list of those assets and liabilities that are measured at fair value by hierarchy level as of December 31, 2013:

<u>(In millions)</u>	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Total</u>
<b>Assets and Liabilities at Fair Value</b>				
Investment Portfolio:				
U.S. government and agency securities	\$ 755.0	\$ 402.9	\$ —	\$ 1,157.9
State and municipal obligations	—	602.3	18.7	621.0
Money market instruments	672.6	—	—	672.6
Corporate bonds and notes	—	1,036.6	—	1,036.6
RMBS	—	560.4	—	560.4
CMBS	—	288.9	—	288.9
Other ABS	—	194.9	0.9	195.8
Foreign government and agency securities	—	40.7	—	40.7
Equity securities (1)	128.3	97.1	0.4	225.8
Other investments (2)	—	2.2	81.5	83.7
<b>Total Investments at Fair Value (3)</b>	<b>1,555.9</b>	<b>3,226.0</b>	<b>101.5</b>	<b>4,883.4</b>
Derivative assets	—	10.3	6.3	16.6
Other assets (4)	—	—	91.9	91.9
<b>Total Assets at Fair Value</b>	<b>\$ 1,555.9</b>	<b>\$ 3,236.3</b>	<b>\$ 199.7</b>	<b>\$ 4,991.9</b>
Derivative liabilities	\$ —	\$ —	\$ 307.2	\$ 307.2
VIE debt (5)	—	—	94.6	94.6
<b>Total Liabilities at Fair Value</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 401.8</b>	<b>\$ 401.8</b>

- (1) Comprising broadly diversified domestic equity mutual funds included within Level I and various preferred and common stocks invested across numerous companies and industries included within Levels II and III.
- (2) Comprising TruPs (\$0.6 million) and short-term CDs (\$1.6 million) included within Level II and lottery annuities (\$0.3 million), TruPs (\$0.2 million), and a guaranteed investment contract held by a consolidated VIE (\$81.0 million) within Level III.
- (3) Does not include fixed-maturities held to maturity (\$0.4 million) and certain other invested assets (\$47.4 million), primarily invested in limited partnerships, accounted for as cost-method investments and not measured at fair value.
- (4) Primarily comprising manufactured housing loan collateral related to two consolidated financial guaranty VIEs.
- (5) Comprising consolidated debt related to NIMS VIEs (\$2.8 million) and financial guaranty VIEs (\$91.8 million).

At December 31, 2013, our total Level III assets approximated 4.0% of total assets measured at fair value and our total Level III liabilities accounted for 100% of total liabilities measured at fair value. Realized and unrealized gains and losses on Level III assets and liabilities in the rollforward represent gains and losses for the periods in which they were classified as Level III.



**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following tables quantify the estimated impact of our non-performance risk on our derivative assets, derivative liabilities and net VIE liabilities (in aggregate by type) presented in our condensed consolidated balance sheets as of the dates indicated:

<u>(In basis points)</u>	March 31, 2014	December 31, 2013	March 31, 2013	December 31, 2012
Radian Group's five-year CDS spread	288	323	513	913

<u>(In millions)</u>	Fair Value Liability before Consideration of Radian Non- Performance Risk March 31, 2014	Impact of Radian Non-Performance Risk March 31, 2014	Fair Value Liability Recorded March 31, 2014
<b>Product</b>			
Corporate CDOs	\$ 26.0	\$ 23.5	\$ 2.5
Non-Corporate CDO-related (1)	357.6	155.7	201.9
NIMS-related (2)	5.2	2.1	3.1
Total	<u>\$ 388.8</u>	<u>\$ 181.3</u>	<u>\$ 207.5</u>

<u>(In millions)</u>	Fair Value Liability before Consideration of Radian Non- Performance Risk December 31, 2013	Impact of Radian Non-Performance Risk December 31, 2013	Fair Value Liability Recorded December 31, 2013
<b>Product</b>			
Corporate CDOs	\$ 30.4	\$ 29.0	\$ 1.4
Non-Corporate CDO-related (1)	409.7	178.7	231.0
NIMS-related (2)	5.0	2.2	2.8
Total	<u>\$ 445.1</u>	<u>\$ 209.9</u>	<u>\$ 235.2</u>

- (1) Includes the net fair value liability recorded within derivative assets and derivative liabilities and the net fair value liabilities included in our consolidated VIEs.
- (2) Includes NIMS VIE debt.

Non-performance risk is commonly measured by default probability, with a credit spread tightening indicating a lesser probability of default. Radian Group's five-year CDS spread at March 31, 2014 implies a market view that there is a 21.1% probability that Radian Group will default in the next five years as compared to a 22.9% implied probability of default at December 31, 2013. The cumulative impact on our derivative assets, derivative liabilities and VIE liabilities attributable to the market's perception of our non-performance risk decreased by \$28.6 million during the first three months of 2014, as presented in the tables above. This decrease was in part due to the decrease in net derivative liabilities outstanding, as well as the market's perception of the lower probability that Radian Group may default.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following is a rollforward of Level III assets and liabilities measured at fair value for the quarter ended March 31, 2014:

<u>(In millions)</u>	<u>Beginning Balance at January 1, 2014</u>	<u>Realized and Unrealized Gains (Losses) Recorded in Earnings (1)</u>	<u>Purchases</u>	<u>Sales</u>	<u>Issuances</u>	<u>Settlements</u>	<u>Transfers Into (Out of) Level III (2)</u>	<u>Ending Balance at March 31, 2014</u>
<b>Investments:</b>								
State and municipal obligations	\$ 18.7	\$ 0.4	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 19.1
Other ABS	0.9	—	—	—	—	0.4	(0.5)	—
Equity securities	0.4	—	—	—	—	—	—	0.4
Other investments	81.5	0.6	—	—	—	—	—	82.1
Total Level III Investments	101.5	1.0	—	—	—	0.4	(0.5)	101.6
Other assets	91.9	5.8	—	—	—	5.2	—	92.5
Total Level III Assets	<u>\$ 193.4</u>	<u>\$ 6.8</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 5.6</u>	<u>\$ (0.5)</u>	<u>\$ 194.1</u>
Derivative liabilities, net	\$ 300.9	\$ 52.2	\$ —	\$ —	\$ —	\$ (3.4)	\$ —	\$ 252.1
VIE debt	94.6	(5.1)	—	—	—	4.1	—	95.6
Total Level III Liabilities, net	<u>\$ 395.5</u>	<u>\$ 47.1</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 0.7</u>	<u>\$ —</u>	<u>\$ 347.7</u>

(1) Includes unrealized gains (losses) relating to assets and liabilities still held as of March 31, 2014 as follows: \$0.2 million for other investments, \$3.6 million for other assets, \$48.6 million for derivative liabilities and \$(4.4) million for VIE debt.

(2) Transfers are recognized at the end of the period as the availability of market observed inputs change from period to period.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following is a rollforward of Level III assets and liabilities measured at fair value for the quarter ended March 31, 2013:

<u>(In millions)</u>	<b>Beginning Balance at January 1, 2013</b>	<b>Realized and Unrealized Gains (Losses) Recorded in Earnings (1)</b>	<b>Purchases</b>	<b>Sales</b>	<b>Issuances</b>	<b>Settlements</b>	<b>Transfers Into (Out of) Level III (2)</b>	<b>Ending Balance at March 31, 2013</b>
<b>Investments:</b>								
State and municipal obligations	\$ 19.0	\$ 0.2	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 19.2
Corporate bonds and notes	—	—	2.7	—	—	—	—	2.7
CMBS	—	—	3.1	—	—	—	—	3.1
Other ABS	1.7	—	—	—	—	0.2	—	1.5
Equity securities	1.0	—	—	0.6	—	—	—	0.4
Other investments	79.0	(1.6)	0.4	0.1	—	0.4	—	77.3
<b>Total Level III Investments</b>	<b>100.7</b>	<b>(1.4)</b>	<b>6.2</b>	<b>0.7</b>	<b>—</b>	<b>0.6</b>	<b>—</b>	<b>104.2</b>
NIMS derivative assets	1.6	—	—	—	—	—	—	1.6
Other assets	99.2	3.3	—	—	—	6.0	—	96.5
<b>Total Level III Assets</b>	<b>\$ 201.5</b>	<b>\$ 1.9</b>	<b>\$ 6.2</b>	<b>\$ 0.7</b>	<b>\$ —</b>	<b>\$ 6.6</b>	<b>\$ —</b>	<b>\$ 202.3</b>
Derivative liabilities, net	\$ 254.9	\$ (167.7)	\$ —	\$ —	\$ —	\$ (3.5)	\$ —	\$ 426.1
VIE debt	108.9	(3.3)	—	—	—	4.8	—	107.4
<b>Total Level III Liabilities, net</b>	<b>\$ 363.8</b>	<b>\$ (171.0)</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 1.3</b>	<b>\$ —</b>	<b>\$ 533.5</b>

- (1) Includes unrealized gains (losses) relating to assets and liabilities still held as of March 31, 2013 as follows: \$(1.5) million for investments, \$0.8 million for other assets, \$(172.6) million for derivative liabilities and \$(2.5) million for VIE debt.
- (2) Transfers are recognized at the end of the period as the availability of market observed inputs change from period to period.

There were no transfers between Level I and Level II for the quarters ended March 31, 2014 or 2013.

For markets in which inputs are not observable or limited, we use significant judgment and assumptions that a typical market participant would use to evaluate the market price of an asset or liability. Given the level of judgment necessary, another market participant may derive a materially different estimate of fair value. These assets and liabilities are classified in Level III of our fair value hierarchy. For fair value measurements categorized within Level III of the fair value hierarchy, we use certain significant unobservable inputs in estimating fair value. Those inputs primarily relate to the probability of default, the expected loss upon default and our own non-performance risk as it relates to our liabilities.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following table summarizes the significant unobservable inputs used in our recurring Level III fair value measurements as of March 31, 2014:

<u>(In millions)</u>	<b>Fair Value Net Asset (Liability) March 31, 2014</b>	<b>Valuation Technique</b>	<b>Unobservable Input</b>	<b>Range/ Weighted Average</b>
<u>(1)</u>	<u>(1)</u>			
<b>Level III Assets/Liabilities:</b>				
State and municipal obligations	\$ 19.1	Discounted cash flow	Discount rate	12.3%
			Expected loss	11.1%
Other investments	81.6	Discounted cash flow	Discount rate	1.0%
Corporate CDOs	(2.5)	Base correlation model	Radian correlation to corporate index	85.0%
			Average credit spread	0.1% - 0.9%
			Own credit spread (2)	0.9% - 3.8%
CDOs of CMBS	(56.3)	Discounted cash flow	Radian correlation to CMBS transaction index	72.0% - 85.0%
			Own credit spread (2)	0.9% - 3.8%
TruPs CDOs	(30.2)	Discounted cash flow	Principal recovery	75.0%
			Principal recovery (stressed)	65.0%
			Probability of conditional liquidity payment	0.2% - 10.0%
			Own credit spread (2)	0.9% - 3.8%
TruPs - related VIE	(47.8)	Discounted cash flow	Discount rate	8.8%
Other non-corporate CDOs and derivative transactions	(115.3)	Risk-based model	Average life (in years)	<1 - 20
			Own credit spread (2)	0.9% - 3.8%
NIMS VIE	(3.1)	Discounted cash flow	NIMS credit spread	43.2%
			Own credit spread (2)	7.2%

- (1) Excludes certain assets and liabilities for which we do not develop quantitative unobservable inputs. The fair value estimates for these assets and liabilities are developed using third-party pricing information, generally without adjustment.
- (2) Represents the range of our CDS spread that a typical market participant might use in the valuation analysis based on the remaining term of the investment.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following table summarizes the significant unobservable inputs used in our recurring Level III fair value measurements as of December 31, 2013:

(In millions)	Fair Value Net Asset (Liability) December 31, 2013 (1)	Valuation Technique	Unobservable Input	Range/ Weighted Average
<b>Level III Assets/Liabilities:</b>				
State and municipal obligations	\$ 18.7	Discounted cash flow	Discount rate	12.3%
			Expected loss	11.1%
Other investments	81.0	Discounted cash flow	Discount rate	1.2%
Corporate CDOs	(1.4)	Base correlation model	Radian correlation to corporate index	85.0%
			Average credit spread	0.1% - 0.9%
			Own credit spread (2)	0.8% - 4.3%
CDOs of CMBS	(67.8)	Discounted cash flow	Radian correlation to CMBS transaction index	72.0% - 85.0%
			Own credit spread (2)	0.8% - 4.3%
TruPs CDOs	(43.9)	Discounted cash flow	Principal recovery	75.0%
			Principal recovery (stressed)	65.0%
			Probability of conditional liquidity payment	1.1% - 12.4%
			Own credit spread (2)	0.8% - 4.3%
TruPs - related VIE	(68.4)	Discounted cash flow	Discount rate	13.1%
Other non-corporate CDOs and derivative transactions	(119.4)	Risk-based model	Average life (in years)	<1 - 20
			Own credit spread (2)	0.8% - 4.3%
NIMS VIE	(2.8)	Discounted cash flow	NIMS credit spread	43.8%
			Own credit spread (2)	7.9%

- (1) Excludes certain assets and liabilities for which we do not develop quantitative unobservable inputs. The fair value estimates for these assets and liabilities are developed using third-party pricing information, generally without adjustment.
- (2) Represents the range of our CDS spread that a typical market participant might use in the valuation analysis based on the remaining term of the investment.

The significant unobservable inputs in the fair value measurement of our investment securities noted in the tables above include an interest rate used to discount the projected cash flows and an expected loss assumption. This expected loss assumption generally represents the principal shortfall we believe that a typical market participant would expect on our security as a result of the obligor's failure to pay. In addition, our other investments include a guaranteed investment contract for which the counterparty's non-performance risk is considered in the discount rate. Significant increases (decreases) in either the discount rates or loss estimates in isolation would result in a lower (higher) fair value measurement. Changes in these assumptions are independent and may move in either similar or opposite directions.

The significant unobservable inputs used in the fair value measurement of our derivative assets, derivative liabilities and VIE debt relate to average credit spreads, average life, discount rates, correlation to indices and projected losses. In addition, when determining the fair value of our liabilities, we are required to incorporate into the fair value of those liabilities an adjustment that reflects our own non-performance risk, if applicable, as discussed below.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

For our corporate CDOs, we estimate the correlation of the default probability between the corporate entities and Radian—the higher the correlation percentage, the higher the probability that both the corporate entities and Radian will default together. In addition, a widening of the average credit spread increases the expected loss for our transactions, and therefore, increases the related liability.

For our CDO of CMBS transactions, we use the CMBX index that most directly correlates to our transaction with respect to vintage and credit rating and then we estimate losses by applying a correlation factor. Because we have more exposure to senior tranches, an increase in this factor generally increases the expected loss for our transactions and therefore, increases our related liability.

For our TruPs CDOs, the performance of each underlying reference obligation is measured by a standard and distressed pricing, which indicates the expected principal recovery. An increase in the standard and stressed principal recovery decreases the loss severity of the transaction, and therefore, in isolation, decreases the related liability. For those transactions where we may be required to pay a “liquidity claim,” we also assign these transactions a probability that we will be required to pay such claim, which generally would increase our related liability.

For our TruPs-related VIE liabilities, the fair value is estimated using similar inputs as in the estimated fair value of our TruPs CDOs, except there is no non-performance risk adjustment, as the derivative liability is limited to the segregated assets already held by the VIE.

For our other non-corporate CDOs, we utilize the internal credit rating, average remaining life, and current par outstanding for each transaction to project both expected losses and an internally developed risk-based capital amount. An increase in the average remaining life typically increases the expected loss of the transactions, and therefore, increases our related liability. An upgrade (downgrade) in the internal credit rating typically decreases (increases) the expected loss of the transactions, and therefore, decreases (increases) our related liability.

For all fair value measurements where we project our non-performance risk, including VIE debt, we utilize a market observed credit spread for Radian, which we believe is the best available indicator of the market’s perception of our non-performance risk. In isolation, a widening (tightening) of this credit spread typically decreases (increases) our related liability. The assumption used to project our own non-performance risk is independent from the other unobservable inputs used in our fair value measurements. The net impact on our reported assets and liabilities from increases or decreases in our own credit spread and from increases or decreases in other unobservable inputs depends upon the magnitude and direction of the changes in each input; such changes may result in offsetting effects to our recorded fair value measurements or they may result in directionally similar impacts, which may be material.

**Other Fair Value Disclosure**

The carrying value and estimated fair value of other selected assets and liabilities not carried at fair value on our condensed consolidated balance sheets were as follows as of the dates indicated:

<b>(In millions)</b>	<b>March 31, 2014</b>		<b>December 31, 2013</b>	
	<b>Carrying Amount</b>	<b>Estimated Fair Value</b>	<b>Carrying Amount</b>	<b>Estimated Fair Value</b>
<b>Assets:</b>				
Fixed-maturities held to maturity	\$ 0.1	\$ 0.1 (1)	\$ 0.4	\$ 0.4 (1)
Other invested assets	46.8	55.4 (1)	47.4	54.3 (1)
<b>Liabilities:</b>				
Long-term debt (3)	938.4	1,559.8 (1)	930.1	1,502.7 (1)
Non-derivative financial guaranty liabilities	148.6	215.2 (2)	144.7	189.1 (2)

(1) These estimated fair values would be classified in Level II of the fair value hierarchy.

(2) These estimated fair values would be classified in Level III of the fair value hierarchy.

(3) The carrying amount of long-term debt is net of the equity component, which is accounted for under the accounting standard for convertible debt instruments that may be settled in cash upon conversion (including partial cash settlement). The fair value is estimated based on the quoted market prices for the same or similar issues. See Note 10 for further information.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**5. VIEs**

Our interests in VIEs for which we are not the primary beneficiary may be accounted for as insurance or reinsurance contracts or credit derivatives, depending on the nature of the transaction. For insurance and reinsurance contracts, we record reserves for losses and LAE, and for credit derivatives, we record cumulative changes in fair value as a derivative asset or liability.

We have determined that we are the primary beneficiary of our NIMS transaction and certain financial guaranty structured finance transactions. Our control rights in these VIEs, which we obtained due to an event of default or breach of a performance trigger as defined in the transaction, generally provide us with either a right to replace the VIE servicer or, in some cases, the right to direct the sale of the VIE assets. In some instances, we have the obligation to absorb the majority of the VIE's losses and the right to receive the majority of any remaining funds through our residual interest agreement and we have the ability to impact the activities of the VIE in certain limited ways that could impact the economic performance of this VIE. In those instances where we have determined that we are the primary beneficiary, we consolidate the assets and liabilities of the VIE. We have elected to carry the financial assets and financial liabilities of these VIEs at fair value. In certain instances, the operating results of the consolidated VIE may generate taxable income or loss. The following discussion relates to our consolidated and unconsolidated VIEs.

*Financial Guaranty Insurance Contracts*

In continually assessing our involvement with VIEs, we consider certain events such as the VIE's failure to meet certain contractual conditions, including performance tests and triggers, servicer termination events and events of default that may, should they occur, provide us with additional control rights over the VIE for a limited number of our transactions. The occurrence of these events would cause us to reassess our initial determination that we are not the primary beneficiary of a VIE. In addition, changes to its governance structure that would allow us to direct the activities of a VIE or our acquisition of additional financial interests in the VIE, would also cause us to reassess our initial determination that we are not the primary beneficiary of a VIE. Many of our financial guaranty contracts provide us with substantial control rights over the activities of VIEs upon the occurrence of default or other performance triggers described above. Therefore, additional VIEs may be consolidated by us if these events were to occur. Prior to the occurrence of these contingent conditions, another party (typically the collateral manager, servicer or equity holder) involved with the transaction holds the power to manage the VIE's assets and to impact the economic performance of the VIE, without our ability to control or direct such powers.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following tables provide a summary of our maximum exposure to losses, and the financial impact on our condensed consolidated balance sheets, our condensed consolidated statements of operations and our condensed consolidated statements of cash flows as of and for the periods indicated, as it relates to our consolidated and unconsolidated financial guaranty insurance contracts and credit derivative VIEs:

<b>(In thousands)</b>	Consolidated		Unconsolidated	
	March 31, 2014	December 31, 2013	March 31, 2014	December 31, 2013
<b>Balance Sheet:</b>				
Other invested assets	\$ 81,635	\$ 81,000	\$ —	\$ —
Premiums receivable	—	—	2,100	2,211
Other assets	92,594	92,023	—	—
Unearned premiums	—	—	1,680	1,872
Reserve for losses and LAE	—	—	9,505	14,094
Derivative liabilities	47,769	68,457	191,945	220,633
VIE debt—at fair value	92,436	91,800	—	—
Other liabilities	190	254	—	—
<b>Maximum exposure (1)</b>	<b>140,242</b>	<b>121,628</b>	<b>4,079,740</b>	<b>4,578,784</b>

- (1) The difference between the carrying amounts of the net asset/liability position and maximum exposure related to VIEs is primarily due to the difference between the face amount of the obligation and the recorded fair values, which include an adjustment for our non-performance risk, as applicable. For those VIEs that have recourse to our general credit, the maximum exposure is based on the net par amount of our insured obligation. For any VIEs that do not have recourse to our general credit, the maximum exposure is generally based on the recorded net assets of the VIE, as of the reporting date.

<b>(In thousands)</b>	Consolidated		Unconsolidated	
	Three Months Ended March 31,		Three Months Ended March 31,	
	2014	2013	2014	2013
<b>Statement of Operations:</b>				
Premiums earned	\$ —	\$ —	\$ 314	\$ 324
Net investment income	440	443	—	—
Net gain (loss) on investments	195	(1,530)	—	—
Change in fair value of derivative instruments				
—gain (loss)	20,117	3,062	29,621	(160,975)
Net gain on other financial instruments	1,016	1,155	—	—
Provision for losses—increase (decrease)	—	—	894	(10)
Other operating expenses	447	503	—	—
<b>Net Cash Inflow (Outflow)</b>	<b>—</b>	<b>114</b>	<b>(4,356)</b>	<b>1,215</b>

*NIMS VIE*

At March 31, 2014, we had one remaining NIMS transaction. We have determined that we are the primary beneficiary of this NIMS transaction, and have consolidated the assets and liabilities of the VIE. We have elected to carry the financial assets and financial liabilities of the VIE at fair value. At March 31, 2014 and December 31, 2013, the amount of VIE debt and our maximum exposure were immaterial. The amount of income and expense related to this VIE was immaterial for 2014 and 2013.



**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**6. Investments**

Our held to maturity and available for sale securities within our investment portfolio consisted of the following as of the dates indicated:

<b>(In thousands)</b>	<b>March 31, 2014</b>			
	<b>Amortized Cost</b>	<b>Fair Value</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>
<b>Fixed-maturities held to maturity:</b>				
State and municipal obligations	\$ 50	\$ 50	\$ —	\$ —
	<u>\$ 50</u>	<u>\$ 50</u>	<u>\$ —</u>	<u>\$ —</u>
<b>Fixed-maturities available for sale:</b>				
U.S. government and agency securities	\$ 8,961	\$ 9,116	\$ 202	\$ 47
State and municipal obligations	26,428	26,699	624	353
Corporate bonds and notes	58,480	58,812	1,102	770
RMBS	36,500	37,196	696	—
Other ABS	64,184	64,124	65	125
Foreign government and agency securities	17,944	17,805	69	208
Other investments	237	237	—	—
	<u>\$ 212,734</u>	<u>\$ 213,989</u>	<u>\$ 2,758</u>	<u>\$ 1,503</u>
Equity securities available for sale (1)	<u>\$ 78,106</u>	<u>\$ 137,920</u>	<u>\$ 59,814</u>	<u>\$ —</u>
Total debt and equity securities	<u>\$ 290,890</u>	<u>\$ 351,959</u>	<u>\$ 62,572</u>	<u>\$ 1,503</u>

- (1) Comprising broadly diversified domestic equity mutual funds (\$130.0 million fair value) and various preferred and common stocks invested across numerous companies and industries (\$8.0 million fair value).

<b>(In thousands)</b>	<b>December 31, 2013</b>			
	<b>Amortized Cost</b>	<b>Fair Value</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>
<b>Fixed-maturities held to maturity:</b>				
State and municipal obligations	\$ 358	\$ 351	\$ —	\$ 7
	<u>\$ 358</u>	<u>\$ 351</u>	<u>\$ —</u>	<u>\$ 7</u>
<b>Fixed-maturities available for sale:</b>				
U.S. government and agency securities	\$ 8,939	\$ 9,106	\$ 224	\$ 57
State and municipal obligations	26,489	25,946	26	569
Corporate bonds and notes	11,951	12,045	578	484
RMBS	72,665	73,115	450	—
Other investments	341	341	—	—
	<u>\$ 120,385</u>	<u>\$ 120,553</u>	<u>\$ 1,278</u>	<u>\$ 1,110</u>
Equity securities available for sale (1)	<u>\$ 78,106</u>	<u>\$ 135,168</u>	<u>\$ 57,062</u>	<u>\$ —</u>
Total debt and equity securities	<u>\$ 198,849</u>	<u>\$ 256,072</u>	<u>\$ 58,340</u>	<u>\$ 1,117</u>

- (1) Comprising broadly diversified domestic equity mutual funds (\$128.3 million fair value) and various preferred and common stocks invested across numerous companies and industries (\$6.9 million fair value).

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The trading securities within our investment portfolio, which are recorded at fair value, consisted of the following as of the dates indicated:

<u>(In thousands)</u>	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
Trading securities:		
U.S. government and agency securities	\$ 333,804	\$ 393,815
State and municipal obligations	611,410	595,070
Corporate bonds and notes	967,207	1,024,574
RMBS	245,232	487,239
CMBS	282,561	288,895
Other ABS	170,289	195,816
Foreign government and agency securities	28,866	40,657
Equity securities	88,860	90,604
Other investments	747	759
<b>Total</b>	<b>\$ 2,728,976</b>	<b>\$ 3,117,429</b>

For trading securities that were still held at March 31, 2014 and December 31, 2013, we had net unrealized gains during 2014 and net unrealized losses during 2013 associated with those securities in the amount of \$58.9 million and \$140.9 million, respectively.

As part of the Freddie Mac Agreement (defined in Note 8), Radian Guaranty had \$208 million and \$205 million at March 31, 2014 and December 31, 2013, respectively, in a collateral account currently invested primarily in trading securities, which is pledged to cover loss mitigation activity on the loans subject to the agreement. A portion of the funds deposited may be released to Radian Guaranty over time.

As of March 31, 2014 and December 31, 2013, our investment portfolio included no Sovereign or sub-Sovereign (collectively, "Sovereign") securities of the six European countries (Portugal, Ireland, Italy, Greece, Spain and Hungary) whose Sovereign obligations have been under particular stress due to economic uncertainty, potential restructuring and ratings downgrades nor securities of any other countries under similar stress.

The following tables show the gross unrealized losses and fair value of our securities deemed "available for sale" and "held to maturity," aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of the dates indicated:

<b>March 31, 2014: (\$ in thousands) Description of Securities</b>	<b>Less Than 12 Months</b>			<b>12 Months or Greater</b>			<b>Total</b>		
	<b># of securities</b>	<b>Fair Value</b>	<b>Unrealized Losses</b>	<b># of securities</b>	<b>Fair Value</b>	<b>Unrealized Losses</b>	<b># of securities</b>	<b>Fair Value</b>	<b>Unrealized Losses</b>
U.S. government and agency securities	1	\$ 5,417	\$ 47	—	\$ —	\$ —	1	\$ 5,417	\$ 47
State and municipal obligations	1	2	4	1	5,389	349	2	5,391	353
Corporate bonds and notes	10	31,135	223	2	2,950	547	12	34,085	770
Other ABS	8	46,709	125	—	—	—	8	46,709	125
Foreign government and agency securities	6	6,432	208	—	—	—	6	6,432	208
<b>Total</b>	<b>26</b>	<b>\$ 89,695</b>	<b>\$ 607</b>	<b>3</b>	<b>\$ 8,339</b>	<b>\$ 896</b>	<b>29</b>	<b>\$ 98,034</b>	<b>\$ 1,503</b>

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

December 31, 2013: (\$ in thousands) Description of Securities	Less Than 12 Months			12 Months or Greater			Total		
	# of securities	Fair Value	Unrealized Losses	# of securities	Fair Value	Unrealized Losses	# of securities	Fair Value	Unrealized Losses
U.S. government and agency securities	1	\$ 5,401	\$ 57	—	\$ —	\$ —	1	\$ 5,401	\$ 57
State and municipal obligations	4	14,502	42	2	5,514	534	6	20,016	576
Corporate bonds and notes	—	—	—	2	2,966	484	2	2,966	484
Total	5	\$ 19,903	\$ 99	4	\$ 8,480	\$ 1,018	9	\$ 28,383	\$ 1,117

During the first three months of 2014 and 2013, there were no credit losses recognized in earnings.

Impairments due to credit deterioration that result in a conclusion that the present value of cash flows expected to be collected will not be sufficient to recover the amortized cost basis of the security are considered other-than-temporary. Other declines in fair value (for example, due to interest rate changes, sector credit rating changes or company-specific rating changes) that result in a conclusion that the present value of cash flows expected to be collected will not be sufficient to recover the amortized cost basis of the security also may serve as a basis to conclude that an other-than-temporary impairment (“OTTI”) has occurred. To the extent we determine that a security is deemed to have had an OTTI, an impairment loss is recognized.

We had securities in an unrealized loss position that we did not consider to be other-than-temporarily impaired as of March 31, 2014. For all investment categories, the unrealized losses of 12 months or greater duration as of March 31, 2014, were generally caused by interest rate or credit spread movements since the purchase date. As of March 31, 2014, we expected the present value of cash flows to be collected from these securities to be sufficient to recover the amortized cost basis of these securities. As of March 31, 2014, we did not have the intent to sell any debt securities in an unrealized loss position, and we determined that it is more likely than not that we will not be required to sell the securities before recovery of their cost basis, which may be at maturity; therefore, we did not consider these investments to be other-than-temporarily impaired at March 31, 2014.

The contractual maturities of fixed-maturity investments are as follows:

(In thousands)	March 31, 2014			
	Held to Maturity		Available for Sale	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less (1)	\$ 50	\$ 50	\$ 3,543	\$ 3,066
Due after one year through five years (1)	—	—	42,858	42,935
Due after five years through ten years (1)	—	—	39,863	39,858
Due after ten years (1)	—	—	25,785	26,809
RMBS (2)	—	—	36,500	37,196
Other ABS (2)	—	—	64,185	64,125
Total	\$ 50	\$ 50	\$ 212,734	\$ 213,989

(1) Actual maturities may differ as a result of calls before scheduled maturity.

(2) RMBS and Other ABS are shown separately, as they are not due at a single maturity date.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**7. Reinsurance**

The effect of reinsurance on net premiums written and earned is as follows:

<u>(In thousands)</u>	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
Net premiums written-insurance:		
Direct	\$ 229,322	\$ 245,467
Assumed	473	(10,397)
Ceded	(16,089)	(27,885)
Net premiums written-insurance	<u>\$ 213,706</u>	<u>\$ 207,185</u>
Net premiums earned-insurance:		
Direct	\$ 221,959	\$ 207,940
Assumed	2,147	2,211
Ceded	(18,441)	(17,563)
Net premiums earned-insurance	<u>\$ 205,665</u>	<u>\$ 192,588</u>

*Mortgage Insurance*

We have two separate quota share reinsurance (“QSR”) agreements with a third-party reinsurance provider (the “Initial QSR Transaction,” and the “Second QSR Transaction,” collectively, the “Reinsurance Transactions”). As of March 31, 2014, RIF ceded under the Initial QSR Transaction and Second QSR Transaction was \$1.3 billion and \$1.4 billion, respectively.

The following tables show the amounts related to the Reinsurance Transactions for the periods indicated:

<u>(In thousands)</u>	<u>Initial QSR Transaction</u>	
	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
Ceded premiums written	\$ 5,304	\$ 6,122
Ceded premiums earned	6,807	7,833
Ceding commissions written	1,326	1,530

<u>(In thousands)</u>	<u>Second QSR Transaction</u>	
	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
Ceded premiums written	\$ 7,293	\$ 16,440
Ceded premiums earned	6,585	2,838
Ceding commissions written	2,553	5,754

We ceded the maximum amount permitted under the Initial QSR Transaction (up to \$1.6 billion of ceded RIF), and therefore, are no longer ceding NIW under this transaction. We continue to cede NIW under the Second QSR Transaction. Ceded losses to date under the Reinsurance Transactions have been immaterial.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**8. Losses and LAE**

Our reserve for losses and LAE, as of the dates indicated, consisted of:

<u>(In thousands)</u>	<u>March 31, 2014</u>	<u>December 31, 2013</u>
Mortgage insurance reserves	\$ 1,893,960	\$ 2,164,353
Financial guaranty reserves	29,751	21,068
Total reserve for losses and LAE	<u>\$ 1,923,711</u>	<u>\$ 2,185,421</u>

See Note 9 for information regarding our financial guaranty reserves.

The following table shows our mortgage insurance reserve for losses and LAE by category at the end of each period indicated:

<u>(In thousands)</u>	<u>March 31, 2014</u>	<u>December 31, 2013</u>
Reserves for losses by category:		
Prime	\$ 790,529	\$ 937,307
Alternative-A (“Alt-A”)	351,695	384,841
A minus and below	189,453	215,545
Incurred but not reported (“IBNR”) and other	347,674	347,698
LAE	50,684	51,245
Reinsurance recoverable (1)	25,751	38,363
Total primary reserves	<u>1,755,786</u>	<u>1,974,999</u>
Pool	123,596	169,682
IBNR and other	5,679	8,938
LAE	4,517	5,439
Total pool reserves	<u>133,792</u>	<u>184,059</u>
Total first-lien reserves	<u>1,889,578</u>	<u>2,159,058</u>
Second-lien and other (2)	4,382	5,295
Total reserve for losses	<u>\$ 1,893,960</u>	<u>\$ 2,164,353</u>

- (1) Primarily represents ceded losses on captive transactions and the Reinsurance Transactions.  
(2) Does not include our second-lien premium deficiency reserve that is included in other liabilities.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following table presents information relating to our mortgage insurance reserves for losses, including IBNR reserves and LAE, for the periods indicated:

<u>(In thousands)</u>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Mortgage Insurance</b>		
Balance at January 1	\$ 2,164,353	\$ 3,083,608
Less reinsurance recoverables (1)	38,363	83,238
Balance at January 1, net of reinsurance recoverables	2,125,990	3,000,370
Add losses and LAE incurred in respect of default notices reported and unreported in:		
Current year (2)	142,696	182,534
Prior years	(93,536)	(50,578)
Total incurred	49,160	131,956
Deduct paid claims and LAE related to:		
Prior years	306,941	309,927
Total paid	306,941	309,927
Balance at end of period, net of reinsurance recoverables	1,868,209	2,822,399
Add reinsurance recoverables (1)	25,751	72,101
Balance at March 31	\$ 1,893,960	\$ 2,894,500

- (1) Related to ceded losses on captive reinsurance transactions and the Reinsurance Transactions. See Note 7 for additional information.
- (2) Related to underlying defaulted loans with a most recent default notice dated in the year indicated. For example, if a loan had defaulted in a prior year, but then subsequently cured and later re-defaulted in the current year, that default would be considered a current year default.

Our mortgage insurance loss reserves declined in the first quarter of 2014, primarily as a result of the volume of paid claims, cures and insurance rescissions and claim denials continuing to outpace new default notices received. Reserves established for new default notices were the primary driver of our total incurred loss for 2014. The impact to incurred losses from default notices reported in 2014 was partially mitigated by favorable reserve development on prior year defaults, which was driven primarily by higher cures and lower claim severity rates than were previously estimated. Total paid claims were generally consistent in the first quarter of 2014 with the comparable period in 2013.

In August 2013, Radian Guaranty entered into a Master Transaction Agreement with Freddie Mac (the “Freddie Mac Agreement”) related to a group of first-liens guaranteed by Freddie Mac that were insured by Radian Guaranty and were in default as of December 31, 2011. We deposited funds into a collateral account to cover future loss mitigation activity on these loans. From the time the collateral account was established through March 31, 2014, approximately \$13.0 million of additional loss mitigation activity had become final in accordance with the Freddie Mac Agreement and \$137.2 million of submitted claims had been rescinded, denied, curtailed or cancelled, but were not considered final in accordance with the Freddie Mac Agreement.

Our mortgage insurance loss reserves declined in the first quarter of 2013, primarily as a result of a decrease in our total inventory of defaults, as the volume of paid claims, cures and insurance rescissions and claim denials outpaced new default notices received during the quarter. Favorable reserve development on default notices reported in prior years partially mitigated the impact from new defaults, as the benefit to prior year defaults from higher cures and claim curtailments was more than previously estimated.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Our aggregate weighted average default to claim rate assumption (net of denials and rescissions) used in estimating our reserve for losses was 46% at March 31, 2014, compared to 47% at December 31, 2013. We develop our default to claim rate estimates on defaulted loans based on the age of the underlying defaulted loans, as measured by the number of monthly payments missed. As of March 31, 2014, our aggregate weighted average default to claim rate estimate on our total first-lien portfolio, net of estimated future denials and rescissions and excluding pending claims, was 39% and ranged from 19% for insured loans that had missed two to three monthly payments, to 48% for such loans that had missed 12 or more monthly payments. Our estimate of expected insurance rescissions and claim denials (net of expected reinstatements) embedded in our default to claim rate is generally based on our experience over the past year, with consideration given for differences in characteristics between those rescinded policies and denied claims and the loans remaining in our defaulted inventory.

Our estimates of future rescissions and denials remain elevated compared to levels experienced before 2009. The elevated levels of our rate of insurance rescissions and claim denials have reduced our paid losses and have resulted in a significant reduction in our loss reserves. Our estimate of net future rescissions and denials reduced our loss reserves as of March 31, 2014 and December 31, 2013 by approximately \$219 million and \$247 million, respectively. Conversely, our estimate of future reinstatements of previously rescinded policies and denied claims, which are primarily reflected in our IBNR reserve estimate, increased our loss reserves as of March 31, 2014 and December 31, 2013 by approximately \$285 million and \$283 million, respectively. The amount of estimated rescissions and denials incorporated into our reserve analysis at any point in time is affected by a number of factors, including not only our estimated rate of rescissions and denials on future claims, but also the volume and attributes of our defaulted insured loans, our estimated default to claim rate and our estimated claim severity, among other assumptions. Although we expect the amount of estimated rescissions and denials embedded within our reserve analysis to remain elevated as compared to levels before 2009, we expect them to continue to decrease over time, as the defaults related to our legacy portfolio decline as a proportion of our total default portfolio and as we realize the results through actual rescissions and denials, or the commutations of insured loans. In the event that we experience a more rapid than expected decrease in the level of future insurance rescissions and claim denials from the current levels, it could have an adverse effect on our paid losses and loss reserves.

The following table illustrates the amount of first-lien claims submitted to us for payment that were rescinded or denied, for the periods indicated, net of any reinstatements of previously rescinded policies or denied claims within each period:

<u>(In millions)</u>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Rescissions	\$ 16.1	\$ 15.3
Denials	12.2	27.2
Total first-lien claims submitted for payment that were rescinded or denied (1)	<u>\$ 28.3</u>	<u>\$ 42.5</u>

(1) Includes an amount related to a small number of submitted claims that were subsequently withdrawn by the insured.

Our reported rescission, denial and claim curtailment activity in any given period is subject to challenge by our lender and servicer customers. We expect that a large number of previously denied claims will be resubmitted with the required documentation and ultimately paid; therefore, we have considered this expectation in developing our IBNR reserve estimate. This IBNR estimate was \$288.2 million and \$281.9 million at March 31, 2014 and December 31, 2013, respectively. For the first quarter of 2014, our IBNR estimate of \$288.2 million includes an estimate of future reinstatements of previously denied claims, rescinded policies and curtailments of \$163.8 million, \$93.3 million and \$13.4 million, respectively. These reserves relate to \$266.9 million of claims that were denied within the preceding 12 months, \$362.5 million of policies rescinded within the preceding 24 months, and \$80.2 million of claim curtailments within the preceding 24 months, as well as a significant number of additional denials and rescissions that were denied or rescinded in earlier periods but remain the subject of continuing settlement discussions with certain of our lender and servicer customers.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Until a liability associated with such activities or discussions becomes probable and can be reasonably estimated, we consider our claim payments or our rescissions, denials and curtailments to be resolved for financial reporting purposes. Under the accounting standard regarding contingencies, an estimated loss is accrued only if we determine that the loss is probable and can be reasonably estimated. For the first quarter of 2014, a significant portion of our IBNR estimate of \$288.2 million relates to one servicer, with whom we are currently in settlement discussions regarding a large population of disputed rescissions, denials, curtailments and potential insurance cancellations. For these populations, we have determined that a settlement is probable and that a loss can be reasonably estimated, and have reflected our best estimate of the expected loss related to the populations under discussion with this servicer in our financial statements, primarily as a component of our IBNR reserve. While our reserves include our best estimate of this loss, the outcome of the discussions or potential legal proceedings that could ensue is uncertain, and it is reasonably possible that a loss exists in excess of the amount accrued. Due to the dynamic nature of these discussions, the range of factors that could impact settlement negotiations and the inherent uncertainty of the outcome of such matters, we cannot estimate the amount of any additional loss that is reasonably possible.

Generally, we estimate our claim liability related to the potential future reinstatement of previously denied claims and rescinded policies by estimating an initial gross reinstatement rate at the time of denial or rescission, which then declines over a 12- or 24-month timeframe. As of March 31, 2014, for previously denied claims, this initial gross reinstatement assumption begins at approximately 60% and declines to 0% after 12 months, while for previously rescinded policies, the initial assumed reinstatement rate begins at approximately 20% and declines to 0% after 24 months. Our IBNR reserve estimate also includes the projected potential impact from future estimated rescissions on reinstated denials. Therefore, at any particular point in time, our IBNR reserve estimate with respect to previously rescinded policies or denied claims is affected not only by our initial reinstatement assumption, but also by the length of time since the denial or rescission, our estimated likelihood of such reinstatements resulting in a paid claim, and the expected claim severity on such paid claims, as well as the potential outcome of any discussions with our lender and servicer customers regarding such rescissions or denials. In addition, as of March 31, 2014, our IBNR reserve estimate incorporates an ultimate overturn rate assumption of approximately 30% for previously curtailed claims.

We also accrue for the premiums that we expect to refund to our lender customers in connection with our estimated insurance rescission activity. Our accrued liability for such refunds, which is included within other liabilities on our condensed consolidated balance sheets, was \$14.8 million and \$17.0 million as of March 31, 2014 and December 31, 2013, respectively.

We considered the sensitivity of first-lien loss reserve estimates at March 31, 2014 by assessing the potential changes resulting from a parallel shift in severity and default to claim rate. For example, assuming all other factors remain constant, for every one percentage point change in primary claim severity (which we estimate to be 28% of unpaid principal balance at March 31, 2014), we estimated that our loss reserves would change by approximately \$49 million at March 31, 2014. For every one percentage point change in pool claim severity (which we estimate to be 44% of unpaid principal balance at March 31, 2014), we estimated that our loss reserves would change by approximately \$2 million at March 31, 2014. For every one percentage point change in our overall net default to claim rate (which we estimate to be 46% at March 31, 2014, including our assumptions related to rescissions and denials), we estimated an approximately \$32 million change in our loss reserves at March 31, 2014.



**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**9. Financial Guaranty Insurance Contracts**

The following table includes information as of March 31, 2014 regarding our financial guaranty claim liabilities on non-derivative transactions, segregated by the surveillance categories that we use in monitoring the risks related to these contracts:

(\$ in thousands)	Surveillance Categories				
	Performing	Special Mention	Intensified Surveillance	Case Reserve	Total
Number of policies	7	221	56	82	366
Remaining weighted-average contract period (in years)	22	16	19	18	17
Insured contractual payments outstanding:					
Principal	\$ 1,513	\$ 1,162,520	\$ 581,107	\$ 79,952	\$ 1,825,092
Interest	172	671,500	306,299	21,614	999,585
Total	\$ 1,685	\$ 1,834,020	\$ 887,406	\$ 101,566	\$ 2,824,677
Gross claim liability	\$ 1	\$ 22,047	\$ 229,993	\$ 25,557	\$ 277,598
Less:					
Gross potential recoveries	—	2,364	334,298	44,075	380,737
Discount, net	—	3,343	(147,419)	(2,328)	(146,404)
Net claim liability/(asset) (prior to reduction for unearned premium)	\$ 1	\$ 16,340	\$ 43,114	\$ (16,190)	\$ 43,265
Unearned premium revenue	\$ 6	\$ 20,513	\$ 9,205	\$ —	\$ 29,724
Net claim liability/(asset) reported in the balance sheet	\$ —	\$ 6,453	\$ 37,552	\$ (16,190)	\$ 27,815
Reinsurance recoverables	\$ —	\$ —	\$ —	\$ —	\$ —

A net claim liability is established for a performing credit if there is evidence that credit deterioration has occurred and the expected loss on the credit exceeds the unearned premium revenue for the contract based on the present value of the expected net cash inflows and outflows. Included in accounts and notes receivable and unearned premiums on our condensed consolidated balance sheets are the present values of premiums receivable and unearned premiums that are received on an installment basis. The premiums receivable is net of commissions on assumed reinsurance business. The present values of premiums receivable and unearned premiums that are received on an installment basis were \$24.8 million and \$26.2 million, respectively, as of March 31, 2014, and \$25.2 million and \$27.0 million, respectively, as of December 31, 2013.

The accretion of these balances is included either in premiums written and premiums earned (for premiums receivable) or policy acquisition costs (for commissions) on our condensed consolidated statements of operations. There was an immaterial amount of accretion recorded in policy acquisition costs and premiums earned for the three months ended March 31, 2014 and 2013.

The nominal (non-discounted) premiums, net of commissions that are expected to be collected on financial guaranty contracts with installment premiums, included in premiums receivable as of March 31, 2014, was \$31.2 million and is expected to decrease over time as the portfolio runs off. The activity related to the net present value of premiums receivable during the three months ended March 31, 2014 and 2013 was not material. The weighted-average risk-free rate used to discount the premiums receivable and premiums to be collected was 2.6% at March 31, 2014.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Premiums earned were affected by the following for the periods indicated:

<u>(In thousands)</u>	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
Refundings	\$ 2,117	\$ 4,753
Recaptures/Commutations	—	(2,447)
Adjustments to installment premiums, gross of commissions	139	2,692
Unearned premium acceleration upon establishment of case reserves	—	65
Foreign exchange revaluation, gross of commissions	314	(768)
Total adjustment to premiums earned	<u>\$ 2,570</u>	<u>\$ 4,295</u>

The following table shows the expected contractual premium revenue from our existing financial guaranty portfolio, assuming no refundings of any financial guaranty obligations, as of March 31, 2014:

<u>(In thousands)</u>	<u>Ending Net Unearned Premiums</u>	<u>Unearned Premium Amortization</u>	<u>Accretion</u>	<u>Total Premium Revenue</u>
2 <sup>nd</sup> quarter 2014	\$ 175,331	\$ 6,088	\$ 199	\$ 6,287
3 <sup>rd</sup> quarter 2014	167,264	8,066	193	8,259
4 <sup>th</sup> quarter 2014	162,654	4,610	191	4,801
2014	162,654	18,764	583	19,347
2015	146,423	16,232	719	16,951
2016	133,021	13,402	657	14,059
2017	120,746	12,274	616	12,890
2018	109,213	11,533	562	12,095
2014 - 2018	109,213	72,205	3,137	75,342
2019 - 2023	61,574	47,639	2,147	49,786
2024 - 2028	30,234	31,341	1,369	32,710
2029 - 2033	12,735	17,499	873	18,372
After 2033	—	12,735	1,009	13,744
Total	<u>\$ —</u>	<u>\$ 181,419</u>	<u>\$ 8,535</u>	<u>\$ 189,954</u>

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following table shows the significant components of changes in our financial guaranty claim liability for the three months ended March 31, 2014 and 2013, excluding reserves related to our trade credit reinsurance and surety business of \$1.9 million and \$2.1 million, respectively, which are excluded from the accounting standard regarding accounting for financial guaranty insurance contracts by insurance enterprises.

<b>(In thousands)</b>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Claim liability at January 1	\$ 19,458	\$ 64,291
Incurring losses and LAE:		
Increase in gross claim liability	8,140	8,390
Decrease (increase) in gross potential recoveries	32,958	(3,946)
Increase in discount	(31,757)	(3,555)
Increase in unearned premiums	(4,110)	(797)
Incurred losses and LAE	5,231	92
Paid losses and LAE:		
Current year	—	1
Prior years	3,126	(41,915)
Paid losses and LAE	3,126	(41,914)
Claim liability at March 31	\$ 27,815	\$ 22,469
Components of incurred losses and LAE:		
Claim liability established in current period	\$ 1,040	\$ 104
Changes in existing claim liabilities	4,191	(12)
Total incurred losses and LAE	\$ 5,231	\$ 92
Components of increase in discount:		
Increase in discount related to claim liabilities established in current period	\$ (491)	\$ (128)
Increase in discount related to existing claim liabilities	(31,266)	(3,427)
Total increase in discount	\$ (31,757)	\$ (3,555)

Paid losses during the first quarter of 2013 include \$41.6 million related to a January 2013 commutation with a primary insurer.

Our financial guaranty loss reserve estimate involves significant judgment surrounding the estimated probability of the likelihood, magnitude and timing of each potential loss based upon different loss scenarios. The probabilities, assumptions and estimates we use to establish our financial guaranty loss reserves are subject to uncertainties, particularly given the current economic and credit environments, including uncertainties regarding our public finance municipal exposures and international Sovereign risk exposures. We continue to monitor the uncertainties surrounding our portfolio, and it is possible that the actual losses paid could differ materially from our present estimates.

The weighted-average risk-free rates used to discount the gross claim liability and gross potential recoveries on our financial guaranty contracts were as follows, as of the dates indicated:

March 31, 2014	2.86%
December 31, 2013	2.95%
March 31, 2013	2.09%
December 31, 2012	2.00%

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**10. Long-Term Debt**

The carrying value of our long-term debt at March 31, 2014 and December 31, 2013 was as follows:

<u>(In thousands)</u>		<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
5.375% Senior Notes due 2015		\$ 54,484	\$ 54,481
9.000% Senior Notes due 2017		191,850	191,611
3.000% Convertible Senior Notes due 2017 (1)		358,985	353,798
2.250% Convertible Senior Notes due 2019 (2)		333,071	330,182
Total long-term debt		<u>\$ 938,390</u>	<u>\$ 930,072</u>

(1) The principal amount of these notes is \$450 million.

(2) The principal amount of these notes is \$400 million.

**Convertible Senior Notes due 2017 and 2019**

During the three-month period ended March 31, 2014, our closing stock prices exceeded the thresholds required for the holders of our Convertible Senior Notes due 2017 and our Convertible Senior Notes due 2019 to be able to exercise their conversion rights during the three-month period ending June 30, 2014. As a result, at March 31, 2014, the equity component related to our Convertible Senior Notes due 2017 was reclassified from permanent equity to mezzanine (temporary) equity as “equity component of currently redeemable convertible senior notes.” We will evaluate whether the conversion threshold requirements have been met on a quarterly basis, and will report the equity component related to our Convertible Senior Notes due 2017 as temporary equity for any period in which the debt remains currently convertible.

Issuance and transaction costs incurred at the time of the issuance of the convertible notes are allocated to the liability and equity components in proportion to the allocation of proceeds and accounted for as debt issuance costs and equity issuance costs, respectively. The convertible notes are reflected on our condensed consolidated balance sheets as follows:

<u>(In thousands)</u>	<u>Convertible Senior Notes due 2017</u>		<u>Convertible Senior Notes due 2019</u>	
	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
<b>Liability component:</b>				
Principal	\$ 450,000	\$ 450,000	\$ 400,000	\$ 400,000
Less: debt discount, net (1)	(91,016)	(96,202)	(66,929)	(69,818)
Net carrying amount	<u>\$ 358,984</u>	<u>\$ 353,798</u>	<u>\$ 333,071</u>	<u>\$ 330,182</u>
<b>Equity component of currently redeemable convertible senior notes</b>				
	<u>\$ 91,016</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Equity component (net of tax impact) (2)	<u>\$ (25,337) (3)</u>	<u>\$ 65,679</u>	<u>\$ 77,026 (4)</u>	<u>\$ 77,026 (4)</u>

(1) Included within long-term debt and is being amortized over the life of the convertible notes.

(2) Amount included within additional paid-in capital, net of the capped call transactions (Convertible Senior Notes due 2017) and related issuance costs (Convertible Senior Notes due 2017 and 2019).

(3) Primarily represents the deferred tax amount related to this transaction due to the reclassification of the debt discount to temporary equity.

(4) There was no net tax impact recorded in equity related to the Convertible Senior Notes due 2019, as a result of our full valuation allowance.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

The following tables set forth total interest expense recognized related to the convertible notes for the periods indicated:

<u>(\$ in thousands)</u>	<b>Convertible Senior Notes due 2017</b>	
	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Contractual interest expense	\$ 4,399	\$ 3,375
Amortization of debt issuance costs	300	283
Amortization of debt discount	5,186	4,712
Total interest expense	<u>\$ 9,885</u>	<u>\$ 8,370</u>
Effective interest rate of the liability component	9.75%	9.75%

<u>(\$ in thousands)</u>	<b>Convertible Senior Notes due 2019</b>	
	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Contractual interest expense	\$ 2,250	\$ 675
Amortization of debt issuance costs	316	92
Amortization of debt discount	2,889	819
Total interest expense	<u>\$ 5,455</u>	<u>\$ 1,586</u>
Effective interest rate of the liability component	6.25%	6.25%

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**11. Accumulated Other Comprehensive Income**

The following table shows the rollforward of accumulated other comprehensive income as of the periods indicated:

<u>(In thousands)</u>	Three Months Ended March 31, 2014		
	Before Tax	Tax Effect	Net of Tax
Balance at beginning of period	\$ 57,345	\$ 19,962	\$ 37,383
Other comprehensive income:			
Unrealized gains on investments:			
Unrealized holding gains arising during the period	4,649	164	4,485
Less: Reclassification adjustment for net gains included in net income (1)	809	285	524
Net unrealized gains on investments	3,840	(121)	3,961
Other comprehensive income	3,840	(121)	3,961
Balance at end of period	\$ 61,185	\$ 19,841	\$ 41,344
	Three Months Ended March 31, 2013		
<u>(In thousands)</u>	Before Tax	Tax Effect	Net of Tax
Balance at beginning of period	\$ 24,904	\$ 8,809	\$ 16,095
Other comprehensive income:			
Unrealized gains on investments:			
Unrealized holding gains arising during the period	11,486	4,020	7,466
Less: Reclassification adjustment for net gains included in net loss (1)	67	46	21
Net unrealized gains on investments	11,419	3,974	7,445
Other comprehensive income	11,419	3,974	7,445
Balance at end of period	\$ 36,323	\$ 12,783	\$ 23,540

(1) Included in net gains (losses) on investments on our condensed consolidated statements of operations.

**12. Income Taxes**

We provide for income taxes in accordance with the provisions of the accounting standard regarding accounting for income taxes. As required under this standard, our deferred tax assets and liabilities are recognized under the balance sheet method, which recognizes the future tax effect of temporary differences between the amounts recorded in our condensed consolidated financial statements and the tax bases of these amounts. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the periods in which the deferred tax asset or liability is expected to be realized or settled.

Our provision for income taxes for interim financial periods is based on an estimate of our annual effective tax rate (“ETR”) for the full year of 2014. When estimating our full year 2014 ETR, we adjust our projected pre-tax income for gains and losses on our derivative transactions and investments, changes in the accounting for uncertainty in income taxes, changes in our beginning of year valuation allowance, and other adjustments. The impact of these items is accounted for discretely at the federal applicable tax rate. During 2013, given the impact on our pre-tax results of net gains or losses resulting from our derivative transactions and our investment portfolio, and the continued uncertainty around our ability to rely on certain short-term financial projections, which directly affected our ability to estimate an ETR for the full year, we recorded our interim period income tax provision (benefit) based on actual results of operations.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

For federal income tax purposes, we had approximately \$1.8 billion of net operating loss (“NOL”) carryforwards and \$26.3 million of foreign tax credit carryforwards as of March 31, 2014. To the extent not utilized, the NOL carryforwards will expire during tax years 2028 through 2032 and the foreign tax credit carryforwards will expire during tax years 2018 through 2020. Certain entities within our consolidated group have also generated deferred tax assets of approximately \$31.6 million relating to state and local NOL carryforwards, which if unutilized, will expire during various future tax periods.

As of March 31, 2014 and December 31, 2013, before consideration of our valuation allowance, we had deferred tax assets, net of deferred tax liabilities, of approximately \$936.5 million and \$1,040.2 million, respectively.

We are required to establish a valuation allowance against our DTA when it is more likely than not that all or some portion of our DTA will not be realized. At each balance sheet date we assess our need for a valuation allowance. Our assessment is based on all available evidence, both positive and negative. This requires management to exercise judgment and make assumptions regarding whether our DTA will be realized in future periods. In making this assessment, the primary negative evidence that we considered is our cumulative losses in recent years and the uncertainty around our future results. We also considered positive evidence when assessing the need for a valuation allowance, such as future reversals of existing taxable temporary differences, future projections of taxable income, taxable income within the applicable carryback periods and potential tax planning strategies. In assessing our need for a valuation allowance, the weight assigned to the effect of both negative and positive evidence is commensurate with the extent to which such evidence can be objectively verified. Future recognition of our DTA will ultimately depend on the existence of sufficient taxable income of the appropriate character (ordinary income or capital gains) within the applicable carryback and carryforward periods provided under the tax law. This recognition may be based on the continued improvement in operating results and increased certainty regarding our projected incurred losses, and our ability to sustain profitability over an appropriate time period in amounts that are sufficient to support a conclusion that it is more likely than not that all or a portion of our DTAs will be realized. It is reasonably possible that we could meet these criteria in the foreseeable future.

A valuation allowance of approximately \$936.5 million and \$1,022.3 million was recorded against our net DTA of approximately \$936.5 million and \$1,040.2 million at March 31, 2014 and December 31, 2013, respectively. The remaining DTA of approximately \$17.9 million at December 31, 2013 represented our NOL carryback that we would be able to utilize as part of an overall settlement of the proposed Internal Revenue Service (“IRS”) adjustments relating to tax years 2000 through 2007. In July 2013, the FASB issued an update to the accounting standard regarding income taxes, which we adopted in the first quarter of 2014. This update provides guidance concerning the balance sheet presentation of an unrecognized tax benefit when Carryforwards are available. This accounting standard requires us to net our liability related to unrecognized tax benefits against the related deferred tax assets for the Carryforwards. A gross presentation will be required when the Carryforwards are not available under the tax law of the applicable jurisdiction or when the Carryforwards would not be used to settle any additional income taxes resulting from disallowance of the uncertain tax position. As a result of our implementation of this new FASB guidance, our March 31, 2014 consolidated balance sheet reflects a full valuation allowance against our deferred tax assets as our remaining DTA was reduced by the reclassification of our liability for unrecognized tax benefits.

During the quarter ended March 31, 2014, our valuation allowance decreased by approximately \$85.8 million. Of this amount, \$84.3 million was recorded as a benefit in continuing operations, offsetting the related deferred tax expense, and the remaining \$1.5 million decrease was recorded through other comprehensive income.

We are currently contesting proposed adjustments resulting from the examination by the IRS of our 2000 through 2007 consolidated federal income tax returns. The IRS opposes the recognition of certain tax losses and deductions that were generated through our investment in a portfolio of non-economic Real Estate Mortgage Investment Conduit (“REMIC”) residual interests and has proposed adjustments denying the associated tax benefits of these items. The proposed adjustments relating to the 2000 through 2007 tax years, if sustained, would result in additional income taxes of approximately \$128 million plus proposed penalties of approximately \$42 million. Additionally, we would incur interest expense on any sustained adjustments. We appealed these proposed adjustments to the IRS Office of Appeals (“Appeals”) and made “qualified deposits” with the U.S. Department of the Treasury (“U.S. Treasury”) of approximately \$85 million in June 2008 relating to the 2000 through 2004 tax years and approximately \$4 million in May 2010 relating to the 2005 through 2007 tax years in order to avoid the accrual of above-market-rate interest with respect to the proposed adjustments.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

We have made several attempts to reach a compromised settlement with Appeals, but in January 2013, we were notified that Appeals had rejected our latest settlement offer and plans to issue the formal notice of deficiency. Upon receipt of that deficiency notice, we will have 90 days to either pay the assessed tax liabilities, penalties and interest (the “deficiency amount”) in full or petition the U.S. Tax Court to litigate the deficiency amount. Litigation of the deficiency amount may result in substantial legal expenses and the litigation process could take several years to resolve. We can provide no assurance regarding the outcome of any such litigation or whether a compromised settlement with the IRS will ultimately be reached. After discussions with counsel about the issues raised in the examination, we believe that an adequate provision for income taxes has been made for the potential liabilities that may result from this matter. However, if the ultimate resolution of this matter produces a result that differs materially from our current expectations, there could be a material impact on our effective tax rate, results of operations and cash flows.

**13. Statutory Information**

We prepare our statutory financial statements in accordance with the accounting practices required or permitted, if applicable, by the insurance departments of the respective states of domicile of our insurance subsidiaries. Required statutory accounting practices include a variety of publications of the National Association of Insurance Commissioners (“NAIC”) as well as state laws, regulations and general administrative rules. In addition, insurance departments have the right to permit other specific practices that may deviate from prescribed practices. As of March 31, 2014, our use of any prescribed or permitted statutory accounting practices did not result in reported statutory surplus or risk-based capital being significantly different from what would have been reported had NAIC statutory accounting practices been followed.

The GSEs and state insurance regulators impose various capital requirements on our insurance subsidiaries. These include risk-to-capital ratios, risk-based capital measures and surplus requirements that limit the amount of insurance that each of our insurance subsidiaries may write. Our failure to maintain adequate levels of capital could lead to intervention by the various insurance regulatory authorities, which could materially and adversely affect our business, business prospects and financial condition.

Radian Group serves as the holding company for our insurance subsidiaries, through which we conduct the business of our mortgage insurance and financial guaranty business segments. These insurance subsidiaries are subject to comprehensive, detailed regulation by the insurance departments in the various states where our insurance subsidiaries are domiciled or licensed to transact business. Insurance laws vary from state to state, but generally grant broad supervisory powers to state agencies or officials to examine insurance companies and enforce rules or exercise discretion affecting almost every significant aspect of the insurance business, including the power to revoke or restrict an insurance company’s ability to write new business. The state insurance regulations include various capital requirements and dividend restrictions based on our insurance subsidiaries’ statutory financial position and results of operations, as described in Note 1 and below. Our failure to maintain adequate levels of capital could lead to intervention by the various insurance regulatory authorities, which could materially and adversely affect our business, business prospects and financial condition. As of March 31, 2014, the amount of restricted net assets held by our consolidated insurance subsidiaries (which represents our equity investment in those insurance subsidiaries) totaled \$1.6 billion of our consolidated net assets.

We actively manage Radian Guaranty’s capital position in various ways, including: (1) through internal and external reinsurance arrangements; (2) by seeking opportunities to reduce our risk exposure through commutations and other negotiated transactions; and (3) by contributing additional capital from Radian Group to our mortgage insurance subsidiaries.

*Radian Guaranty*

Radian Guaranty is domiciled and licensed in Pennsylvania as a stock casualty insurance company authorized to carry on the business of credit insurance, which includes the authority to write mortgage guaranty insurance. It is a monoline insurer, restricted to writing only residential mortgage guaranty insurance.

Radian Guaranty’s statutory net income (loss), statutory surplus and contingency reserve as of or for the periods indicated were as follows:

<u>(In millions)</u>	<u>As of and for the Three Months Ended March 31, 2014</u>	<u>As of and for the Year Ended December 31, 2013</u>
Statutory net income (loss)	\$ 68.2	\$ (23.8)
Statutory surplus	1,305.5	1,317.8
Contingency reserve	108.2	23.0



**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Radian Guaranty’s risk-to-capital calculation appears in the table below. For purposes of the risk-to-capital requirements imposed by certain states, statutory capital is defined as the sum of statutory policyholders’ surplus (i.e., statutory capital and surplus) plus statutory contingency reserves.

<u>(\$ in millions)</u>	<u>March 31, 2014</u>	<u>December 31, 2013</u>
RIF, net (1)	\$ 27,075.0	\$ 26,128.2
Statutory surplus	\$ 1,305.5	\$ 1,317.8
Statutory contingency reserve	108.2	23.0
Statutory position	\$ 1,413.7	\$ 1,340.8
Risk-to-capital	19.2:1	19.5:1

(1) Excludes risk ceded through reinsurance contracts (to third parties and affiliates) and RIF on defaulted loans.

Currently, we expect to maintain Radian Guaranty’s risk-to-capital ratio at or below 20 to 1. Radian Guaranty was in compliance with the Statutory RBC Requirements or MPP Requirements, as applicable, in each of the RBC States as of March 31, 2014. See Note 1 for information regarding the Statutory RBC Requirements and MPP Requirements as well as the new GSE eligibility requirements that we expect will be released as early as the second quarter of 2014.

The reduction in Radian Guaranty’s risk-to-capital ratio in the first quarter of 2014 was primarily due to an increase in statutory net income, partially offset by an increase in net RIF at Radian Guaranty.

*Radian Asset Assurance*

Radian Asset Assurance is domiciled and licensed in New York as a monoline financial guaranty insurer. It is also licensed under the New York insurance laws to write some types of surety insurance and credit insurance.

Radian Asset Assurance’s ability to pay dividends to its parent, Radian Guaranty, is restricted by certain provisions of the insurance laws of New York. Under the New York insurance laws, Radian Asset Assurance may only pay dividends from statutory earned surplus. Without the prior approval from the NYSDFS, Radian Asset Assurance can only pay a dividend, which when totaled with all other dividends declared or distributed by it during the preceding 12 months, is the lesser of 10% of its statutory surplus to policyholders, as shown by its last statement on file with the NYSDFS, or 100% of statutory adjusted net investment income during such period. In addition, the NYSDFS, in its discretion, may approve a dividend distribution greater than would be permitted as an ordinary dividend (generally referred to as an “extraordinary dividend”). In July 2013, Radian Asset Assurance paid an ordinary dividend of \$36 million to Radian Guaranty. We expect that in the third quarter of 2014, Radian Asset Assurance will have the capacity to pay another ordinary dividend to Radian Guaranty of approximately \$32 million. As of March 31, 2014, Radian Asset Assurance maintained claims paying resources of \$1.6 billion, which consists of statutory surplus of \$1.2 billion, plus contingency reserves, unearned premium reserves, the present value of installment premiums and loss and LAE reserves.

Since Radian Asset Assurance ceased writing new business in June 2008, Radian Asset Assurance has reduced its aggregate net par exposure by approximately 80% to \$22.7 billion as of March 31, 2014. This reduction included large declines in many of the riskier segments of Radian Asset Assurance’s insured portfolio. In light of this risk reduction and the significant level of capital, including \$1.2 billion of statutory surplus, remaining at Radian Asset Assurance, Radian Asset Assurance submitted a request to the NYSDFS seeking permission to pay an extraordinary dividend to Radian Guaranty. The NYSDFS currently is considering this request and there can be no assurance if and when such request will be granted in whole or in part, and if granted, that it will not be subject to material conditions.

New York insurance law also establishes aggregate risk limits on the basis of aggregate net liability as compared with statutory capital. “Aggregate net liability” is a risk-based calculation based on outstanding principal and interest of guaranteed obligations insured, net of qualifying reinsurance and collateral. Under these limits, policyholders’ surplus and contingency reserves must not be less than a percentage of aggregate net liability equal to the sum of various percentages of aggregate net liability for various categories of specified obligations. The percentage varies from 0.33% for certain municipal obligations to 4% for certain non-investment grade obligations. As of March 31, 2014, the aggregate net liability of Radian Asset Assurance was significantly below the applicable limit.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

New York insurance law requires financial guaranty insurers to maintain minimum policyholders' surplus of \$65 million. When added to the minimum policyholders' surplus of \$1.4 million separately required for the other lines of insurance that Radian Asset Assurance is licensed to write, Radian Asset Assurance is required to maintain an aggregate minimum policyholders' surplus of \$66.4 million. Radian Asset Assurance's statutory net income (loss), statutory surplus and contingency reserve as of or for the periods indicated were as follows:

<u>(In millions)</u>	<u>As of and for the Three Months Ended March 31, 2014</u>	<u>As of and for the Year Ended December 31, 2013</u>
Statutory net income (loss)	\$ 2.1	\$ (24.9)
Statutory surplus	1,186.3	1,198.0
Contingency reserve	271.8	264.0

**14. Selected Financial Information of Registrant—Radian Group**

<u>(In thousands)</u>	<u>March 31, 2014</u>	<u>December 31, 2013</u>
Investment in subsidiaries, at equity in net assets	\$ 1,721,213	\$ 1,419,360
Total assets	2,318,631	2,112,495
Long-term debt	938,390	930,072
Total liabilities	1,172,048	1,172,850
Equity component of currently redeemable convertible senior notes	91,016	—
Total stockholders' equity	1,055,567	939,645
Total liabilities and stockholders' equity	2,318,631	2,112,495

**15. Commitments and Contingencies**

*Legal Proceedings*

We are routinely involved in a number of legal actions and proceedings, the outcome of which are uncertain. The legal proceedings could result in adverse judgments, settlements, fines, injunctions, restitutions or other relief that could require significant expenditures or have other effects on our business. In accordance with applicable accounting standards and guidance, we establish accruals for a legal proceeding only when we determine both that it is probable that a loss has been incurred and the amount of the loss is reasonably estimable. We accrue the amount that represents our best estimate of the probable loss; however, if we can only determine a range of estimated losses, we accrue an amount within the range that, in our judgment, reflects the most likely outcome, and if none of the estimates within the range is more likely, we accrue the minimum amount of the range.

In the course of our regular review of pending legal matters, we determine whether it is reasonably possible that a potential loss relating to a legal proceeding may have a material impact on our liquidity, results of operations or financial condition. If we determine such a loss is reasonably possible, we disclose information relating to any such potential loss, including an estimate or range of loss or a statement that such an estimate cannot be made. On a quarterly and annual basis, we review relevant information with respect to legal loss contingencies and update our accruals, disclosures and estimates of reasonably possible losses or range of losses based on such reviews. We are often unable to estimate the possible loss or range of loss until developments in such matters have provided sufficient information to support an assessment of the range of possible loss, such as quantification of a damage demand from plaintiffs, discovery from other parties and investigation of factual allegations, rulings by the court on motions or appeals, analysis by experts, and the progress of settlement negotiations. In addition, we generally make no disclosures for loss contingencies that are determined to be remote. For matters for which we disclose an estimated loss, the disclosed estimate reflects the reasonably possible loss or range of loss in excess of the amount accrued, if any.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Loss estimates are inherently subjective, based on currently available information, and are subject to management's judgment and various assumptions. Due to the inherently subjective nature of these estimates and the uncertainty and unpredictability surrounding the outcome of legal proceedings, actual results may differ materially from any amounts that have been accrued.

On August 1, 2011, Radian Guaranty filed a lawsuit against Quicken Loans Inc. ("Quicken") in the U.S. District Court for the Eastern District of Pennsylvania. On September 5, 2012, Radian Guaranty filed an amended complaint. Radian Guaranty's complaint, as amended, seeks a declaratory judgment that it properly rescinded mortgage insurance coverage under Radian Guaranty's master insurance policy and delegated underwriting endorsement for approximately 220 home mortgage loans originated by Quicken based upon deficiencies and improprieties in the underwriting process. The approximately 220 home mortgage loans relate to an aggregate RIF of approximately \$13 million. On October 25, 2012, Quicken answered Radian Guaranty's amended complaint and asserted counterclaims against Radian Guaranty for alleged breach of contract and bad faith. On November 19, 2012, Radian Guaranty moved to dismiss Quicken's counterclaims. On October 28, 2013, the court granted Radian Guaranty's motion to dismiss in part and denied it in part. The court ruled that Quicken could not pursue a tort theory of bad faith and that Quicken had not stated a basis to toll the statute of limitations for any claims arising after the lawsuit was filed. The court permitted Quicken's remaining claims to proceed at this stage. Discovery has commenced in this litigation. The parties have agreed to increase the population of loans that are at issue from 220 loans to approximately 507 loans relating to an aggregate RIF of approximately \$29 million. This litigation is in the early stages of the proceedings, and therefore, we are unable to estimate whether a loss is reasonably possible in this matter.

We have been named as a defendant in a number of putative class action lawsuits alleging, among other things, that our captive reinsurance agreements violate the Real Estate Settlement Procedures Act of 1974 ("RESPA"). On December 9, 2011, an action titled Samp v. JPMorgan Chase Bank, N.A. (the "Samp case"), was filed in the U.S. District Court for the Central District of California. The defendants are JPMorgan Chase Bank, N.A., its affiliates (collectively, "JPMorgan"), and several mortgage insurers, including Radian Guaranty. The plaintiffs purport to represent a class of borrowers whose loans allegedly were referred to mortgage insurers by JPMorgan in exchange for reinsurance agreements between the mortgage insurers and JPMorgan's captive reinsurer. Plaintiffs assert violations of RESPA. On October 4, 2012, Radian Guaranty filed a motion to dismiss on a number of grounds, and on May 7, 2013, the court granted the motion and dismissed the plaintiffs' claims with prejudice. The court ruled that the plaintiffs could not state a claim against Radian Guaranty because it did not insure their loans, and, in addition, ruled that their claims were barred by the statute of limitations. On June 5, 2013, plaintiffs appealed these rulings to the U.S. Court of Appeals for the Ninth Circuit. On November 9, 2013, plaintiffs voluntarily dismissed their appeal.

Each of the cases described below are putative class actions (with alleged facts substantially similar to the facts alleged in the Samp case discussed above) in which Radian Guaranty has been named as a defendant and has insured at least one loan of one of the plaintiffs:

- On December 30, 2011, a putative class action under RESPA titled White v. PNC Financial Services Group was filed in the U.S. District Court for the Eastern District of Pennsylvania. On September 29, 2012, plaintiffs filed an amended complaint. On November 26, 2012, Radian Guaranty filed a motion to dismiss the plaintiffs' claims as barred by the statute of limitations. On June 20, 2013, the court granted Radian Guaranty's motion and dismissed plaintiffs' claims, but granted plaintiffs leave to file a second amended complaint. Plaintiffs filed their second amended complaint on July 5, 2013, reasserting a putative claim under RESPA on substantially the same allegations. Radian Guaranty filed a motion to dismiss plaintiffs' second amended complaint on July 22, 2013.
- On January 13, 2012, a putative class action under RESPA titled Menichino, et al. v. Citibank, N.A., et al., was filed in the U.S. District Court for the Western District of Pennsylvania. Radian Guaranty was not named as a defendant in the original complaint. On December 4, 2012, plaintiffs amended their complaint to add Radian Guaranty as an additional defendant. On February 4, 2013, Radian Guaranty filed a motion to dismiss the claims against it as barred by the statute of limitations. On July 19, 2013, the court granted Radian Guaranty's motion and dismissed plaintiffs' claims, but granted plaintiffs leave to file a second amended complaint. Plaintiffs filed their second amended complaint on August 16, 2013, reasserting a putative claim under RESPA on substantially the same allegations. Radian Guaranty filed a motion to dismiss plaintiffs' second amended complaint on September 17, 2013. The court denied Radian Guaranty's motion on February 4, 2014, without prejudice to Radian Guaranty's ability to raise the statute of limitations bar on a motion for summary judgment. On March 26, 2014, the court stayed the Menichino case, pending the outcome of an appeal filed by plaintiffs in Riddle v. Bank of America Corporation, et al. (another putative class action under RESPA in which Radian Guaranty is not a party) after the Riddle case was dismissed on summary judgment on November 18, 2013.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

- On April 5, 2012, a putative class action under RESPA titled *Manners, et al. v. Fifth Third Bank, et al.* was filed in the U.S. District Court for the Western District of Pennsylvania. On November 28, 2012, Radian Guaranty moved to dismiss plaintiffs' claims as barred by the statute of limitations. On July 19, 2013, the court granted Radian Guaranty's motion and dismissed plaintiffs' claims, but granted plaintiffs leave to file a second amended complaint. Plaintiffs filed their second amended complaint on August 16, 2013, reasserting a putative claim under RESPA on substantially the same allegations. Radian Guaranty filed a motion to dismiss plaintiffs' second amended complaint on September 17, 2013. The court denied Radian Guaranty's motion on February 5, 2014, without prejudice to Radian Guaranty's ability to raise the statute of limitations bar on a motion for summary judgment. On March 26, 2014, the court stayed the *Manners* case, pending the outcome of an appeal filed by plaintiffs in *Riddle v. Bank of America Corporation, et. al.* (another putative class action under RESPA in which Radian Guaranty is not a party) after the *Riddle* case was dismissed on summary judgment on November 18, 2013.
- On June 28, 2012, a putative class action under RESPA titled *Cunningham, et al. v. M&T Bank Corporation, et al.* was filed in the U.S. District Court for the Middle District of Pennsylvania. On December 10, 2012, Radian Guaranty moved to dismiss plaintiffs' claims as barred by the statute of limitations, and on February 11, 2013, plaintiffs filed an opposition to the motion to dismiss. On October 30, 2013, the court denied that motion and ordered a brief period of discovery limited to the statute of limitations issue. On January 31, 2014, plaintiffs voluntarily dismissed Radian Guaranty from this lawsuit.

With respect to the ongoing putative class actions discussed above, Radian Guaranty believes that the claims are without merit and intends to vigorously defend itself against these claims. We are not able to estimate the reasonably possible loss or range of loss for these matters because the proceedings are in a very preliminary stage and there is uncertainty as to the likelihood of a class being certified or the ultimate size of a class.

In addition to the litigation discussed above, we are involved in litigation that has arisen in the normal course of our business. We are contesting the allegations in each such pending action and management believes, based on current knowledge and after consultation with counsel, that the outcome of such litigation will not have a material adverse effect on our consolidated financial condition. However, the outcome of litigation and other legal and regulatory matters is inherently uncertain, and it is possible that one or more of the matters currently pending or threatened could have an unanticipated adverse effect on our liquidity, financial condition or results of operations for any particular period.

In addition to the private lawsuits discussed above, we and other mortgage insurers have been subject to inquiries from the Minnesota Department of Commerce and the Office of the Inspector General of the U.S. Department of Housing and Urban Development ("HUD"), requesting information relating to captive reinsurance. We have cooperated with these requests for information. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") amended RESPA and transferred the authority to implement and enforce RESPA from HUD to the Consumer Financial Protection Bureau ("CFPB"). In January 2012, we and other mortgage insurers received a request for information and documents from the CFPB relating to captive reinsurance arrangements, and in June 2012, we and other mortgage insurers received a Civil Investigative Demand from the CFPB as part of its investigation to determine whether mortgage lenders and private mortgage insurance providers engaged in acts or practices in violation of the Dodd-Frank Act, RESPA and the Consumer Financial Protection Act. On April 4, 2013, we reached a settlement with the CFPB, which was approved by the U.S. District Court for the Southern District of Florida on April 9, 2013. The settlement concludes the investigation with respect to Radian Guaranty without the CFPB making any findings of wrongdoing. As part of the settlement, Radian Guaranty agreed not to enter into new captive reinsurance arrangements for a period of ten years and to pay a civil penalty of \$3.75 million. We have not entered into any new captive reinsurance arrangements since 2007. During the high-claim years that followed the most recent economic downturn, captive arrangements have proven to represent a critical component of our loss mitigation strategy, effectively serving as designed to protect our capital position during a period of stressed losses. As of March 31, 2014 we had received total cash reinsurance recoveries from these captive reinsurance arrangements of approximately \$800 million. In August 2013, Radian Guaranty and other mortgage insurers received a draft Consent Order from the Minnesota Department of Commerce, containing proposed conditions and unspecified penalties, to resolve its outstanding inquiries related to captive reinsurance arrangements involving mortgage insurance in Minnesota. We continue to cooperate with the Minnesota Department of Commerce and are engaged in active discussions with them with respect to their inquiries, including various alternatives for resolving this matter. We cannot predict the outcome of this matter or whether additional actions or proceedings may be brought against us.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

We are contesting proposed adjustments resulting from the examination by the IRS of our 2000 through 2007 consolidated federal income tax returns. The IRS opposes the recognition of certain tax losses and deductions that were generated through our investment in a portfolio of non-economic REMIC residual interests currently held by Radian Guaranty Reinsurance Inc., one of our wholly-owned subsidiaries. The proposed adjustments relating to the 2000 through 2007 tax years, if sustained, will result in additional income taxes of approximately \$128 million plus proposed penalties of approximately \$42 million. Additionally, we would incur interest on any sustained adjustments. After several attempts to reach a settlement, we were notified in January 2013 that Appeals rejected our latest offer and plans to issue a formal notice of deficiency. Upon receipt of that notice, we will have 90 days to pay the deficiency amount or petition the U.S. Tax Court to litigate the matter. Litigation of the deficiency amount may result in substantial legal expenses and the litigation process could take several years to resolve. We can provide no assurance regarding the outcome of any such litigation or whether a settlement with the IRS may ultimately be reached. See Note 12 for additional information.

Under our master insurance policy, any suit or action arising from any right of an insured under the policy must be commenced within two years after such right first arose for primary insurance and within three years for certain other policies, including certain pool insurance policies. We continue to face a number of challenges from certain lender and servicer customers regarding our loss mitigation activities, which have resulted in some reversals of our decisions regarding rescissions, denials or claim curtailments. We are currently in discussions with customers regarding these loss mitigation activities, which if not resolved, could result in arbitration or additional judicial proceedings. See Note 8 for further information.

Further, we have identified a significant number of loans in our total defaulted portfolio (in particular, our older defaulted portfolio) for which “appropriate proceedings” (actions or proceedings such as foreclosure that provide the insured with title to the property) may not have been commenced within the outermost deadline in our master insurance policy. We currently are in discussions with the servicers for these loans regarding this potential violation and our corresponding rights under the master insurance policy. While we can provide no assurance regarding the outcome of these discussions or the ultimate resolution of these issues, it is possible that these discussions could result in arbitration or legal proceedings.

The elevated levels of our loss mitigation activities (related to servicer negligence) have led to an increased risk of litigation by lenders, policyholders and servicers challenging our right to rescind coverage, deny claims or curtail claim amounts. Although we believe that our loss mitigation actions are justified under our policies, if we are not successful in defending these actions, we may need to reassume the risk on and increase loss reserves for previously rescinded policies or pay additional claims on curtailed amounts. See Note 8 for further information.

*Other*

Securities regulations became effective in 2005 that impose enhanced disclosure requirements on issuers of ABS (including mortgage-backed securities). To allow our customers to comply with these regulations at that time, we typically were required, depending on the amount of credit enhancement we were providing, to provide: (1) audited financial statements for the insurance subsidiary participating in the transaction; or (2) a full and unconditional holding company-level guarantee for our insurance subsidiaries’ obligations in such transactions. Radian Group has guaranteed two structured transactions for Radian Guaranty involving approximately \$140.4 million of remaining credit exposure as of March 31, 2014.

On March 1, 2011, our subsidiary, Enhance Financial Services Group Inc. (“EFSG”) sold its 45% interest in the holding company of a Brazilian insurance company, which specializes in surety and agricultural insurance, to another owner for a nominal purchase price. This holding company and its subsidiaries are subject to regulation by The Superintendence of Private Insurance, the regulatory agency responsible for the supervision and control of the insurance market in Brazil. Although EFSG wrote off its entire interest in this company in 2005 and has sold its ownership interest, under Brazilian law, it is possible that EFSG could become liable for its proportionate share of the liabilities of the company related to the period in which EFSG was a significant shareholder, if the company was to become insolvent and had insufficient capital to satisfy its outstanding liabilities. EFSG’s share of the liabilities of the company attributable to this period was approximately \$103.4 million as of December 31, 2010, the date of the most recent financial information available to us.

As part of the non-investment-grade allocation component of our investment program, we had unfunded commitments of \$7.8 million at March 31, 2014, related to alternative investments that are primarily private equity structures. These commitments have capital calls expected through 2015, with the possibility of additional calls through 2017, and certain fixed expiration dates or other termination clauses.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

Our mortgage insurance business provides an outsourced underwriting service to its customers known as contract underwriting. Typically, we agree that if we make a material error in underwriting a loan, we will provide a remedy to the customer, by purchasing the loan or placing additional mortgage insurance coverage on the loan, or by indemnifying the customer against loss up to a maximum specified amount. By providing these remedies, we assume some credit risk and interest-rate risk if an error is found during the limited remedy period in the agreements governing our provision of contract underwriting services. Beginning in 2008, we limited the recourse available to our contract underwriting customers to apply only to those loans that are simultaneously underwritten for compliance with secondary market compliance and for potential mortgage insurance. In the first three months of 2014, we paid losses related to contract underwriting remedies of approximately \$0.5 million. Rising mortgage interest rates or further economic uncertainty may expose our mortgage insurance business to an increase in such costs. In the first three months of 2014, our provision for contract underwriting expenses was approximately \$0.2 million and our reserve for contract underwriting obligations at March 31, 2014 was approximately \$3.4 million. We monitor this risk and negotiate our underwriting fee structure and recourse agreements on a client-by-client basis. We also routinely audit the performance of our contract underwriters.

Through March 31, 2014, Radian Asset Assurance has received a series of claims totaling €9.1 million (\$12.5 million) from one of its trade credit and surety ceding companies related to surety bonds for Spanish housing cooperative developments. The ceding company is still in the process of settling additional similar claims, so the ultimate amount the ceding company will claim is uncertain. Based on information we received from the ceding company and the advice of our legal advisors, we believe that these claims are subject to a number of defenses, including that the risk under these surety bonds was not eligible for cession to Radian Asset Assurance under the terms and conditions of the applicable reinsurance treaties. We have rejected all claims related to these surety bonds and have not recorded a liability with respect to any of these claims, because we do not believe that a loss is probable. Without giving any consideration to our defenses, we believe the possible liability range for these surety bonds is from €9.1 million (\$12.5 million), representing our share of the amount the ceding company reported paid and claimed from us through March 31, 2014, to €16.5 million (\$22.8 million), representing our estimate of the maximum aggregate potential liability for current and future claims related to these surety bonds. The decrease in our estimate of the maximum aggregate potential liability from the €19.3 million (\$26.6 million) estimated as of December 31, 2013, is primarily due to additional information received during the first quarter of 2014, partially offset, in the case of our U.S. Dollar estimates, by adverse changes in the Euro/Dollar exchange rate.

We have incentive, retention and severance agreements with certain employees in our financial guaranty business. The total cost expected to be incurred under these agreements is \$12.1 million, of which \$2.0 million of unearned retention expense has not been recorded as of March 31, 2014. The remaining cost for these agreements is expected to be recorded by the end of 2015.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**16. Net Income (Loss) Per Share**

Basic net income (loss) per share is computed by dividing net income (loss) by the weighted-average number of common shares outstanding, while diluted net income (loss) per share reflects the maximum potential dilution that could occur from our stock-based compensation arrangements and the conversion of our outstanding convertible senior notes.

The calculation of the basic and diluted net income (loss) per share was as follows:

<u>(In thousands, except per share amounts)</u>	Three Months Ended March 31,	
	2014	2013
Net income (loss)—basic	\$ 202,759	\$ (187,500)
Adjustment for dilutive Convertible Senior Notes due 2019 (1)	5,455	—
Net income (loss)—diluted	\$ 208,214	\$ (187,500)
Average common shares outstanding—basic	173,165	144,355
Dilutive effect of Convertible Senior Notes due 2017 (2)	9,003	—
Dilutive effect of Convertible Senior Notes due 2019	37,736	—
Dilutive effect of stock-based compensation arrangements (3)	2,764	—
Adjusted average common shares outstanding—diluted	222,668	144,355
Net income (loss) per share—basic	\$ 1.17	\$ (1.30)
Net income (loss) per share—diluted	\$ 0.94	\$ (1.30)

- (1) As applicable, includes coupon interest, amortization of discount and fees, and other changes in income or loss that would result from the assumed conversion.
- (2) Does not include the anti-dilutive impact of 6,112,498 shares due to capped call transactions related to the Convertible Senior Notes due 2017. Such transactions were designed to offset the potential dilution of the notes up to a stock price of approximately \$14.11 per share. See Note 11 of Notes to Consolidated Financial Statements in our 2013 Form 10-K.
- (3) For the three months ended March 31, 2014, 946,400 shares of our common stock equivalents issued under our stock-based compensation arrangements were not included in the calculation of diluted net income per share as of such date because they were anti-dilutive. As a result of our net loss for the three months ended March 31, 2013, 5,198,389 shares of our common stock equivalents issued under our stock-based compensation arrangements were not included in the calculation of diluted net loss per share as of such date because they were anti-dilutive.

**Radian Group Inc.**  
**Notes to Unaudited Condensed Consolidated Financial Statements — (Continued)**

**17. Subsequent Events**

***Purchase Agreement***

On May 6, 2014, Radian Group entered into a Purchase Agreement with Clayton, Paul T. Bossidy and Cobra Green LLC (“Cobra Green”), with a related guarantee of the obligations of Cobra Green by Greenfield Acquisition Partners V, L.P., an affiliate of Cobra Green. Under the Purchase Agreement, at closing Radian Group will pay aggregate cash consideration of \$305 million, which includes repayment of Clayton’s outstanding debt, to purchase all of the outstanding equity interests in Clayton, subject to customary purchase price adjustments. Radian Group anticipates funding the entire purchase price and related expenses through net proceeds received from the issuance of debt and equity.

Clayton provides outsourced solutions to the mortgage industry, including a full suite of outsourced services, information-based analytics and specialty consulting for buyers and sellers of, and investors in, mortgage-related loans and securities and other debt instruments.

We expect to complete the Clayton acquisition during the summer of 2014, subject to satisfaction of customary closing conditions, including expiration of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, receipt of certain state licensing approvals, accuracy of representations and warranties, compliance with covenants and agreements and continued employment by Clayton’s chief executive officer and its president.



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

The following analysis should be read in conjunction with our unaudited condensed consolidated financial statements and the notes thereto included in this report and our audited financial statements, notes thereto and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” (“MD&A”) included in our Annual Report on Form 10-K for the year ended December 31, 2013 (the “2013 Form 10-K”), for a more complete understanding of our financial position and results of operations. In addition, investors should review the “Cautionary Note Regarding Forward Looking Statements—Safe Harbor Provisions” above and the “Risk Factors” detailed in Item 1A of our 2013 Form 10-K and in Item 1A of Part II of this Quarterly Report on Form 10-Q for a discussion of those risks and uncertainties that have the potential to affect our business, financial condition, results of operations, cash flows or prospects in a material and adverse manner. Our results of operations for interim periods are not necessarily indicative of results to be expected for the full year or for any other period.

Unless otherwise indicated, financial information in our MD&A is presented in accordance with accounting principles generally accepted in the United States of America (“GAAP”). Our senior management, including our Chief Executive Officer (the Company’s chief operating decision maker), uses “adjusted pretax operating income (loss)” as our primary measure to facilitate evaluation of the fundamental financial performance of the Company’s business segments and to allocate resources to the segments. Adjusted pretax operating income (loss) is defined as pretax income (loss) excluding the effects of net gains (losses) on investments and other financial instruments and net impairment losses recognized in earnings. It also excludes gains and losses related to changes in fair value estimates on insured credit derivatives and includes the impact of changes in the present value of estimated insurance claims and recoveries on insured credit derivatives, based on our ongoing insurance loss monitoring, as well as premiums earned on insured credit derivatives. In this MD&A, we present among our key performance indicators, “adjusted pretax operating income (loss),” which, on a consolidated basis, is a measure not determined in accordance with GAAP. See “*Use of Non-GAAP Financial Measure*” for more information regarding this non-GAAP financial measure, including a reconciliation to the most directly comparable GAAP measure.

### Overview

We are a credit enhancement company with a primary strategic focus on domestic residential mortgage insurance on first-lien mortgage loans (“first-liens”). We have two business segments—mortgage insurance and financial guaranty. Our mortgage insurance segment provides credit-related insurance coverage, principally through private mortgage insurance and risk management services, to mortgage lending institutions. We conduct our mortgage insurance business primarily through Radian Guaranty Inc. (“Radian Guaranty”), our principal mortgage insurance subsidiary. Our financial guaranty segment has provided direct insurance and reinsurance on credit-based risks, and also offered credit protection on various asset classes through financial guaranty policies and credit default swaps (“CDS”). While we discontinued writing new financial guaranty business in 2008, we continue to provide financial guaranty insurance on a portfolio of transactions, consisting primarily of public finance and structured finance transactions. In addition, our principal financial guaranty subsidiary, Radian Asset Assurance Inc. (“Radian Asset Assurance”), is a wholly-owned subsidiary of Radian Guaranty, which has allowed our financial guaranty business to serve as an important source of capital support for our mortgage insurance business. On May 6, 2014, Radian Group Inc. (“Radian Group”) entered into an agreement to purchase Clayton Holdings LLC (“Clayton”), a leading provider of outsourced solutions to the mortgage industry. See “Recent Developments” below for more information.

*Operating Environment.* As a seller of credit protection, our results are subject to macroeconomic conditions and specific events that impact the origination environment and the credit performance of our underlying insured assets. The financial crisis and the downturn in the housing and related credit markets that began in 2007 has had a significant negative impact on the operating environment and results of operations for both of our business segments. This was characterized by a decrease in mortgage originations, a broad decline in home prices, mortgage servicing and foreclosure delays, and ongoing deterioration in the credit performance of mortgage and other assets originated prior to 2009, together with macroeconomic factors such as high unemployment, limited employment growth, limited economic growth and a lack of meaningful liquidity in many sectors of the capital markets. More recently, we have experienced a period of economic recovery and the operating environment for our businesses has improved. Our results of operations have continued to improve as the negative impact from losses on the mortgage insurance we wrote during the poor underwriting years of 2005 through 2008 (we refer to our mortgage insurance portfolio on business written prior to 2009, as our “legacy portfolio”) has been reduced and we continue to write insurance on higher credit quality loans. As of March 31, 2014, our legacy portfolio had been reduced to approximately 38% of our total primary risk in force (“RIF”), while insurance on loans written after 2008 constituted approximately 62% of our primary RIF.

Although the United States (“U.S.”) economy and certain housing markets remain weak compared to historical standards, home prices have been appreciating on a broad basis throughout the U.S., foreclosure activity has declined and the credit quality of recent mortgage market originations continues to be significantly better than the credit quality of our legacy portfolio. In addition, although the economic recovery has been sluggish, there are signs of a broader recovery in the U.S. economy, including importantly, a reduction in unemployment rates. As a consequence of these and other factors, in 2014 we have experienced improvement in our results of operations. This positive development has been driven primarily by a significant reduction in our incurred losses as a result of an 18% decline in new primary mortgage insurance defaults in the three months ended March 31, 2014 compared to the number of new defaults in the comparable period of 2013 and by other positive default and claim developments.

Currently, our business strategy is primarily focused on: (1) growing our mortgage insurance business by writing insurance on high-quality mortgages in the U.S.; (2) pursuing other potential alternatives for providing credit-related services to the mortgage finance market, such as expanding our presence in the mortgage finance market through our agreement to acquire Clayton, as further discussed below; (3) continuing to manage losses in our legacy mortgage insurance and financial guaranty portfolios; (4) continuing to reduce our legacy mortgage insurance and financial guaranty exposures; and (5) continuing to effectively manage our capital and liquidity positions.

## **Recent Developments**

### *Purchase Agreement*

On May 6, 2014, Radian Group entered into a Unit Purchase Agreement (the “Purchase Agreement”) with Clayton, Paul T. Bossidy and Cobra Green LLC (“Cobra Green”), with a related guarantee of the obligations of Cobra Green by Greenfield Acquisition Partners V, L.P., an affiliate of Cobra Green. Under the Purchase Agreement, at closing Radian Group will pay aggregate cash consideration of \$305 million, which includes repayment of Clayton’s outstanding debt, to purchase all of the outstanding equity interests in Clayton, subject to customary purchase price adjustments. Radian Group anticipates funding the entire purchase price and related expenses through net proceeds received from the issuance of debt and equity.

Clayton is a leading provider of outsourced solutions to the mortgage industry, providing a full suite of outsourced services, information-based analytics and specialty consulting for buyers and sellers of, and investors in, mortgage-related loans and securities and other debt instruments. Clayton’s services primarily include:

- Loan Review/Due Diligence—Loan-level due diligence for the mortgage and residential mortgage backed securities (“RMBS”) markets through skilled professionals and proprietary technology, with offerings focused on credit underwriting, regulatory compliance and collateral valuation;
- Surveillance—Third-party performance oversight, risk management and consulting services, with offerings focused on RMBS surveillance, loan servicer oversight, reviews of loans in default and loan reviews for exception management;
- Component Services—Outsourced solutions focused on the real estate owned (“REO”) to rental market, REO-to-rental analysis and management, and REO-to-rental securitization reviews;
- REO/Short-Sale Services—REO asset and short sale management services, with offerings including residential and commercial REO asset management, short-sale management and borrower outreach; and
- EuroRisk—Outsourced mortgage services in the United Kingdom and other locations, with offerings including due diligence services, asset management, portfolio assessment and evaluation and consulting services.

Clayton's customers include a wide range of financial institutions, government sponsored entities, securitization trusts, investors, regulators and other mortgage-related service providers in various capacities, including as mortgage originators, mortgage purchasers, mortgage-backed securities issuers, mortgage-backed securities investors and mortgage servicers. For the twelve-month period ended December 31, 2013, Clayton reported that it had net income of \$9.1 million, which reflected, among other items, amortization of intangible assets of \$10.8 million and total revenues of \$135.0 million.

We expect to complete the Clayton acquisition during the summer of 2014, subject to satisfaction of customary closing conditions, including expiration of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, receipt of certain state licensing approvals, accuracy of representations and warranties, compliance with covenants and agreements and continued employment by Clayton's chief executive officer and its president.

#### *Other Initiatives*

Since Radian Asset Assurance ceased writing new business in June 2008, Radian Asset Assurance has reduced its aggregate net par exposure by approximately 80% to \$22.7 billion as of March 31, 2014. This reduction included large declines in many of the riskier segments of Radian Asset Assurance's insured portfolio. In light of this risk reduction and the significant level of capital, including \$1.2 billion of statutory surplus, remaining at Radian Asset Assurance, Radian Asset Assurance submitted a request with the New York State Department of Financial Services ("NYSDFS") seeking permission to pay an extraordinary dividend to Radian Guaranty. The NYSDFS currently is considering this request and there can be no assurance if and when such request will be granted in whole or in part, and if granted, that it will not be subject to material conditions. Without approval of an extraordinary dividend, we expect that Radian Asset Assurance will next have the capacity to pay an ordinary dividend of approximately \$32 million to Radian Guaranty in the third quarter of 2014.

### **Key Factors Affecting Our Results**

#### **Mortgage Insurance**

- *Premiums.* The premium rates we charge for our insurance are based on a number of borrower, loan and property characteristics. Premiums on our mortgage insurance products are paid either on a monthly installment basis ("monthly premium"), in a single payment at origination ("single premium"), as a combination of up-front premium at origination plus a monthly renewal, or in some cases, as an annual or multi-year premium.

New insurance written ("NIW") increases our insurance in force ("IIF") and premiums written and earned. An increase or decrease in IIF will generally have a corresponding impact on premiums earned. Cancellations of our insurance policies and other reductions of IIF, such as rescissions of coverage and claims paid, generally have a negative effect on premiums earned. The measure for assessing the impact of policy cancellations on our IIF is our persistency rate, defined as the percentage of IIF that remains on our books after any 12-month period. Insurance premiums on our monthly premium insurance policies are paid and earned over time; therefore, higher persistency rates on monthly premium insurance policies enable us to earn more premiums and recover more of our policy acquisition costs, and generally result in increased profitability. When single premium policies are cancelled by the insured because the loan has been paid off or otherwise, we accelerate the recognition of any remaining unearned premiums. Therefore, assuming all other factors remain constant, profitability increases on our single premium business when persistency rates are lower. Rescissions, which are discussed in further detail below, result in a full refund of the inception-to-date premiums received, and therefore, premiums earned are affected by any changes in our accrual for estimated rescission refunds. Additionally, premiums ceded to third-party reinsurance counterparties decrease premiums written and earned.

- *NIW*. NIW is affected by the overall size of the mortgage origination market, the penetration percentage of private mortgage insurance into the overall mortgage origination market and our market share of the private mortgage insurance market. The overall mortgage origination market is influenced by macroeconomic factors such as household composition, home affordability, interest rates, housing markets in general, credit availability and the impact of various legislative and regulatory actions that may influence the mortgage finance industry. The penetration percentage of private mortgage insurance is mainly influenced by the competitiveness of private mortgage insurance on Government-Sponsored Enterprise (“GSE”) conforming loans compared to Federal Housing Administration (“FHA”) insurance and the relative percentage of mortgage originations that are for purchased homes versus refinances. Typically, private mortgage insurance penetration is significantly higher on new mortgages for purchased homes than on the refinance of existing mortgages because average loan-to-value (“LTV”) ratios are higher on home purchases. Radian Guaranty’s share of the private mortgage insurance market is influenced by competition in that market and our ability to maintain or grow existing levels of new mortgage originations from our current customers and expand our customer base. We compete with other private mortgage insurers on the basis of price, terms and conditions, customer relationships, reputation, financial strength measures and overall service. Service-based competition includes effective and timely delivery of products, risk management services, timeliness of claims payments, training, loss mitigation efforts and management and field service expertise.
- *Losses*. Incurred losses represent the estimated future claim payments on newly defaulted insured loans as well as any change in our claim estimates for previously existing defaults. Our mortgage insurance incurred losses are driven primarily by new defaults and changes in the estimates we use to determine our losses, including estimates with respect to the likelihood, magnitude and timing of anticipated losses, and our estimate of the rate at which we expect defaults will ultimately result in paid claims. Other factors influencing incurred losses include:
  - The product mix of our total direct RIF (loans with higher risk characteristics generally result in more delinquencies and claims);
  - The average loan size (higher average loan amounts generally result in higher incurred losses);
  - The percentage of coverage on insured loans (higher percentages of insurance coverage generally result in higher incurred losses) and the presence of structural mitigants such as deductibles or stop losses;
  - Changes in housing values (declines in housing values negatively impact our ability to mitigate our losses by either paying the full claim amount and acquiring the property for resale or facilitating a sale of the property, and also may negatively affect a borrower’s willingness to continue to make mortgage payments when the home value is less than the mortgage balance);
  - The distribution of claims over the life cycle of a portfolio (historically, claims are relatively low during the first two years after a loan is originated and then increase substantially over a period of several years before declining; however, as happened with much of our legacy portfolio, several factors can impact and change this cycle, including the economic environment, the characteristics of the mortgage loan, the credit profile of the borrower, housing prices and unemployment rates); and
  - Our ability to mitigate potential losses through rescissions, denials, cancellations and the curtailment of claims submitted to us. Generally, we rescind insurance coverage when we conclude, through our review of the underwriting of a loan, that the loan was not originated in accordance with our underwriting guidelines. Generally, we deny claims when the documentation we receive is not sufficient to perfect the claim in accordance with our master insurance policy. In addition, we may cancel coverage or curtail claim payments when we identify servicer negligence, or we may make other adjustments to claims as permitted by our master insurance policy. These actions all reduce our incurred losses. Conversely, if our loss mitigation activities are successfully challenged at rates that are higher than expected, our incurred losses will increase. In general, our loss mitigation activities have been more frequent with respect to our legacy insured portfolio, including the historically poor underwriting years of 2005 through 2008.

- *Other Operating Expenses.* Our other operating expenses are affected by both the level of NIW, as well as the level of RIF. Additionally, in recent periods, our operating expenses have been impacted significantly by compensation expense associated with changes in the estimated fair value of certain of our long-term incentive awards that are settled in cash. The fair value of these awards, and associated compensation expense, is dependent, in large part, on our stock price at any given point in time.
- *Third-Party Reinsurance.* We use third-party reinsurance in our mortgage insurance business to manage capital and risk. When we enter into a reinsurance agreement, the reinsurer receives a premium and, in exchange, agrees to insure an agreed upon portion of incurred losses. This arrangement has the impact of reducing our earned premiums but also reduces our net RIF, which provides capital relief to the insurance subsidiary ceding the RIF and reduces our incurred losses by any incurred losses ceded in accordance with the reinsurance agreement. In addition, we often receive ceding commissions from the reinsurer as part of the transaction, which contributes to reducing our overall expenses. In the past, we also had entered into capital markets-based reinsurance transactions (“Smart Home”) designed to transfer all or a portion of the risk associated with certain higher risk mortgage insurance products. See Note 7 of Notes to Unaudited Condensed Consolidated Financial Statements for more information about our reinsurance arrangements.

### **Financial Guaranty**

- *Premiums.* We earn premiums on our financial guaranty insurance policies and on the other forms of credit protection we have provided. In our financial guaranty business, premiums on public finance exposures are generally paid as single up-front premiums and are earned over the life of the contract. Premiums on our structured finance contracts are generally paid on a periodic basis (monthly or quarterly installment premiums) and are earned on a monthly basis. In addition, we recognize the remaining unearned premium revenue when securities that we insure are redeemed or otherwise retired (we refer to this activity as “refundings”), which generally results in the termination of the financial guaranty policies insuring such securities. Furthermore, our earned premiums are reduced by premiums ceded through reinsurance agreements. Since we have discontinued writing new financial guaranty insurance, our premiums earned have been reduced commensurate with the decrease in our net par outstanding.
- *Net Par Outstanding.* Our net par outstanding represents principal risk exposure on insured contracts. As noted above, our net par outstanding has been declining since we discontinued writing new financial guaranty business in 2008. The decline in our net par outstanding is driven by scheduled maturities and permitted early terminations within our financial guaranty portfolio and negotiated commutations and other transactions that we have entered into to reduce our net par outstanding.

Factors outside of our control also may affect our net par outstanding. Low interest rates may cause the issuers of our public finance obligations to refinance the obligations that we insure, thereby reducing our net par outstanding. In addition, a majority of our financial guaranty net par outstanding is subject to termination at any time by our CDS counterparties or by our non-affiliated primary insurance customers that have ceded exposure to us. Various market factors, including declining default rates on the obligations that we have insured and the market’s perception of the increasing likelihood of our default on our own obligations, may make it economically attractive for our counterparties to exercise their early termination rights and cancel our insurance coverage, whereas rising default rates and a market perception of a decreasing likelihood that we will default on our own obligations, may make it less attractive for our counterparties to exercise such early termination rights.

- *Losses/Credit Performance.* Our financial guaranty incurred losses are driven primarily by economic conditions that affect the ability of the issuers of our insured obligations to meet such financial obligations and by changes in the assumptions used to determine our losses, including assumptions with respect to the likelihood, magnitude and timing of anticipated losses. Stronger economic conditions increase the likelihood that obligors will have the ability to pay interest and principal on the bonds we insure. Weaker economic conditions often place strains on the revenue flows available to pay interest and principal on our insured obligations. Other significant factors influencing defaults and incurred losses include:
  - Real estate values, which can affect the ability of municipalities and other governmental entities to generate sufficient tax revenues to satisfy their financial obligations;
  - The potential impact of federal, state and local budgetary constraints affecting funding and payments (including Medicare and Medicaid payments) to healthcare, long-term care, educational and other governmental and non-governmental entities whose obligations we insure;
  - The potential impact of threatened or actual government shutdowns or defaults on the payment of government-issued debt securities or other financial obligations;
  - Potential changes to entitlement programs, such as Social Security, Medicare and Medicaid, that could affect the ability of certain entities whose obligations we insure to receive adequate reimbursement for the services they provide and for individuals and entities to utilize the services provided by these entities;
  - Performance of commercial and residential mortgage loans and other types of indebtedness that we insure;
  - The movement of interest rates (increases in interest rates will increase the interest component of the variable rate obligations we insure, and as a result, will increase the strain on the obligors to make payments on these obligations); and
  - The performance of the primary insurers from whom we have either ceded reinsurance or who have the primary obligation to pay claims on our second-to-pay obligations; if such primary insurers have financial difficulties, they may be unable or unwilling to devote sufficient resources to loss mitigation efforts or could fail to pay claims on transactions where we have second-to-pay obligations.

While all of these factors could affect losses on the underlying transactions we insure, the structure of a transaction, including the level of subordination in such transaction available to absorb losses before we would incur losses, further impacts our ultimate loss on a particular transaction.

### **Other Factors Affecting Consolidated Results**

- *Investment Income.* Investment income is determined primarily by the investment balances held and the average yield on our overall investment portfolio.
- *Changes in Fair Value of Obligations.* Many of our structured finance, some of our public finance and our net interest margin securities (“NIMS”) contracts are accounted for as derivatives or variable interest entities (“VIEs”), which are carried at fair market value. Therefore, our results are impacted by changes in the fair value of these contracts. The estimated fair value of these obligations and instruments is measured as of a specific point in time and may be influenced by changes in interest rates, credit spreads (of both the underlying collateral as well as the credit spread for Radian Group), credit ratings, changes in regulations affecting the holders of such obligations or the value of obligations underlying our insured portfolio and other market, asset-class and transaction-specific conditions and factors that may be unrelated or only indirectly related to our obligation to pay future claims. The estimated changes in fair value of these obligations and instruments are reported in change in fair value of derivative instruments and net gains (losses) on other financial instruments in our statements of operations.

Radian Group’s credit spread reflects the perceived risk of default that investors associate with us, which we are required to consider when determining the fair market values of our obligations. A higher credit spread is indicative of a higher perception of risk. If all else remains constant, when our credit spread increases, or widens, the fair value liability of our insured obligations declines, and when our credit spread decreases, or tightens, the fair value liability of our insured obligations increases.

Because we generally do not settle our insurance contracts before maturity (other than in a negotiated termination), in the absence of actual credit losses on which we are obligated to make claim payments, we expect unrealized gains or losses related to changes in fair value to reverse before or at the maturity of these obligations. If we agree to settle obligations prior to maturity at amounts that are greater or less than their fair values at the time of settlement, it could result in the realization of additional gains or losses.

- *Net Gains (Losses) on Investments.* The recognition of realized investment gains or losses can vary significantly across periods as the activity is highly discretionary based on such factors as market opportunities, our tax and capital profile and overall market cycles that impact the timing of the sales of securities. Unrealized investment gains and losses arise primarily from changes in the market value of our investments that are classified as trading and these unrealized gains and losses are generally the result of interest rates or market credit spreads and may not necessarily result in economic gains or losses.

### **Results of Operations—Consolidated**

Radian Group serves as the holding company for our insurance subsidiaries and does not have any significant operations of its own. Because of this, our consolidated operating results primarily reflect the financial results and performance of our two business segments—mortgage insurance and financial guaranty. In addition, pretax income is also affected by “Other Factors Affecting Consolidated Results” described above. See “—Use of Non-GAAP Financial Measure” for more information regarding changes in fair value of derivative instruments expected to reverse over time. See also “—Results of Operations—Mortgage Insurance” and “—Results of Operations—Financial Guaranty” for the operating results of our two business segments.

The following table highlights selected information related to our consolidated results of operations for the three months ended March 31, 2014 and 2013:

(\$ in millions)	Three Months Ended March 31,		% Change
	2014	2013	2014 vs. 2013
Net income (loss)	\$ 202.8	\$ (187.5)	n/m
Net investment income	24.2	26.9	(10.0)%
Net gains (losses) on investments	64.5	(5.5)	n/m
Change in fair value of derivative instruments	50.1	(167.7)	n/m
Net gains (losses) on other financial instruments	0.7	(5.7)	n/m
Provision for losses	54.8	132.1	(58.5)
Policy acquisition costs	8.6	17.2	(50.0)
Other operating expenses	59.9	80.1	(25.2)
Interest expense	19.9	15.9	25.2
Income tax benefit	(0.2)	(14.7)	(98.6)
Adjusted pretax operating income (loss) (1)	91.1	(15.2)	n/m

n/m – not meaningful

(1) See “—Use of Non-GAAP Financial Measure” which follows.

*Net Income (Loss).* For the three months ended March 31, 2014, we had net income compared to a net loss for the same period in 2013. This was primarily due to net gains on investments and net gains in the change in the fair value of derivative instruments compared to net losses for both of these items in the comparable period of 2013, as well as a significant reduction in the provision for losses in 2014. Adjusted pretax operating income for the three months ended March 31, 2014 also improved from the same period of 2013, primarily due to the significant reduction in the provision for losses in 2014.

*Net Investment Income.* For the three months ended March 31, 2014, net investment income decreased compared to the same period in 2013 primarily due to a decline in dividend income and a significant decline in portfolio yields. Our current allocation to short-term and short duration investments remains high in anticipation of elevated near-term claim payments in our mortgage insurance segment and potential capital contributions from Radian Group to Radian Guaranty. This allocation, combined with certain sales of securities and subsequent reinvestment of longer duration securities in the low interest rate environment, has resulted in a lower yield profile for the portfolio

*Net Gains (Losses) on Investments.* The components of the net gains (losses) on investments for the periods indicated are as follows:

(In millions)	Three Months Ended March 31,	
	2014	2013
Net unrealized gains (losses) related to change in fair value of trading securities and other investments	\$ 68.3	\$ (19.3)
Net realized (losses) gains on sales	(3.8)	13.8
Net gains (losses) on investments	\$ 64.5	\$ (5.5)



*Change in Fair Value of Derivative Instruments.* The components of the gains (losses) included in change in fair value of derivative instruments for the periods indicated are as follows:

<u>(In millions)</u>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Net premiums earned—derivatives	\$ 3.5	\$ 5.0
Financial Guaranty credit derivatives	28.0	(175.7)
Financial Guaranty VIE derivative	20.1	3.0
Other	(1.5)	—
<b>Change in fair value of derivative instruments</b>	<b>\$ 50.1</b>	<b>\$ (167.7)</b>

The results for the three months ended March 31, 2014 reflect credit improvement in the underlying collateral in our non-corporate collateralized debt obligation (“CDO”) portfolio and improved pricing in the underlying assets of our VIEs. The results for the three months ended March 31, 2014 and 2013 also reflect a tightening of Radian Group’s five-year CDS spread by 35 basis points and 400 basis points, respectively, resulting in unrealized losses. See “Item 3. Quantitative and Qualitative Disclosures About Market Risk” for additional information about the impact of changes in Radian Group’s five-year CDS spread on the fair value of certain of our financial instruments.

*Impact of Radian’s Non-performance Risk on Consolidated Results*

Radian Group’s five-year CDS spread is an observable quantitative measure of our non-performance risk and is used by typical market participants to determine the likelihood that we will default on our obligations; the CDS spread that we actually use in the valuation of our specific fair value liabilities is typically based on the remaining term of the insured obligation, rather than five years. Non-performance risk is commonly measured by default probability, with a credit spread tightening indicating a lesser probability of default. Radian Group’s five-year CDS spread at March 31, 2014 implies a market view that there is a 21.1% probability that Radian Group will default on its obligations in the next five years, as compared to a 22.9% implied probability of default at December 31, 2013.

<u>(In basis points)</u>	<b>March 31, 2014</b>	<b>December 31, 2013</b>	<b>March 31, 2013</b>	<b>December 31, 2012</b>
Radian Group’s five-year CDS spread	288	323	513	913

The following tables quantify the impact of our non-performance risk on our derivative assets, derivative liabilities and net VIE liabilities (in aggregate by type) presented in our condensed consolidated balance sheets:

<u>(In millions)</u>	<b>Fair Value Liability before Consideration of Radian Non-Performance Risk March 31, 2014</b>	<b>Impact of Radian Non-Performance Risk March 31, 2014</b>	<b>Fair Value Liability Recorded March 31, 2014</b>
<b>Product</b>			
Corporate CDOs	\$ 26.0	\$ 23.5	\$ 2.5
Non-Corporate CDO-related (1)	357.6	155.7	201.9
Net interest margin securities (“NIMS”)-related (2)	5.2	2.1	3.1
<b>Total</b>	<b>\$ 388.8</b>	<b>\$ 181.3</b>	<b>\$ 207.5</b>

<u>(In millions)</u>	Fair Value Liability before Consideration of Radian Non-Performance Risk December 31, 2013	Impact of Radian Non-Performance Risk December 31, 2013	Fair Value Liability Recorded December 31, 2013
<b>Product</b>			
Corporate CDOs	\$ 30.4	\$ 29.0	\$ 1.4
Non-Corporate CDO-related (1)	409.7	178.7	231.0
NIMS-related (2)	5.0	2.2	2.8
Total	\$ 445.1	\$ 209.9	\$ 235.2

- (1) Includes the net fair value liability recorded within derivative assets and derivative liabilities and the net fair value liabilities included in our consolidated VIEs.
- (2) Includes NIMS VIE debt.

The estimated fair value of our insured credit derivatives and VIEs is measured as of a specific point in time and is influenced by changes in interest rates, credit spreads, credit ratings and other factors. Other factors that may cause a difference between the fair value of these obligations and our estimated credit loss payments include the effects of our non-performance risk and differing assumptions regarding discount rate and future performance, as well as the expected impact of our loss mitigation activities such as commutations. Because we have the ability to hold our financial guaranty contracts to maturity, changes in market spreads often are not indicative of our ultimate net credit loss payments with respect to these obligations. In the absence of actual credit losses on which we are obligated to make claim payments, we expect unrealized gains or losses related to changes in fair value to reverse before or at the maturity of these obligations. In addition, as we have done with other obligations, we may agree to settle some or all of these obligations prior to maturity at amounts that are greater or less than their fair values at the time of settlement, which could result in the realization of additional gains or losses.

The following table summarizes amounts related to insured obligations valued at fair value, as reflected on our condensed consolidated balance sheet at March 31, 2014 and the present value of our estimated credit loss recoveries on these obligations. Because we expect to have net recoveries on these obligations, we expect the fair value liability ultimately to reverse before or at the maturity of these transactions, and in addition, expect to recover amounts previously paid on these transactions.

<u>(In millions)</u>	NIMS and Other	Financial Guaranty Derivatives and VIEs	Total
<b>Balance Sheet</b>			
Other invested assets	\$ —	\$ 81.6	\$ 81.6
Derivative assets	8.9	5.6	14.5
Other assets	—	92.5	92.5
Total assets	8.9	179.7	188.6
Derivative liabilities (including VIE derivatives)	—	257.7	257.7
VIE debt - at fair value	3.1	92.4	95.5
Other liabilities	—	0.2	0.2
Total liabilities	3.1	350.3	353.4
Total fair value net assets (liabilities)	\$ 5.8	\$ (170.6)	\$ (164.8)
Present value of estimated credit loss payments (recoveries) (1)	\$ 6.5	\$ (74.7)	\$ (68.2)

- (1) Represents the present value of our estimated credit loss recoveries (net of estimated credit loss payments) for those transactions for which we currently anticipate paying net losses or receiving recoveries of losses already paid. The present value is calculated using a discount rate of approximately 1.9%, which approximates the average investment yield as reported in our most recently filed statutory financial statements. As illustrated above, expected recoveries for our insured financial guaranty credit derivatives and VIEs exceeded estimated credit loss payments for these transactions as of March 31, 2014.

*Other Operating Expenses.* Other operating expenses for the three months ended March 31, 2014 as compared to the three months ended March 31, 2013, reflect a lower impact related to changes in the estimated fair value of cash-settled long-term incentive awards that are valued relative to Radian Group's common stock price. If our stock price increases during a quarter, additional expense is recognized for these awards. Our stock price increased from \$14.12 at December 31, 2013 to \$15.03 at March 31, 2014, while the stock price increased from \$6.11 at December 31, 2012 to \$10.71 at March 31, 2013.

*Interest Expense.* For the three months ended March 31, 2014, interest expense increased compared to the same period in 2013, primarily due to the exchange of a portion of our 5.375% Senior Notes due June 2015 for a new series of 9.000% Senior Notes due June 2017 and the issuance of \$400 million principal amount of 2.250% Convertible Senior Notes due March 2019 with an effective rate of 6.25% in the first quarter of 2013.

*Income Tax Benefit.* The effective tax rate was (0.12)% for the three months ended March 31, 2014, compared to 7.28% for the three months ended March 31, 2013. The change from our statutory tax rate of 35% for each period was primarily due to the impact of the accounting for uncertainty of income taxes and changes in our overall valuation allowance against our deferred tax asset ("DTA"). Comparability between these interim periods is impacted given that we calculated our 2014 income tax benefit based on an estimated annualized effective tax rate for the full year 2014, compared to the 2013 tax benefit calculation, which was based on actual results of operations for 2013.

*Use of Non-GAAP Financial Measure.* In addition to the traditional GAAP financial measures, we have presented a non-GAAP financial measure for the consolidated company, "adjusted pretax operating income," among our key performance indicators to facilitate evaluation of our fundamental financial performance. This non-GAAP financial measure aligns with the way the Company's business performance is evaluated by both management and the board of directors. This measure has been established in order to increase transparency for the purposes of evaluating our core operating trends and enabling more meaningful comparisons with our peers. Although on a consolidated basis "adjusted pretax operating income (loss)" is a non-GAAP financial measure, we believe this measure aids in understanding the underlying performance of our operations. Our senior management, including our Chief Executive Officer (the Company's chief operating decision maker), uses adjusted pretax operating income (loss) as our primary measure to facilitate evaluation of the fundamental financial performance of the Company's business segments and to allocate resources to the segments. Management's use of this measure as its primary measure to evaluate segment performance began with the quarter ended March 31, 2014. Accordingly, for comparison purposes, we also present the applicable measures from the corresponding period of 2013 on a basis consistent with the current year presentation.

Adjusted pretax operating income adjusts GAAP pretax income to remove the effects of net gains (losses) on investments and other financial instruments and net impairment losses recognized in earnings. It also excludes gains and losses related to changes in fair value estimates on insured credit derivatives and includes the impact of changes in the present value of insurance claims and recoveries on insured credit derivatives, based on our ongoing insurance loss monitoring, as well as premiums earned on insured credit derivatives.

Although adjusted pretax operating income excludes certain items that have occurred in the past and are expected to occur in the future, the excluded items represent those that are: (1) not viewed as part of the operating performance of our primary activities; or (2) not expected to result in an economic impact equal to the GAAP measure. These adjustments, along with the reasons for their treatment, are described below.

- (1) *Change in fair value of derivative instruments*. Gains and losses related to changes in the fair value of insured credit derivatives are subject to significant fluctuation based on changes in interest rates, credit spreads (of both the underlying collateral as well as our credit spread), credit ratings and other market, asset-class and transaction-specific conditions and factors that may be unrelated or only indirectly related to our obligation to pay future claims. With the exception of the estimated present value of net credit (losses) recoveries incurred and net premiums earned on derivatives, discussed in items 2 and 3 below, we believe these gains and losses will reverse over time and consequently these changes are not expected to result in economic gains or losses. Therefore, these gains and losses are excluded from our calculation of adjusted pretax operating income.
- (2) *Estimated present value of net credit (losses) recoveries incurred*. The change in present value of insurance claims we expect to pay or recover on insured credit derivatives represents the amount of the change in credit derivatives from item 1 above, that we expect to result in an economic loss or recovery based on our ongoing loss monitoring analytics. Therefore, this item is expected to have an economic impact and is included in our calculation of adjusted pretax operating income. Also included in this item is the expected recovery of miscellaneous operating expenses associated with our consolidated VIEs.
- (3) *Net premiums earned on derivatives*. The net premiums earned on insured credit derivatives are classified as part of the change in fair value of derivative instruments discussed in item 1 above. However, since net premiums earned on derivatives are considered part of our fundamental operating activities, these premiums are included in our calculation of adjusted pretax operating income.
- (4) *Net gains (losses) on investments and other financial instruments*. The recognition of realized investment gains or losses can vary significantly across periods as the activity is highly discretionary based on the timing of individual securities sales due to such factors as market opportunities, our tax and capital profile and overall market cycles. Unrealized investment gains and losses arise primarily from changes in the market value of our investments that are classified as trading. These valuation adjustments may not necessarily result in economic gains or losses. We do not view them to be indicative of our fundamental operating activities. Trends in the profitability of our fundamental operating activities can be more clearly identified without the fluctuations of these realized and unrealized gains or losses. Therefore, these items are excluded from our calculation of adjusted pretax operating income.
- (5) *Net impairment losses recognized in earnings*. The recognition of net impairment losses on investments can vary significantly in both size and timing, depending on market credit cycles. We do not view them to be indicative of our fundamental operating activities. Therefore, these losses are excluded from our calculation of adjusted pretax operating income.

Adjusted pretax operating income is not a measure of total profitability, and therefore should not be viewed as a substitute for GAAP pretax income. Our definition of adjusted pretax operating income may not be comparable to similarly-named measures reported by other companies.

The following table provides a reconciliation of our non-GAAP financial measure for the consolidated company, adjusted pretax operating income (loss), to the most comparable GAAP measure, pretax income (loss):

<u>(In thousands)</u>	<b>Reconciliation of Consolidated Non-GAAP Financial Measure</b>	
	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Adjusted pretax operating income (loss):		
Mortgage Insurance	\$ 101,329	\$ (11,403)
Financial Guaranty	(10,239)	(3,834)
Adjusted pretax operating income (loss)	<u>\$ 91,090</u>	<u>\$ (15,237)</u>
Change in fair value of derivative instruments	50,086	(167,670)
Less: Estimated present value of net credit recoveries incurred	362	3,144
Less: Net premiums earned on derivatives	3,445	4,992
Change in fair value of derivative instruments expected to reverse over time	<u>46,279</u>	<u>(175,806)</u>
Net gains (losses) on investments	64,451	(5,505)
Net gains (losses) on other financial instruments	698	(5,675)
Pretax income (loss)	<u>\$ 202,518</u>	<u>\$ (202,223)</u>

### Results of Operations—Mortgage Insurance

#### *Quarter Ended March 31, 2014 Compared to Quarter Ended March 31, 2013*

The following table summarizes our mortgage insurance segment's results of operations for the three months ended March 31, 2014 and 2013:

<u>(\$ in millions)</u>	<b>Three Months Ended March</b>		<b>% Change</b>
	<b>31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2014 vs. 2013</b>
Adjusted pretax operating income (loss) (1)	\$ 101.3	\$ (11.4)	n/m
Net premiums written—insurance	213.0	217.3	(2.0)%
Net premiums earned—insurance	198.8	183.0	8.6
Net investment income	14.0	15.1	(7.3)
Provision for losses	49.2	132.0	(62.7)
Policy acquisition costs	7.0	11.7	(40.2)
Other operating expenses	50.4	65.8	(23.4)
Interest expense	5.4	2.7	100.0
Income tax (benefit) provision	—	—	n/m
Pretax income (loss)	—	—	n/m

n/m – not meaningful

(1) Our senior management uses adjusted pretax operating income (loss) as our primary measure to facilitate evaluation of the fundamental financial performance of the Company's business segments and to allocate resources to the segments.

*Adjusted Pretax Operating Income (Loss).* Our mortgage insurance segment had adjusted pretax operating income for the three months ended March 31, 2014, compared to adjusted pretax operating loss for the same period in 2013, primarily due to a significant reduction in the provision for losses, an increase in premiums earned and a reduction in other operating expenses.

### *NIW, IIF, RIF*

A key component of our current business strategy is to grow our mortgage insurance business by writing insurance on high-quality mortgages in the U.S. Consistent with this objective, we wrote \$6.8 billion of primary new mortgage insurance in the three months ended March 31, 2014, compared to \$10.9 billion in the three months ended March 31, 2013. The decrease in NIW for the three months ended March 31, 2014, compared to the three months ended March 31, 2013, is attributable to a decrease in the total mortgage originations market and increased competition in the mortgage insurance industry. As the level of refinance originations has declined and the purchase origination volume as a percentage of our total NIW has increased, the FICO distribution of our NIW is more concentrated in lower level FICO scores and the LTV distribution of our NIW is more concentrated in higher LTV categories.

Due to the recent increase in mortgage interest rates, the current volume of mortgage refinance business has significantly declined. With the impact of reduced refinance volume expected to continue in 2014, we expect our NIW for 2014 to continue to be negatively impacted by a reduction in the overall mortgage origination market and increased competition in the private mortgage insurance industry. These challenges are expected to be partially offset by improvement in the housing market, in particular increased purchase origination volume as compared to refinance originations, and continued increases in the penetration rate of private mortgage insurance in the overall insured mortgage market. While it remains difficult to project future NIW, based on revised mortgage origination projections from the Mortgage Bankers Association and other sources, we now expect that our new business volume for 2014 will be modestly lower than \$40 billion.

Since 2009, virtually all of our new mortgage insurance business production has been prime business. In addition, Fair Isaac Corporation (“FICO”) scores for the borrowers of these insured mortgages have increased and the average LTV on these mortgages has decreased (meaning that borrowers generally are making larger down payments in connection with the more recent mortgages that we are insuring), in both cases as compared to mortgages in our legacy portfolio. Our portfolio of business written since 2009 has been steadily increasing in proportion to our total portfolio of RIF. As of March 31, 2014, our 2009 through 2014 vintage portfolios represented approximately 62% of our total mortgage insurance portfolio compared to 60% at December 31, 2013. These origination years possess significantly improved credit characteristics compared to our legacy portfolios. The growth of the portion of our portfolio written beginning in 2009, together with continued improvement in the portfolio as a result of HARP refinancings (further described below), has resulted in significant improvement in the credit quality of our overall mortgage insurance portfolio. As a result, our expected future losses on our mortgage insurance portfolio written since 2009 are significantly lower than those experienced on our legacy portfolio, and therefore, the changing composition of our overall mortgage insurance portfolio should contribute to improvement in the mortgage insurance segment’s operating profitability.

In 2009, the GSEs began offering the Homeowner Affordable Refinance Program (“HARP”). HARP allows a borrower who is not delinquent to refinance a mortgage if the borrower has been unable to take advantage of lower interest rates because the borrower’s home has decreased in value. Radian Guaranty and other private mortgage insurers have agreed with the Federal Housing Finance Agency (“FHFA”) to facilitate the transfer of mortgage insurance on loans to be refinanced through HARP without regard to LTV. In November 2011, the FHFA extended the program and made enhancements to the HARP program (“HARP 2”) that expanded the number of borrowers who can qualify for refinancing. The changes implemented by the enhanced HARP 2 program have increased the number of borrowers who are eligible to benefit from the program and, as of March 31, 2014, approximately 11% of our total primary RIF had successfully completed a HARP refinance. The HARP 2 program has now been extended until December 31, 2015. We exclude HARP loans from our NIW for the period in which the refinance occurs; however, the HARP programs have had a positive impact on the overall credit quality and composition of our mortgage insurance portfolio given that the refinancing generally results in terms at which a borrower has a greater ability to pay and more financial flexibility to cover the loan obligations. During the three months ended March 31, 2014, new HARP loans accounted for \$0.6 billion of newly refinanced loans that were not included in Radian Guaranty’s NIW for the period, compared to \$2.5 billion for the same period of 2013.

On March 27, 2013, the FHFA announced its new streamlined loan modification initiative, which was effective as of that date. This new program eliminates the need for borrowers who are applying for modifications to document their hardship or financial information. Instead, borrowers must be at least 90 days delinquent and no more than 24 months delinquent on their mortgage to qualify for a loan modification. We believe this streamlined modification program will further assist delinquent borrowers. As of July 1, 2013, servicers were required to begin offering the modification program to eligible borrowers. The streamlined modification program is scheduled to end on August 1, 2015. We have written a small amount of NIW from this program since its inception in 2013.

The following tables provide selected information as of and for the periods indicated related to mortgage insurance NIW, RIF and IIF. Primary RIF and IIF amounts at March 31, 2014, include \$498 million and \$1,978 million, respectively, related to the loans which were in default (as of December 31, 2011) that are subject to the Master Transaction Agreement that we entered into with Freddie Mac (the "Freddie Mac Agreement") in August 2013, because we continue to receive premiums on the related loans and the insurance remains in force.

(\$ in millions)	Three Months Ended March 31,			
	2014		2013	
<b>Primary NIW</b>				
Prime	\$ 6,807	100.0%	\$ 10,905	100.0%
Alternative-A ("Alt-A") and A minus and below	1	—	1	—
Total Primary	\$ 6,808	100.0%	\$ 10,906	100.0%

(\$ in millions)	Three Months Ended March 31,			
	2014		2013	
<b>Total primary NIW by FICO Score</b>				
>=740	\$ 4,345	63.8%	\$ 8,210	75.3%
680-739	2,041	30.0	2,398	22.0
620-679	422	6.2	298	2.7
<=619	—	—	—	—
Total Primary	\$ 6,808	100.0%	\$ 10,906	100.0%

(\$ in millions)	Three Months Ended March 31,	
	2014	2013
<b>Percentage of primary NIW</b>		
Refinances	18%	48%
LTV (1)		
95.01% and above	0.9%	1.7%
90.01% to 95.00%	51.8%	39.8%
85.01% to 90.00%	34.4%	39.3%
80.01% to 85.00%	12.9%	19.2%
<b>Primary risk written</b>	\$ 1,722	\$ 2,589

(1) LTV ratio: The percentage of the original loan amount to the original value of the property.

<u>(\$ in millions)</u>	<b>March 31, 2014</b>		<b>December 31, 2013</b>		<b>March 31, 2013</b>	
<b>Primary IIF (1)</b>						
Flow	\$ 152,731	94.1%	\$ 151,383	93.9%	\$ 133,693	92.4%
Structured	9,637	5.9	9,857	6.1	10,950	7.6
Total Primary	<u>\$ 162,368</u>	<u>100.0%</u>	<u>\$ 161,240</u>	<u>100.0%</u>	<u>\$ 144,643</u>	<u>100.0%</u>
Prime	\$ 148,736	91.6%	\$ 147,072	91.2%	\$ 128,361	88.8%
Alt-A	8,317	5.1	8,634	5.4	10,027	6.9
A minus and below	5,315	3.3	5,534	3.4	6,255	4.3
Total Primary	<u>\$ 162,368</u>	<u>100.0%</u>	<u>\$ 161,240</u>	<u>100.0%</u>	<u>\$ 144,643</u>	<u>100.0%</u>

<b>Persistence (12 months ended)</b>	82.3%	81.1%	80.9%
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(1) Includes amounts related to loans subject to the Freddie Mac Agreement.

<u>(\$ in millions)</u>	<b>March 31, 2014</b>		<b>December 31, 2013</b>		<b>March 31, 2013</b>	
<b>Primary RIF (1)</b>						
Flow	\$ 38,252	94.6%	\$ 37,792	94.4%	\$ 33,027	93.2%
Structured	2,180	5.4	2,225	5.6	2,419	6.8
Total Primary	<u>\$ 40,432</u>	<u>100.0%</u>	<u>\$ 40,017</u>	<u>100.0%</u>	<u>\$ 35,446</u>	<u>100.0%</u>
Prime	\$ 37,159	91.9%	\$ 36,613	91.5%	\$ 31,565	89.1%
Alt-A	1,939	4.8	2,017	5.0	2,315	6.5
A minus and below	1,334	3.3	1,387	3.5	1,566	4.4
Total Primary	<u>\$ 40,432</u>	<u>100.0%</u>	<u>\$ 40,017</u>	<u>100.0%</u>	<u>\$ 35,446</u>	<u>100.0%</u>

(1) Includes amounts related to loans subject to the Freddie Mac Agreement.



(\$ in millions)	March 31, 2014		December 31, 2013		March 31, 2013	
<b>Total primary RIF by FICO score</b>						
Flow						
>=740	\$ 21,976	57.4%	\$ 21,525	57.0%	\$ 17,556	53.2%
680-739	11,158	29.2	11,019	29.2	9,865	29.9
620-679	4,459	11.7	4,555	12.0	4,801	14.5
<=619	659	1.7	693	1.8	805	2.4
<b>Total Flow</b>	<b>\$ 38,252</b>	<b>100.0%</b>	<b>\$ 37,792</b>	<b>100.0%</b>	<b>\$ 33,027</b>	<b>100.0%</b>
Structured						
>=740	\$ 590	27.1%	\$ 602	27.0%	\$ 647	26.7%
680-739	624	28.6	640	28.8	698	28.9
620-679	572	26.2	585	26.3	642	26.5
<=619	394	18.1	398	17.9	432	17.9
<b>Total Structured</b>	<b>\$ 2,180</b>	<b>100.0%</b>	<b>\$ 2,225</b>	<b>100.0%</b>	<b>\$ 2,419</b>	<b>100.0%</b>
Total						
>=740	\$ 22,566	55.8%	\$ 22,127	55.3%	\$ 18,203	51.3%
680-739	11,782	29.1	11,659	29.1	10,563	29.8
620-679	5,031	12.5	5,140	12.9	5,443	15.4
<=619	1,053	2.6	1,091	2.7	1,237	3.5
<b>Total Primary</b>	<b>\$ 40,432</b>	<b>100.0%</b>	<b>\$ 40,017</b>	<b>100.0%</b>	<b>\$ 35,446</b>	<b>100.0%</b>
<b>Primary RIF on defaulted loans</b>	<b>\$ 2,466</b>	<b>(1)</b>	<b>\$ 2,786</b>	<b>(1)</b>	<b>\$ 3,953</b>	

(1) Excludes risk related to loans subject to the Freddie Mac Agreement.

(\$ in millions)	March 31, 2014		December 31, 2013		March 31, 2013	
<b>Percentage of primary RIF</b>						
Refinances	29%		29%		32%	
Loan Type:						
Fixed	94.3%		94.1%		92.3%	
Adjustable rate mortgages						
Less than five years	2.2%		2.4%		3.2%	
Five years and longer	3.5%		3.5%		4.5%	
<b>Total primary RIF by LTV (1)</b>						
95.01% and above	\$ 4,008	9.9%	\$ 4,171	10.4%	\$ 4,494	12.7%
90.01% to 95.00%	17,767	44.0	17,239	43.1	13,988	39.5
85.01% to 90.00%	14,807	36.6	14,750	36.9	13,473	38.0
85.00% and below	3,850	9.5	3,857	9.6	3,491	9.8
Total Primary	<u>\$ 40,432</u>	<u>100.0%</u>	<u>\$ 40,017</u>	<u>100.0%</u>	<u>\$ 35,446</u>	<u>100.0%</u>
<b>Total primary RIF by policy year</b>						
2005 and prior	\$ 4,209	10.4%	\$ 4,461	11.1%	\$ 5,362	15.1%
2006	2,243	5.6	2,326	5.8	2,635	7.4
2007	5,064	12.5	5,247	13.1	5,876	16.6
2008	3,810	9.4	3,950	9.9	4,436	12.5
2009	1,363	3.4	1,448	3.6	1,855	5.2
2010	1,144	2.8	1,206	3.0	1,573	4.5
2011	2,165	5.4	2,263	5.7	2,735	7.7
2012	7,511	18.6	7,710	19.3	8,397	23.7
2013	11,210	27.7	11,406	28.5	2,577	7.3
2014	1,713	4.2	—	—	—	—
Total Primary	<u>\$ 40,432</u>	<u>100.0%</u>	<u>\$ 40,017</u>	<u>100.0%</u>	<u>\$ 35,446</u>	<u>100.0%</u>

(1) LTV ratio: The percentage of the original loan amount to the original value of the property.

*Net Premiums Written and Earned.* Net premiums written decreased for the three months ended March 31, 2014, compared to the same period of 2013, primarily resulting from a reduction in NIW in the first quarter of 2014.

Net premiums earned increased for the three months ended March 31, 2014, compared to the same period of 2013, primarily resulting from an increase in direct premiums earned as a result of an increase in NIW during 2013, which caused our IIF to grow significantly, and a decrease in premiums refunded in connection with rescissions in 2014 compared to 2013. The increase in net premiums earned in 2014 was partially offset by an increase in ceded premiums earned.

Our expected rate of return on our single premium business is lower than on our monthly premium business. Assuming all other factors remain constant, if loans prepay earlier than expected, then our profitability on these single premium policies is likely to be higher than anticipated. If loans are repaid later than expected, however, our profitability on these single premium policies is likely to be lower than anticipated. Prepayment speeds impact the expected profitability of our monthly premium business in the opposite direction. For our monthly premium business, earlier than anticipated prepayments reduce profitability. As a result, the ultimate profitability of our business is affected by the impact of mortgage prepayment speeds on the mix of business we write. Because prepayment speeds are difficult to project, our strategy has been to write a mix of single premium and monthly premium business, which we believe balances the overall impact on our results if actual prepayment speeds are significantly different from expectations. Approximately 73% and 27% of our NIW for the three months ended March 31, 2014 was written with monthly and single premiums, respectively, compared to 64% and 36%, respectively, for the comparable period of 2013.

Throughout this report, unless otherwise noted, RIF includes the amount ceded through reinsurance.

(\$ in thousands)	Three Months Ended March 31,	
	2014	2013
<b>First-Lien Captives</b>		
Premiums earned ceded to captives	\$ 3,508	\$ 5,152
% of total premiums	1.6%	2.6%
IIF subject to captives (1)	3.5%	5.8%
RIF subject to captives (2)	3.3%	5.7%
<b>Initial Quota Share Reinsurance ("QSR") Transaction</b>		
Ceded premiums written	\$ 5,304	\$ 6,122
% of premiums written	2.3%	2.5%
Ceded premiums earned	\$ 6,807	\$ 7,833
% of total premiums	3.2%	4.0%
Ceding commissions written	\$ 1,326	\$ 1,530
RIF included in Initial QSR Transaction (3)	\$ 1,289,856	\$ 1,471,580
<b>Second QSR Transaction</b>		
Ceded premiums written	\$ 7,293	\$ 16,440
% of premiums written	3.2%	6.7%
Ceded premiums earned	\$ 6,585	\$ 2,838
% of total premiums	3.1%	1.4%
Ceding commissions written	\$ 2,553	\$ 5,754
RIF included in Second QSR Transaction (3)	\$ 1,360,651	\$ 900,378

(1) IIF on captives as a percentage of total IIF.

(2) RIF on captives as a percentage of total RIF.

(3) RIF ceded under Reinsurance Transactions and included in primary RIF.

*Net Investment Income.* Our mortgage insurance net investment income decreased for the three months ended March 31, 2014, compared to the same period of 2013, primarily due to a significant decline in portfolio yields. Our current allocation to short-term and short duration investments remains high in anticipation of elevated near-term claim payments in our mortgage insurance segment. This allocation, combined with certain sales of securities and subsequent reinvestment of longer duration securities in the low interest rate environment, has resulted in a lower yield profile for the portfolio. All periods include an allocation to the mortgage insurance segment of net investment income from Radian Group based on relative GAAP equity of the mortgage insurance segment.

*Provision for Losses.* Our mortgage insurance provision for losses decreased significantly for the three months ended March 31, 2014, compared to the same period of 2013. The following table details the financial impact of the significant components of our provision for losses for the periods indicated:

<u>(In millions)</u>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
New defaults	\$ 77.0	\$ 108.7
Existing defaults, second-liens, loss adjustment expenses (“LAE”) and other (1)	(27.8)	23.3
Provision for losses	\$ 49.2	\$ 132.0

(1) Represents the provision for losses attributable to loans that were in default as of the beginning of each period indicated, including: (a) the change in reserves for loans that were in default status (including pending claims) as of both the beginning and end of each period indicated; (b) the net impact to provision for losses from loans that were in default as of the beginning of each period indicated but were either cured (“cures”), prepaid, or resulted in a paid claim or a rescission or denial during the period indicated; (c) the impact to our incurred but not reported (“IBNR”) reserve during the period related to changes in actual and estimated reinstatements of previously rescinded policies and denied claims, including potential reinstatements we are in the process of discussing with servicers; (d) second-lien loss reserves; and (e) LAE and other loss reserves.

Our mortgage insurance provision for losses for the three months ended March 31, 2014 decreased by \$82.8 million as compared to 2013. This decrease was driven primarily by a continued decline in new defaults and more favorable development in our estimate of future losses on default notices reported in prior years, mainly due to higher claim curtailments, as discussed below, and cures for which we experienced higher rates in 2014, as reflected in the rollforward of primary loans in default shown below.

Our first-lien primary default rate at March 31, 2014 was 6.3% compared to 10.9% at March 31, 2013. Our primary defaulted inventory comprised 53,119 loans at March 31, 2014, compared to 85,109 loans at March 31, 2013, representing a 37.6% decrease. The Freddie Mac Agreement contributed to this decrease by eliminating Radian Guaranty’s claim exposure on delinquent loans subject to the Freddie Mac Agreement. Our primary defaulted inventory declined by an additional 4% in April 2014 from March 31, 2014. In addition to the impact of the Freddie Mac Agreement, the reduction in our primary defaulted inventory is the result of the total number of defaulted loans: (1) that have cured; (2) for which claim payments have been made; or (3) that have resulted in net insurance rescissions and claim denials, collectively exceeding the total number of new defaults on insured loans. Despite this positive trend, which we expect to continue, our overall primary default rates remain elevated compared to historical levels, driven primarily by the poor performance of our legacy portfolio.

Since 2007, a slowdown in mortgage foreclosures has contributed to the sustained high level of our defaulted inventory. This slowdown has resulted in more defaults remaining unresolved for a longer period of time than had historically been the case. New primary defaults for the three months ended March 31, 2014 decreased 18% compared to the same period in 2013. Although significant uncertainty remains, we currently expect total new defaults for 2014 to decrease approximately 16% as compared to 2013.

As discussed above, the time it has taken to cure or otherwise resolve a delinquent loan has been prolonged. Consequently, in recent years, our primary defaulted inventory experienced an increase in its weighted average age, and because we apply higher estimated “default to claim rates” (rate at which defaulted loans are expected to result in claim) on our more aged delinquent loans, this has resulted in additional incurred losses. In addition, our estimated rates of insurance rescissions and claim denials have declined in recent periods after a period of elevated rates. Our aggregate weighted average net default to claim rate assumption for our primary loans used in estimating our reserve for losses, which is net of estimated denials and rescissions, was approximately 48% at March 31, 2014, compared to 51% at March 31, 2013.

The following tables show additional information about our primary loans in default as of the dates indicated:

March 31, 2014							
(\$ in thousands)	#	%	Projected Default to Claim Rate		Cure % During the 1st Quarter	Reserve for Losses	% of Reserve
			Gross (1)	Net (2)			
			%	%			
<b>Missed payments:</b>							
Three payments or less	10,958	20.6%	24%	22%	36.4%	\$ 111,488	8.2%
Four to eleven payments	11,862	22.3	48	44	18.1	241,966	17.9
Twelve payments or more	22,330	42.1	57	50	4.5	638,335	47.0
Pending claims	7,969	15.0	100	88	0.6	365,639	26.9
Total	<u>53,119</u>	<u>100.0%</u>	54%	48%		1,357,428	<u>100.0%</u>
IBNR and other						347,674	
LAE						50,684	
Total primary reserves						<u>\$ 1,755,786</u>	

March 31, 2013							
(\$ in thousands)	#	%	Projected Default to Claim Rate		Cure % During the 1st Quarter	Reserve for Losses	% of Reserve
			Gross (1)	Net (2)			
			%	%			
<b>Missed payments:</b>							
Three payments or less	13,945	16.4%	25%	23%	34.8%	\$ 149,865	6.6%
Four to eleven payments	18,548	21.8	49	45	14.0	406,486	17.8
Twelve payments or more	35,202	41.4	57	48	4.0	949,269	41.6
Pending claims	17,414	20.4	100	88	0.2	776,625	34.0
Total	<u>85,109</u>	<u>100.0%</u>	59%	51%		2,282,245	<u>100.0%</u>
IBNR and other						247,526	
LAE						59,739	
Total primary reserves						<u>\$ 2,589,510</u>	

- (1) Represents the weighted average default to claim rate before consideration of estimated rescissions, denials and reinstatements of rescissions and denials for each category of defaulted loans.
- (2) Net of estimate of rescissions, denials and reinstatements of rescissions and denials.

The following table shows the number of primary and pool loans that we have insured, the number of loans in default and the percentage of loans in default as of the dates indicated:

	March 31, 2014	December 31, 2013	March 31, 2013
<b>Default Statistics—Primary Insurance:</b>			
Total Primary Insurance			
Prime			
Number of insured loans	746,598	741,554	683,227
Number of loans in default	32,708	37,932	55,490
Percentage of loans in default	4.38%	5.12%	8.12%
Alt-A			
Number of insured loans	43,018	44,905	51,981
Number of loans in default	10,173	11,209	14,833
Percentage of loans in default	23.65%	24.96%	28.54%
A minus and below			
Number of insured loans	39,338	40,930	47,656
Number of loans in default	10,238	11,768	14,786
Percentage of loans in default	26.03%	28.75%	31.03%
Total Primary			
Number of insured loans (1)	839,802	839,249	782,864
Number of loans in default (2)	53,119	60,909	85,109
Percentage of loans in default	6.33%	7.26%	10.87%
<b>Default Statistics—Pool Insurance:</b>			
Number of loans in default	9,814	11,921	16,750

(1) Includes 10,848 and 11,860 insured loans subject to the Freddie Mac Agreement at March 31, 2014 and December 31, 2013, respectively.

(2) Excludes 6,022 and 7,221 loans that are in default at March 31, 2014 and December 31, 2013, respectively, that are subject to the Freddie Mac Agreement, and for which we no longer have claims exposure.

The following table shows a rollforward of our primary loans in default:

	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Beginning default inventory	60,909	93,169
Plus: New defaults (1)	12,113	14,846
Less: Cures (1)	13,645	16,897
Less: Claims paid (2)	6,049	5,560
Less: Rescissions (3)	181	187
Less: Denials (4)	28	262
Ending default inventory	<u>53,119</u>	<u>85,109</u>

(1) Amounts reflected are compiled monthly based on reports received from loan servicers. The number of new defaults and cures presented includes the following monthly defaults that both defaulted and cured within the periods indicated:

	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Intra-period new defaults	5,332	6,286

- (2) Includes those charged to a deductible or captive.
- (3) Net of any previously rescinded policies or denied claims that were reinstated during the period. Such reinstated rescissions may ultimately result in a paid claim.
- (4) Net of any denied claims that were reinstated during the period. Such previously denied but reinstated claims are generally reviewed for possible rescission prior to any claim payment.

Our loss reserve estimate incorporates our future expectations based on our recent experience with respect to the number of claims that have been denied due to the policyholder's failure to submit sufficient documentation to perfect a claim within the time period permitted under our master insurance policy and also incorporates our future expectations based on our recent experience with respect to the number of insurance certificates that ultimately will be rescinded due to fraud, underwriter negligence or other factors. Our mortgage insurance reserves also incorporate, for future rescissions and denials on defaulted loans, our expectations regarding the number of policies that we expect to reinstate as a result of our claims rebuttal process (see below for more information). Our current level of rescissions and denials remains elevated compared to historical levels, primarily due to legacy portfolio loans that remain in our defaulted inventory, as well as our efforts to review a substantial portion of our claims related to legacy portfolio loans for potential rescissions or denials. While the level of rescissions and denials has been declining in recent periods as our defaulted legacy portfolio continues to decline, we expect the level of rescissions and denials to remain elevated compared to historical levels as long as our legacy portfolio comprises a significant percentage of our defaulted inventory.

The table below shows the details related to the number of rescinded policies and denied claims for the periods indicated. Recent trends in insurance rescissions and claim denial activity reflect a decrease in the number of policies rescinded and claims denied, and an overall increase in the number of claims denied that subsequently have been perfected and reinstated. This increase in reinstated denials is partly due to lenders and servicers challenging a greater number of denials, as well as the overall effectiveness of these challenges based on their ability to produce new or additional information that supports a perfection of a claim payment.

	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Rescinded policies:</b>		
Rescinded	(212)	(441)
Reinstated	31	254
<b>Denied claims:</b>		
Denied	(1,281)	(2,106)
Reinstated	1,253	1,844
<b>Total net rescissions and denials</b>	<b>(209)</b>	<b>(449)</b>

The following table illustrates the impact of estimated future insurance rescissions and claim denials (net of estimated reinstatements) on our loss reserve estimates as of the dates indicated:

<b>(In millions)</b>	<b>March 31, 2014</b>	<b>December 31, 2013</b>	<b>March 31, 2013</b>
Decrease to our loss reserve due to estimated future rescissions and denials	\$ 219	\$ 247	\$ 392

The following table illustrates the amount of first-lien claims submitted to us for payment that were rescinded or denied, net of any reinstatements of previously rescinded policies or denied claims for the periods indicated:

<b>(In millions)</b>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Rescissions	\$ 16.1	\$ 15.3
Denials	12.2	27.2
<b>Total first-lien claims submitted for payment that were rescinded or denied (1)</b>	<b>\$ 28.3</b>	<b>\$ 42.5</b>

(1) Includes an amount related to a small number of submitted claims that were subsequently withdrawn by the insured.

Our reported rescission and denial activity in any given period is subject to challenge by our lender and servicer customers. We expect that a portion of previously rescinded policies will be reinstated and previously denied claims will be resubmitted with the required documentation and ultimately paid; therefore, we have incorporated this expectation into our IBNR reserve estimate. Our IBNR reserve estimate was \$288.2 million and \$281.9 million at March 31, 2014 and December 31, 2013, respectively. As of March 31, 2014, the IBNR reserve estimate of \$288.2 million includes an estimate of future reinstatements of previously denied claims, rescinded policies and claim curtailments of \$163.8 million, \$93.3 million, and \$13.4 million, respectively. These reserves relate to \$266.9 million of claims that were denied within the preceding 12 months, \$362.5 million of policies rescinded within the preceding 24 months, and \$80.2 million of claim curtailments within the preceding 24 months, as well as a significant number of additional denials and rescissions that were denied or rescinded in earlier periods but remain the subject of continuing settlement discussions with certain of our lender and servicer customers.



Until a liability associated with such activities or discussions becomes probable and can be reasonably estimated, we consider our claim payments or our rescissions, denials and curtailments to be resolved for financial reporting purposes. Under the accounting standard regarding contingencies, an estimated loss is accrued only if we determine that the loss is probable and can be reasonably estimated. For the first quarter of 2014, a significant portion of our IBNR estimate of \$288.2 million relates to one servicer, with whom we are currently in settlement discussions regarding a large population of disputed rescissions, denials, curtailments and potential insurance cancellations. For these populations, we have determined that a settlement is probable and that a loss can be reasonably estimated, and have reflected our best estimate of the expected loss related to the populations under discussion with this servicer in our financial statements, primarily as a component of our IBNR reserve. While our reserves include our best estimate of this loss, the outcome of the discussions or potential legal proceedings that could ensue is uncertain, and it is reasonably possible that a loss exists in excess of the amount accrued. Due to the dynamic nature of these discussions, the range of factors that could impact settlement negotiations and the inherent uncertainty of the outcome of such matters, we cannot estimate the amount of any additional loss that is reasonably possible.

Generally, we estimate our claim liability related to the potential future reinstatement of previously denied claims and rescinded policies by estimating an initial gross reinstatement rate at the time of denial or rescission, which then declines over a 12- or 24-month timeframe based on our expectation that there is a reduced likelihood that a reinstatement will occur as time passes from our initial decision regarding a denial or rescission. As of March 31, 2014, for previously denied claims, this initial gross reinstatement assumption begins at approximately 60% and declines to 0% after 12 months, while for previously rescinded policies, the initial assumed reinstatement rate begins at approximately 20% and declines to 0% after 24 months. Our IBNR reserve estimate also includes the projected potential impact from future estimated rescissions on reinstated denials. Therefore, at any particular point in time, our IBNR reserve estimate with respect to previously rescinded policies or denied claims is affected not only by our initial reinstatement assumption, but also by the length of time since the denial or rescission, our estimated likelihood of such reinstatements resulting in a paid claim, and the expected claim severity on such paid claims, as well as the potential outcome of any discussions with our lender and servicer customers regarding such rescissions or denials. In addition, as of March 31, 2014, our IBNR reserve estimate incorporates an ultimate overturn rate assumption of approximately 30% for previously curtailed claims.

The following table shows the projected net cumulative denial and rescission rates in our first-lien portfolio, net of both actual and expected reinstatements, as of March 31, 2014, with respect to claims received in each quarter indicated below:

<b>Claim Received Quarter</b>	<b>Projected Net Cumulative Rescission/Denial Rate for Each Quarter (1)</b>	<b>Percentage of Total Claims Resolved (2)</b>
Q3 2011	30.5%	100%
Q4 2011	26.6%	100%
Q1 2012	23.5%	100%
Q2 2012	21.1%	99%
Q3 2012	18.3%	98%
Q4 2012	17.1%	95%
Q1 2013	17.0%	90%
Q2 2013	17.3%	86%
Q3 2013	15.1%	81%

(1) Projected net cumulative rescission/denial rates represent the ratio of claims rescinded or denied to claims received (by claim count). Rescissions and denials are net of actual reinstatements, plus our current estimate for expected reinstatements of previously rescinded policies or denied claims (excluding certain potential reinstatements we are in the process of discussing with servicers). These projected amounts represent the cumulative rates for each quarter as of March 31, 2014. Until all of the claims received during the periods shown have been internally resolved, the rescission/denial rates for each quarter will be subject to change; these rates also will remain subject to change based on differences between estimated and actual reinstatements of previously rescinded policies or denied claims.

- (2) The percentage of claims resolved for each quarter presented in the table above represents the number of claims that have been internally resolved as a percentage of the total number of claims received for that specific quarter. A claim is considered internally resolved when it is either paid or it is concluded that the claim should be denied or rescinded, though such denials and rescissions could be challenged and potentially reinstated or overturned. For the fourth quarter of 2013 and the first quarter of 2014, a significant portion of claims received for those quarters have not been internally resolved; therefore, we do not believe the projected net cumulative rescission/denial rates for those periods are presently meaningful.

The following table shows information regarding our reserve for losses and reserve for premium deficiency (“PDR”) as of the dates indicated:

<u>(In thousands)</u>	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
<b>Reserves for losses by category:</b>		
Prime	\$ 790,529	\$ 937,307
Alt-A	351,695	384,841
A minus and below	189,453	215,545
IBNR and other	347,674	347,698
LAE	50,684	51,245
Reinsurance recoverable (1)	25,751	38,363
<b>Total primary reserves</b>	<b>1,755,786</b>	<b>1,974,999</b>
Pool	123,596	169,682
IBNR and other	5,679	8,938
LAE	4,517	5,439
<b>Total pool reserves</b>	<b>133,792</b>	<b>184,059</b>
<b>Total first-lien reserves</b>	<b>1,889,578</b>	<b>2,159,058</b>
Second-lien and other (2)	4,382	5,295
<b>Total reserve for losses</b>	<b>\$ 1,893,960</b>	<b>\$ 2,164,353</b>
<b>PDR on second-liens</b>	<b>\$ 2,251</b>	<b>\$ 1,785</b>

- (1) Primarily represents ceded losses on captive transactions and the Reinsurance Transactions.  
(2) Does not include second-lien PDR.

The following table shows information regarding our average loss reserves per default:

	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
<b>First-lien reserve per default (1)</b>		
Primary reserve per default excluding IBNR and other	\$ 26,509	\$ 26,717
Pool reserve per pool default excluding IBNR and other (2)	13,054	14,690

- (1) Calculated as total reserves excluding IBNR and other divided by total defaults.  
(2) If calculated before giving effect to deductibles and stop losses in pool transactions, the pool reserve per default at March 31, 2014 and December 31, 2013 would be \$22,172 and \$24,640, respectively.

Total mortgage insurance claims paid of \$306.9 million for the three months ended March 31, 2014 have increased from claims paid of \$283.4 million in the fourth quarter of 2013 and decreased slightly from \$309.9 million in the first quarter of 2013. The increase in the three months ended March 31, 2014 compared to the fourth quarter of 2013 is primarily due to greater efficiencies in our claims review process, which have allowed us to pay valid claims more quickly than in previous periods. We currently expect claims paid to be between \$900 million and \$1.0 billion in 2014.

Notwithstanding our process improvements, we continue to experience the effects of the foreclosure backlogs, servicer delays and loan modification programs that were prevalent during the economic downturn and have resulted in a reduced number of defaults going to claim.

In addition, as part of our claims review process, we assess whether defaulted loans were serviced appropriately in accordance with our insurance policies and servicing guidelines. To the extent a servicer has failed to satisfy its servicing obligations, our policies provide that we may curtail the claim payment for such default, and in some circumstances, cancel coverage or deny the claim. Since 2011, claim curtailments due to servicer noncompliance with our insurance policies and servicing guidelines have increased both in frequency and in size, which has contributed to a reduction in the severity of our claim payments during this period. Claim curtailments due to servicer noncompliance with our insurance policies and servicing guidelines were approximately \$14.0 million for the three months ended March 31, 2014, compared to approximately \$7.8 million in the comparable period of 2013. While we cannot give assurance regarding the extent or level at which such claim curtailments will continue, we expect the trend of elevated claim curtailments to continue in light of well publicized issues in the servicing industry and our existing legacy portfolio of aged defaults.

The following table shows claims paid by product and average claims paid by product for the periods indicated:

<u>(In thousands)</u>	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
<b>Net claims paid:</b>		
Prime	\$ 194,718	\$ 200,517
Alt-A	46,191	49,091
A minus and below	33,286	27,486
<b>Total primary claims paid</b>	<b>274,195</b>	<b>277,094</b>
Pool	30,863	30,949
Second-lien and other	727	1,884
Subtotal	305,785	309,927
Impact of captive terminations	1,156	—
<b>Total net claims paid</b>	<b>\$ 306,941</b>	<b>\$ 309,927</b>
<b>Average net claim paid (1):</b>		
Prime	\$ 44.1	\$ 49.0
Alt-A	54.9	60.1
A minus and below	36.7	37.6
<b>Total average net primary claim paid</b>	<b>44.5</b>	<b>49.1</b>
Pool	60.3	73.5
Second-lien and other	20.8	22.2
<b>Total average net claim paid</b>	<b>\$ 45.6</b>	<b>\$ 50.4</b>
Average direct primary claim paid (2)	\$ 46.2	\$ 51.4
Average total direct claim paid (2)	\$ 47.2	\$ 52.6

(1) Net of reinsurance recoveries and without giving effect to captive terminations.

(2) Before reinsurance recoveries and without giving effect to captive terminations.

*Policy Acquisition Costs.* Policy acquisition costs for the three months ended March 31, 2013 reflect \$4.2 million of additional amortization as a result of a decrease in our persistency rate during that quarter. There was an immaterial amount of additional amortization in the first quarter of 2014.

*Other Operating Expenses.* Our other operating expenses for the three months ended March 31, 2014, compared to the same period in 2013, reflect a lower impact related to the changes in the estimated fair value of cash-settled long-term incentive awards that are valued relative to Radian Group's common stock price. If our stock price increases during a quarter, additional expense is recognized for these awards. Our stock price increased from \$14.12 at December 31, 2013 to \$15.03 at March 31, 2014, while the stock price increased from \$6.11 at December 31, 2012 to \$10.71 at March 31, 2013.

## Results of Operations—Financial Guaranty

Since 2008, when we ceased writing new financial guaranty business, we have significantly reduced our financial guaranty operations and have reduced our financial guaranty net par exposures in order to mitigate uncertainty, maximize the ultimate capital and liquidity available for our mortgage insurance business and accelerate our access to that capital and liquidity. In addition to the normal amortization or scheduled maturity of our financial guaranty insured portfolios, this reduction has been achieved primarily through risk commutations, ceded reinsurance, discounted insured bond purchases and transaction settlements and terminations.

### Financial Guaranty Portfolio

#### Net Par Outstanding

The following tables show the distribution of our financial guaranty segment's net par outstanding, by type of exposure, as a percentage of total net par outstanding and the related net claim (asset) liability and fair value net liability as of the dates indicated:

Type of Obligation	March 31, 2014			
	Net Par Outstanding (1)	% of Total Net Par Outstanding (1)	Net Claim (Asset) Liability (2)	Fair Value Net Liability (3)
	(In billions)		(In millions)	(In millions)
<b>Public finance:</b>				
General obligation and other tax supported (4)	\$ 5.2	22.9%	\$ 14.8	\$ 0.2
Healthcare and long-term care	2.3	10.1	12.6	1.0
Water/sewer/electric gas and investor-owned utilities	1.3	5.7	(1.6)	1.5
Education	1.1	4.9	(3.9)	—
Airports/transportation	0.9	4.0	—	28.6
Escrowed transactions (5)	0.8	3.5	—	—
Housing	0.1	0.4	—	—
Other public finance (6)	0.5	2.2	(13.0)	0.1
Total public finance (7)	12.2	53.7	8.9	31.4
<b>Structured finance:</b>				
CDO	9.8	43.3	2.2	164.6
Asset-backed obligations	0.6	2.6	16.7	8.0
Other structured (8)	0.1	0.4	—	0.3
Total structured finance	10.5	46.3	18.9	172.9
Total	\$ 22.7	100.0%	\$ 27.8	\$ 204.3

December 31, 2013

Type of Obligation	Net Par	% of Total	Net Claim (Asset)	Fair Value
	Outstanding (1)	Net Par	Liability (2)	Net
	(In billions)	Outstanding (1)	(In millions)	Liability (3)
				(In millions)
<b>Public finance:</b>				
General obligation and other tax supported (4)	\$ 5.3	22.2%	\$ 12.9	\$ 0.2
Healthcare and long-term care	2.4	10.0	11.1	0.8
Water/sewer/electric gas and investor-owned utilities	1.3	5.4	(9.6)	1.2
Education	1.1	4.6	(4.2)	—
Airports/transportation	0.9	3.8	(0.5)	27.5
Escrowed transactions (5)	0.9	3.8	—	—
Housing	0.1	0.4	—	—
Other public finance (6)	0.5	2.1	(12.9)	0.4
Total public finance (7)	12.5	52.3	(3.2)	30.1
<b>Structured finance:</b>				
CDO	10.7	44.8	2.9	193.4
Asset-backed obligations	0.6	2.5	19.6	8.6
Other structured (8)	0.1	0.4	—	0.2
Total structured finance	11.4	47.7	22.5	202.2
Total	\$ 23.9	100.0%	\$ 19.3	\$ 232.3

- (1) Represents our exposure to the aggregate outstanding principal on insured obligations. We are also responsible for the timely payment of interest on substantially all of our public finance and our non-corporate CDO structured finance obligations. For our insured corporate CDOs and CDOs of collateralized mortgage-backed securities (“CMBS”), net par outstanding represents the notional amount of credit protection we are providing on a pool of obligations.
- (2) A net claim liability is recorded on the balance sheet when there is evidence that deterioration has occurred and the net present value of our expected losses for a particular policy exceeds the unearned premium reserve for that policy. The claim liability reported is net of estimated salvage and subrogation, which may result in a net claim asset.
- (3) Represents the net (asset) liability recorded within derivative assets or derivative liabilities for derivative contracts, or the net (asset) liability recorded within VIE debt and other financial statement line items for financial guaranty consolidated VIEs.
- (4) Includes \$1.4 billion and \$1.5 billion at March 31, 2014 and December 31, 2013, respectively, of tax supported revenue bonds.
- (5) Escrowed transactions are legally defeased bond issuances where cash or U.S. government securities, in an amount sufficient to pay remaining obligations under such bonds, have been deposited in an escrow account for the benefit of the bond holders. Although we have little to no remaining credit risk on these transactions, they remain outstanding for GAAP purposes.
- (6) Represents other types of municipal obligations, including human service providers, second-to-pay international public finance, non-profit institutions, project finance accommodations and stadiums, none of which individually constitutes a material amount of our financial guaranty net par outstanding.
- (7) Includes \$2.4 billion at March 31, 2014 and December 31, 2013, of international public finance insured obligations (which includes sovereign and sub-sovereign (collectively, “Sovereign”) indebtedness, of which \$102.0 million and \$101.2 million at March 31, 2014 and December 31, 2013, respectively, is related to Greece, Spain, Italy, Hungary, Portugal and Ireland (collectively, the “Stressed European Countries”).
- (8) Represents other types of structured finance obligations, including collateralized guaranteed investment contracts or letters of credit, foreign commercial assets and life insurance securitizations, none of which individually constitutes a material amount of our financial guaranty net par outstanding.

In addition to our net par outstanding, we continue to have exposure to trade credit reinsurance and surety insurance and reinsurance. This exposure to these lines of business is measured using probable maximum loss (“PML”), which is the anticipated value of the largest potential loss affecting the insured exposure under a highly stressed scenario, while giving effect to any protective features (i.e. reinsurance or salvage). Based on our estimates, we believe the PML for our remaining trade credit and surety exposure was not material at March 31, 2014, and has not been material for the past several years. However, as discussed in Note 15 of Notes to Unaudited Condensed Consolidated Financial Statements—Commitments and Contingencies— *Other*, we recently received claims relating to certain surety bonds, which we are in the process of disputing.

### *Credit Performance/Credit Quality*

Unless otherwise indicated, the ratings of our financial guaranty obligations that are referenced in this report have been developed internally.

At March 31, 2014, the percentage of our total net par outstanding of obligations rated AAA, BBB and below investment grade (“BIG”) was 36.3%, 34.2% and 10.9%, respectively, compared to 38.5%, 34.7% and 9.2%, respectively, at December 31, 2013.

During the first quarter of 2014, the AAA and BBB ratings categories of our insured portfolio experienced the largest reductions in both net par outstanding and as a percentage of our total net par outstanding, while the BIG ratings category experienced the largest increase in both net par outstanding and as a percentage of our total net par outstanding. The reductions in our AAA net par outstanding was primarily due to a counterparty terminating one AAA-rated CDO CMBS transaction on a walkaway basis (meaning that our counterparty was not obligated to pay any unaccrued premium or other amount to terminate the transaction) and the scheduled maturity of one AAA-rated corporate CDO. The net par reduction in the BBB ratings category and the increase in the BIG ratings categories were primarily due to the downgrade of the \$434 million net par outstanding of our insured indebtedness issued by the Commonwealth of Puerto Rico (“Puerto Rico”) and certain of its agencies and instrumentalities (our “Puerto Rico Exposure”) that had been rated investment grade to BIG during the first quarter of 2014. See *Public Finance* below for additional information regarding our Puerto Rico Exposure.

*Public Finance.* Our public finance insured portfolio continues to experience stress due to the current economic environment. In general, municipal governments have been negatively impacted by the most recent recession and subsequent period of limited economic growth. For example, there have been several municipal defaults and bankruptcy filings since the beginning of 2012.

In recent years, more hospitals have been experiencing a decrease in patient revenues as a result of a significant decline in patient volumes, increased charity care and limited increases in commercial and government reimbursements, particularly those from Medicare. Many healthcare institutions are reporting that further expense reduction efforts are unrealistic and that operating losses are expected as healthcare inflation outpaces weak revenue growth. We are beginning to see the negative impact on our insured hospitals’ operating margins due to increased operating expenses, declines in patient volumes, decreases in reimbursements by government providers and delays in rendering reimbursements to hospitals. This trend is likely to continue at least through the remainder of 2014 and could result in further credit deterioration and require increases in our net claim liability and loss reserves related to our healthcare credits. While the impact of the implementation of the Patient Protection and Affordable Care Act (the “ACA”) on operating expenses, patient volumes and the level of charity care remains uncertain, it could result in unintended negative consequences, which could add to the financial burden of hospitals and other healthcare providers.

We have experienced some credit deterioration in our insured portfolio of other tax-supported bond transactions, in particular, those that are payable from real estate tax revenues derived from the value of real estate in narrowly defined special districts or from special assessments for improvements on certain properties. Declining property values have reduced the assessed value of the tax base in these jurisdictions, resulting in reduced tax revenues being available to pay interest and principal on these insured bonds. Where property values begin to increase, as has occurred recently in certain areas, there often is a lag between the rise of property values and the realization of corresponding higher tax revenues. We may experience further credit deterioration in these transactions, which would increase the likelihood that ultimately we would be required to make claim payments with respect to these bonds, especially those from special districts.

As of March 31, 2014, we had an aggregate of \$452.2 million of net par outstanding (excluding escrowed transactions) related to our Puerto Rico Exposure. Included in our Puerto Rico Exposure as of March 31, 2014 is \$239.4 million that is supported by the general obligations of Puerto Rico, facility lease payments by Puerto Rican governmental entities guaranteed by Puerto Rico or loan repayments of municipalities supported by Puerto Rico appropriations in the case of debt issued by the Puerto Rico Municipal Finance Agency. The remaining \$212.8 million of our Puerto Rico Exposure as of March 31, 2014 is secured by pledged revenues such as tolls, special taxes, electric, water and sewer utility revenues. All of our Puerto Rico Exposure is on a secondary market or assumed basis, which may limit the availability of certain remedies to us.

In February 2014, Standard & Poor’s Financial Services LLC (“S&P”), Moody’s Investor Service (“Moody’s”) and Fitch Ratings (“Fitch”) downgraded the credit rating of Puerto Rico and its debt below investment grade to BB+, Ba2 and BB, respectively. The rating agencies confirmed these ratings in March 2014 following a bond sale described below. Due to the deteriorating financial condition of Puerto Rico, including the potential effects of the February 2014 ratings downgrades of Puerto Rico and its debt, we downgraded our remaining Puerto Rico Exposure in February 2014 such that all of our Puerto Rico Exposure is currently rated BIG.

Puerto Rico has taken a number of significant steps to improve its budgetary position and financial condition and, in March 2014, it successfully sold \$3.5 billion general obligation bonds to address short term liquidity needs through 2015, at yields, although high, that were below widely predicted yields. Puerto Rico, however, remains in a multi-year recession and continues to suffer from high debt levels, persistent structural budget deficits that require additional borrowing and an under-funded pension system.

We expect that it will take several years for Puerto Rico to erase current deficits and provide for sustainable structurally balanced budgets. Puerto Rico's fiscal issues have resulted in volatile pricing on its debt securities, which together with the recent downgrades of Puerto Rico's published ratings described above may constrain Puerto Rico's future access to capital markets at reasonable cost. The Puerto Rico Government Development Bank hired a restructuring specialist and other professionals, and legislation has been introduced to establish a legal framework in Puerto Rico for adjusting the debt of the Commonwealth's public authorities. These actions have heightened the perception and risk that Puerto Rico may seek to restructure its outstanding debt, notwithstanding the current opposition of Puerto Rico's governor. We can provide no assurances that Puerto Rico will not seek to restructure or impair any or all of our Puerto Rico Exposure.

Puerto Rico and its debt securities remain vulnerable to volatile pricing and negative developments, including further ratings downgrades. Despite these concerns, and the possibility of future negative net claim liability developments, we do not currently anticipate paying claims on any of our Puerto Rico Exposure.

As of March 31, 2014, we had an aggregate of \$172.9 million of Sovereign net par outstanding, \$100.8 million of which was rated at least investment grade, and \$72.1 million of which was rated BIG. All of our BIG exposure relates to the Stressed European Countries whose Sovereign obligations have been under particular stress due to economic uncertainty, potential debt restructuring and ratings downgrades. Due to volatile economic conditions and political uncertainty, particularly in the Stressed European Countries, we believe that our Sovereign insured credits in the Stressed European Countries remain vulnerable to further credit deterioration, potential ratings downgrades and increases in our net claim liability.

We expect the negative trend in the public finance sector to continue, primarily due to the slow economic recovery, federal funding reductions, expected Medicare cuts, rising employee wages, pension and healthcare costs and continued stress on tax-based revenue receipts (in particular where tax revenues are derived from the value of real estate). We expect these factors to continue to strain the ability of government entities to maintain balanced budgets and adequate liquidity to meet near-term financial obligations. We may experience further credit deterioration and municipal defaults in our government-related insured credits, which could require increases in our net claim liability with respect to these credits.

*Structured Finance.* Overall, the transactions in our financial guaranty structured finance portfolio have continued to experience stable credit performance during the first quarter of 2014. The credit performance of our \$6.9 billion corporate CDO portfolio continues to improve and we continue to have strong subordination remaining in our corporate CDO transactions. There were no credit events that reduced subordination levels in our corporate CDO transactions in the first quarter of 2014. Three of these corporate CDO transactions, with \$1.1 billion of net par outstanding, are scheduled to mature later this year and the remaining 13 transactions, with \$5.8 billion of net par outstanding, are scheduled to mature in 2017. All but \$0.8 billion of the corporate CDO transactions we insure were rated AAA as of March 31, 2014.

We continue to see stabilization and improved performance across many of the transactions in our \$957.0 million net par outstanding directly insured trust preferred securities ("TruPs") CDO portfolio. The banking sector continues to face increasing pressure from regulatory compliance costs, limited growth in loan portfolio and reduced earnings from a flattening yield curve. Smaller community banks, which comprise a significant portion of the issuers in our directly insured TruPs CDO portfolio, face these pressures acutely, due to additional pressure from their lack of economies of scale, limited revenue resources and often undiversified businesses. Notwithstanding these pressures, the collateral fundamentals of the bank issuers within these insured transactions continue to show improved performance. The number of cures of previous defaults and the repayment of interest payments previously deferred on the TruPs collateral has outpaced new initial defaults and interest payment deferrals by the TruPs issuers, (which deferrals are permissible for up to five years). The insurance company issuers in our TruPs CDO portfolio generally remain stable. Our weighted average rating for our directly insured TruPs bonds was BBB at March 31, 2014 and December 31, 2013. As of March 31, 2014, \$114.5 million of our net par outstanding related to one of the TruPs bonds we insure was rated BIG compared to \$224.7 million of net par outstanding related to two TruPs bonds that we insured being rated BIG as of December 31, 2013.

Our \$1.4 billion of insured CDO of CMBS transactions have experienced mixed performance so far in 2014. In January 2014, our counterparty to a \$450 million AAA-rated CDO of CMBS transaction exercised its right to terminate the transaction on a walkaway basis. During the first three months of 2014, the average total delinquencies in the collateral supporting each of our three remaining directly-insured CDOs of CMBS decreased. However, average loss severity across the CMBS backing these CDOs increased during the first three months of 2014, and interest shortfalls occurred in three of the 99 CMBS tranches that back the CDOs we insure as a result of: (1) reductions in the appraised value of properties, which allow servicers to stop making advances for interest; and (2) expenses related to the liquidation of certain properties. Our maximum total exposure to interest shortfalls on our CDO of CMBS transactions is limited to the estimated \$2.0 million (as of March 31, 2014) of contractual premium that is payable to us over the remaining life of the contracts. Although we project that future interest shortfalls will result in reductions in the amount of premiums we receive for a period of time, based on our internal cash flow projections, we also expect that such amounts will eventually be repaid to us.

One of the CMBS tranches backing one of our CDO of CMBS transactions began experiencing principal losses during the second quarter of 2013. Since then, additional principal losses on this CDO of CMBS were recorded such that the total principal loss has reduced the subordination for the transaction by approximately \$10.5 million of the initial \$97.5 million of subordination. The ratings for our CDO of CMBS transactions remained unchanged as of March 31, 2014, with one rated AAA, one rated AA- and one rated BBB-. We continue to expect not to have to pay net claims on our CDO of CMBS transactions.

In April 2014, our counterparty to one of our two CDO of collateralized loan obligation (“CLO”) transactions outstanding as of March 31, 2014 exercised its right to terminate the transaction on a walkaway basis. Our rating on our sole remaining CLO of middle market loans that we insure in a second-to-pay position through a CDS (the “CLO Transaction”) with \$387.3 million net par outstanding as of March 31, 2014, remains unchanged at B+. The rating for this transaction remains subject to the potential deteriorating credit quality of the primary insurer of the CLO Transaction, MBIA Insurance Corporation.

#### ***Quarter Ended March 31, 2014 Compared to Quarter Ended March 31, 2013***

The following table summarizes the results of operations for our financial guaranty segment for the periods indicated:

<b>(\$ in millions)</b>	<b>Three Months Ended March 31,</b>		<b>% Change</b>
	<b>2014</b>	<b>2013</b>	<b>2014 vs. 2013</b>
Adjusted pretax operating loss (1)	\$ (10.2)	\$ (3.8)	n/m
Net premiums written—insurance	0.8	(10.1)	n/m
Net premiums earned—insurance	6.9	9.6	(28.1)%
Net premiums earned on derivatives	3.4	5.0	(32.0)
Net investment income	10.2	11.8	(13.6)
Provision for losses	5.7	0.1	n/m
Policy acquisition costs	1.6	5.5	(70.9)
Other operating expenses	9.6	14.3	(32.9)
Interest expense	14.6	13.2	10.6

n/m – not meaningful

(1) Our senior management uses adjusted pretax operating income (loss) as our primary measure to facilitate evaluation of the fundamental financial performance of the Company’s business segments and to allocate resources to the segments.

*Adjusted Pretax Operating Loss.* The results for the three months ended March 31, 2014 reflect an increase in the financial guaranty segment’s adjusted pretax operating loss, primarily due to an increase in provision for losses, lower net premiums earned and investment income and increased interest expense, partially offset by reductions in policy acquisition costs and other operating expenses compared to the same period in 2013.

*Net Premiums Written and Earned.* Net premiums earned for the three months ended March 31, 2014 reflect a lower level of refundings on public finance exposures than in 2013. Net premiums written and earned for the three months ended March 31, 2013 reflect the impact of the commutation of the remaining \$822.2 million net par reinsured by Radian Asset Assurance from Financial Guaranty Insurance Company (the “FGIC Commutation”), which decreased premiums written and earned by \$12.6 million and \$2.5 million, respectively.



The following table shows net premiums earned by our financial guaranty segment's various product lines for the periods indicated:

<u>(In thousands)</u>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Net premiums earned:		
Public finance direct	\$ 4,543	\$ 7,200
Public finance reinsurance	1,679	1,447
Structured direct	226	200
Structured reinsurance	453	3,196
Trade credit reinsurance	2	—
Total premiums earned—insurance	6,903	12,043
Impact of commutations/recaptures	—	(2,447)
Total net premiums earned—insurance	\$ 6,903	\$ 9,596
Refundings included in total net premiums earned	\$ 2,117	\$ 4,753

*Net Investment Income.* Our financial guaranty net investment income decreased for the three months ended March 31, 2014, compared to the same period for 2013, primarily due to a decline in dividend income and lower yielding investment securities. Our current allocation to short-term and short duration investments remains high. This allocation, combined with certain sales of securities and subsequent reinvestment of longer duration securities in the low interest rate environment, has resulted in a lower yield profile for the portfolio. Both periods include an allocation to the financial guaranty segment of net investment income from Radian Group based on relative GAAP equity for this segment.

*Provision for Losses.* Our financial guaranty provision for losses for the three months ended March 31, 2014 reflects an increase compared to the same period for 2013, primarily as a result of the establishment of new reserves for several public finance credits and one structured finance credit.

The following tables show financial guaranty reserve for losses and claims paid as of or for the periods indicated:

<u>(In thousands)</u>	<b>March 31, 2014</b>	<b>December 31, 2013</b>	<b>March 31, 2013</b>
Total reserve for losses	\$ 29,752	\$ 21,069	\$ 24,573

<u>(In thousands)</u>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Total claims paid	\$ 3,033	\$ 41,858 <sup>(1)</sup>

(1) Reflects the payment of \$41.6 million related to the FGIC Commutation.

*Policy Acquisition Costs.* Policy acquisition costs for the three months ended March 31, 2013 reflect the write-off of \$3.3 million of acquisition costs as a result of the FGIC Commutation and lower commission income.

*Other Operating Expense.* Our other operating expenses for the three months ended March 31, 2014, compared to the same period in 2013, reflect a lower impact related to changes in the estimated fair value of cash-settled long-term incentive awards that are valued relative to Radian Group's common stock price. If our stock price increases during a quarter, additional expense is recognized for these awards. Our stock price increased from \$14.12 at December 31, 2013 to \$15.03 at March 31, 2014, while the stock price increased from \$6.11 at December 31, 2012 to \$10.71 at March 31, 2013.

*Interest Expense.* The results for the three months ended March 31, 2014 and 2013 reflect an allocation to the financial guaranty segment of the interest expense from Radian Group based on relative GAAP equity. The amount for the three months ended March 31, 2014 reflects an increase related to the issuance of \$400 million of convertible debt during the first quarter of 2013.

## Off-Balance Sheet Arrangements

As a provider of credit enhancement, we have provided credit protection directly on transaction structures that involve VIEs. VIEs are entities, including corporations, trusts or partnerships, in which equity investors do not have a controlling financial interest or do not have sufficient equity at risk to finance the VIE's activities without additional subordinated financial support. We evaluate all VIEs for potential consolidation in accordance with the accounting standard regarding consolidation of VIEs.

VIEs often are created in structured transactions having a specific risk profile desired by investors and as a means of transferring risk. Our primary involvement with VIEs relates to transactions in which we provide a financial guaranty to one or more classes of beneficial interest holders in the VIE. Our interests in VIEs either are accounted for as insurance contracts, financial guaranty derivatives or, in some cases, as consolidated VIEs. See Note 5 of Notes to Unaudited Condensed Consolidated Financial Statements for more information on consolidated VIEs. For insurance contracts with VIEs that we do not consolidate, we estimate reserves for losses and LAE, and for derivative interests in VIEs that we do not consolidate, we estimate changes in the fair value as a corresponding derivative asset or derivative liability. We do not record the underlying assets or liabilities of the VIEs on our balance sheets unless we consider that we are the primary beneficiary of the VIE.

## Contractual Obligations and Commitments

There have been no material changes outside the ordinary course of our business in the contractual obligations specified in our 2013 Form 10-K, except as follows:

On May 6, 2014, Radian Group entered into the Purchase Agreement to purchase all of the outstanding equity interests in Clayton for aggregate cash consideration of \$305 million. In connection with the acquisition, we plan to raise the aggregate cash consideration by seeking financing through the issuance of debt and equity. See "Recent Developments" herein and Note 17 of Notes to Unaudited Condensed Consolidated Financial Statements for additional information.

## Liquidity and Capital Resources

### *Radian Group—Short-Term Liquidity Needs*

Radian Group serves as the holding company for our insurance subsidiaries and does not have any significant operations of its own. At March 31, 2014, Radian Group had immediately available, either directly or through an unregulated subsidiary, unrestricted cash and liquid investments of approximately \$615 million. This amount excludes certain additional cash and liquid investments that have been advanced from our subsidiaries for corporate expenses and interest payments.

Radian Group's principal liquidity demands for the next 12 months are expected to include: (i) potential additional capital support for our mortgage insurance subsidiaries; (ii) the payment of dividends on our common stock; (iii) the payment of corporate expenses; and (iv) interest payments on our outstanding long-term debt. As of March 31, 2014, the holders of our Convertible Senior Notes due 2017 and of our Convertible Senior Notes due 2019 are able to exercise their conversion rights during the three month period ending June 30, 2014. As a result, an additional liquidity demand may occur in the event these holders elect to exercise their conversion rights during that period, because the conversion amounts for these notes may, at our option, be settled in cash (and in the case of the 2017 notes, a portion of the conversion amount must be settled in cash). On a quarterly basis, we will evaluate whether the conversion threshold requirement has been met. See Note 11 in our 2013 Form 10-K and Note 10 of Notes to Unaudited Condensed Consolidated Financial Statements for further information.

In addition, as discussed under "Recent Developments," on May 6, 2014, we announced an agreement to acquire Clayton for \$305 million. In connection with the acquisition, we plan to raise an aggregate amount to fund the purchase price and any related expenses of the transaction, which we anticipate seeking to finance through the issuance of debt and equity. Any additional proceeds received from such issuance will be used to fund the early redemption of our \$54.5 million Senior Notes due 2015, scheduled to mature on June 15, 2015, and for working capital. We can provide no assurance that we will be successful in raising these funds on favorable terms or at all, in which case, we may be required to fund the acquisition with available liquidity, which would reduce the amounts available for payment of our expenses and for capital contributions to Radian Guaranty.

In addition to existing available cash and marketable securities, Radian Group's principal sources of cash include dividends from Radian Guaranty (to the extent permitted under applicable laws and regulations) and payments made to Radian Group under tax- and expense-sharing arrangements with our subsidiaries, as discussed below. Radian Guaranty's ability to pay dividends to Radian Group is subject to various conditions imposed by the GSEs and by insurance regulations requiring insurance department approval. In general, dividends in excess of prescribed limits are deemed "extraordinary" and require insurance department approval. In light of the protracted period of losses for Radian Guaranty following the financial crises, we do not anticipate that Radian Guaranty will be permitted under applicable insurance laws to issue dividends to Radian Group for the foreseeable future. To the extent Radian Asset Assurance is permitted to pay future dividends, these dividends will be paid to its direct parent, Radian Guaranty, and not to Radian Group.

Except for the acquisition discussed above, we expect to fund Radian Group's short-term liquidity needs with: (i) existing cash and marketable securities and (ii) cash received under the expense-sharing arrangements with our subsidiaries, as further discussed below. If Radian Group's current sources of liquidity are insufficient for Radian Group to fund its obligations, or if we otherwise decide to increase our liquidity position, Radian Group may seek additional capital by incurring additional debt, by issuing additional equity, or by selling assets, which we may not be able to do on favorable terms, if at all.

At March 31, 2014, we did not have the intent to sell any debt securities classified as held to maturity or available for sale and in an unrealized loss position. We determined that it is more likely than not that we will have the ability to hold the securities until recovery of their cost basis or maturity.

*Corporate Expenses and Interest Expense.* Radian Group has expense-sharing arrangements in place with its principal operating subsidiaries that require those subsidiaries to pay their allocated share of certain holding-company-level expenses, including interest payments on all of our outstanding long-term debt other than the interest on our Convertible Senior Notes due 2019. Payments of such corporate expenses for the next 12 months, excluding interest payments on our long-term debt, are expected to be approximately \$ 57.5 million. For the same period, payments of interest on our long-term debt are expected to be approximately \$43.0 million. Substantially all of these amounts are reimbursed by our subsidiaries under our existing expense-sharing arrangements. These arrangements, as amended, have been approved by applicable state insurance departments, but such approval may be modified or revoked at any time.

*Capital Support for Subsidiaries.* Radian Guaranty's risk-to-capital ratio was 19.2 to 1 as of March 31, 2014. Currently, we expect to maintain Radian Guaranty's risk-to-capital ratio at or below 20 to 1. We estimate that an immaterial amount of additional capital contributions from Radian Group to Radian Guaranty would be required during the next 12 months in order to maintain Radian Guaranty's risk-to-capital ratio at or below 20 to 1.

We expect the GSEs to release revisions to their standard mortgage insurer eligibility requirements in draft form for public comment as early as the second quarter of 2014. Among other changes, the new GSE eligibility requirements are expected to contain new capital adequacy standards for private mortgage insurers that are more onerous than the capital requirements that are currently in effect, including potentially: (i) a risk-to-capital ratio below Radian Guaranty's 19.2 to 1 risk-to-capital ratio as of March 31, 2014; (ii) capital requirements based on a variety of risk characteristics and measures of credit quality; and (iii) a limitation on the amount of capital credit available for subsidiary capital (including Radian Guaranty's capital that is attributable to its ownership of Radian Asset Assurance). The form of the new eligibility requirements and the timeframe for their implementation remain uncertain. If the new GSE eligibility requirements include more onerous capital requirements, including any one or more of the potential requirements referenced above, we may need to provide additional capital support to, or arrange additional capital relief for, Radian Guaranty, including potentially, entering into new reinsurance arrangements, increasing the amount of capital contributions from Radian Group's available holding company funds or seeking to raise funds in private or public capital transactions. For example, if Radian Guaranty is required to maintain a maximum risk-to-capital ratio of 18 to 1, absent any other form of risk-to-capital support, we estimate that we would be required to contribute approximately \$200 million to Radian Guaranty during the next 12 months, assuming for purposes of this example that there is no implementation period for these requirements. Although we can provide no assurances, we expect that the new eligibility requirements will include an implementation period. Because we expect that Radian Guaranty will generate capital internally in the future, the length of the implementation period could reduce that amount of additional capital support, if any, that we may need to provide to Radian Guaranty.

Radian Group also could be required to provide capital support for Radian Guaranty and our other mortgage insurance subsidiaries if additional capital is required pursuant to insurance laws and regulations. The National Association of Insurance Commissioners (“NAIC”) is in the process of reviewing the minimum capital and surplus requirements for mortgage insurers and considering changes to the Mortgage Guaranty Insurers Model Act (“Model Act”) that could include more stringent capital requirements for Radian Guaranty, which, if adopted, could increase the capital requirements for Radian Guaranty in states that adopt the new Model Act. In addition, certain of our mortgage insurance subsidiaries that provide reinsurance to Radian Guaranty currently have required, and in the future may again require, additional capital contributions from Radian Group, although these amounts are not expected to be material.

*Dividends.* Our quarterly common stock dividend is currently \$0.0025 per share and, based on our current outstanding shares of common stock, we would require approximately \$1.7 million in the aggregate to pay our quarterly dividends for the next 12 months. Radian Group is not subject to any limitations on its ability to pay dividends except those generally applicable to corporations, such as Radian Group, that are incorporated in Delaware. Delaware corporation law provides that dividends are only payable out of a corporation’s capital surplus or (subject to certain limitations) recent net profits. As of March 31, 2014, our capital surplus was \$1.1 billion, representing our dividend limitation under Delaware law.

*Tax Payments.* Under our current tax-sharing agreement between Radian Group and its subsidiaries, our subsidiaries are required to pay to Radian Group, on a quarterly basis, amounts representing their estimated separate company federal tax liability for the current tax year. Radian Group is required to refund to each subsidiary any amount that such subsidiary overpaid to Radian Group for a taxable year, as well as any amount that the subsidiary could utilize through existing carryback provisions of the Internal Revenue Code had such subsidiary filed its federal tax return on a separate company basis. Any payments that Radian Group is expected to make during the next 12 months under the tax-sharing agreement are not expected to have a material impact on Radian Group’s available liquidity. Our tax-sharing agreement may not be changed without the pre-approval of the applicable state insurance departments for certain of the insurance subsidiaries that are parties to the agreement.

### ***Radian Group—Long-Term Liquidity Needs***

Our most significant needs for liquidity beyond the next 12 months are: (i) the repayment of our outstanding long-term debt, including \$54.5 million principal amount of outstanding debt due in June 2015, \$195.5 million principal amount of outstanding debt due in June 2017, \$450 million principal amount of convertible debt due in November 2017 and, at our option, any related conversion premium that we elect to settle in cash, and potentially \$400 million of convertible debt due in March 2019 for which the principal amount and any conversion premium may, at our option, be settled in cash; (ii) potential additional capital contributions to our mortgage insurance subsidiaries; and (iii) potential payments to the U.S. Department of the Treasury (“U.S. Treasury”) resulting from the examination of our 2000 through 2007 consolidated federal income tax returns by the Internal Revenue Service (“IRS”).

As of the balance sheet date, certain of our insurance subsidiaries, including Radian Guaranty, have incurred net operating losses (“NOLs”) that could not be carried-back and utilized on a separate company tax return basis. As a result, we are not currently obligated under our tax-sharing agreement to reimburse these subsidiaries for their separate company NOL carryforward. However, if in a future period our consolidated NOL is fully utilized before a subsidiary has utilized its share of NOLs on a separate entity basis, then Radian Group may be obligated to fund such subsidiary’s share of our consolidated tax liability to the IRS. Currently, we do not expect to fund material obligations under the provisions described in this paragraph with regard to subsidiary NOLs incurred to date.

We are currently contesting proposed adjustments resulting from the IRS examination of the 2000 through 2007 tax years, which if sustained, will result in additional income taxes of approximately \$128 million plus proposed penalties of approximately \$42 million. Additionally, we would incur interest on any sustained adjustments. Radian Group and Radian Guaranty Reinsurance Inc. (“RGRI”) are parties to an Assumption and Indemnification Agreement with regard to these proposed adjustments. Through this agreement, Radian Group agreed to indemnify RGRI for the amount of any tax payments ultimately due to the IRS for the proposed adjustments, which relate to the recognition of certain tax losses and deductions that were generated through our investment in a portfolio of non-economic Real Estate Mortgage Investment Conduit residual interests currently held by RGRI. This indemnification agreement was made in lieu of an immediate capital contribution to RGRI that otherwise would have been required for RGRI to maintain its minimum statutory surplus requirements in light of remeasurement as of December 31, 2011 of uncertain tax positions related to the portfolio of REMIC residual interests. See Note 12 of Notes to Unaudited Condensed Consolidated Financial Statements for additional information regarding the IRS matter. We can provide no assurance regarding the outcome of this IRS matter, which may take several years to resolve. As such, there remains significant uncertainty with regard to the amount and timing of any potential payments under the indemnity agreement described above.

We expect to meet the long-term liquidity needs of Radian Group with a combination of: (i) available cash and marketable securities; (ii) private or public issuances of debt or equity securities, which we may not be able to do on favorable terms, if at all; (iii) cash received under expense-sharing arrangements with our subsidiaries; and (iv) dividends from our subsidiaries, to the extent available.

We regularly evaluate opportunities, based on market conditions, to finance our operations by accessing the capital markets or other types of indebtedness with institutional lenders, and consider various measures to improve our capital and liquidity position, as well as our debt maturity profile. In the past, we have repurchased and exchanged, prior to maturity, some of our outstanding debt, and in the future, we may, from time to time, seek to redeem, repurchase or exchange for other securities, prior to maturity, some or all of our outstanding debt in the open market, through private transactions, pursuant to one or more tender offers, or through any combination of the foregoing, as circumstances may allow. The timing or amount of any potential transactions, which may or may not occur, will depend on a number of factors, including market opportunities and our capital and liquidity needs. We may seek to refinance all or a portion of our long-term debt, but we may not be able to do on favorable terms, if at all.

### ***Mortgage Insurance***

As of March 31, 2014, our mortgage insurance segment maintained claims paying resources of \$2.7 billion, which consists of contingency reserves, statutory policyholders' surplus, unearned premium reserves and loss reserves.

The principal demands for liquidity in our mortgage insurance business include the payment of claims and potential claim settlement transactions, operating expenses (including those allocated from Radian Group) and taxes. The principal sources of liquidity in our mortgage insurance business currently are insurance premiums, net investment income, capital contributions from Radian Group, and dividends from Radian Asset Assurance. Our mortgage insurance business has incurred significant losses over the past six years due to the housing and related credit market downturns. We believe that the operating cash flows generated by each of our mortgage insurance subsidiaries will provide these subsidiaries with a substantial portion of the funds necessary to satisfy their claim payments and operating expenses for the foreseeable future. We believe that we have the ability to fund any operating cash flow shortfall from sales and maturities of marketable securities in our investment portfolio maintained at our operating companies. In the event that we are unable to fund excess claim payments and operating expenses through the sale of these marketable securities and from maturing fixed-income investments, we may be required to incur unanticipated capital losses or delays in connection with the sale of less liquid marketable securities held by our operating companies.

The amount, if any, and timing of Radian Asset Assurance's dividend paying capacity will depend, in part, on the performance of our insured financial guaranty portfolio, including the establishment of, or change in, statutory reserves, as well as the amount we may pay to commute transactions. If the exposure in our financial guaranty business is reduced on an accelerated basis through the recapture or settlement of business from the primary customers in our financial guaranty reinsurance business or otherwise, we may have the ability to pay dividends to our mortgage insurance business more quickly and in a greater amount. However, if the performance of our financial guaranty portfolio deteriorates materially, Radian Asset Assurance may have limited or no capacity to pay dividends to Radian Guaranty. In the event of a default giving rise to a claim payment obligation in our financial guaranty business, the statutory policyholders' surplus of Radian Asset Assurance (and consequently Radian Guaranty) would be reduced in an amount equal to the present value of our expected future net claim liability (net of taxes) for such transactions. Any significant reduction in statutory policyholders' surplus could also reduce Radian Asset Assurance's capacity to pay dividends to Radian Guaranty and Radian Asset Assurance could be restricted from paying dividends altogether without prior approval from the New York State Department of Financial Services. See Capital and Liquidity in Note 1 of Notes to Unaudited Condensed Consolidated Financial Statements for information regarding Radian Asset Assurance's recent request to the NYSDFS to pay an extraordinary dividend to Radian Guaranty.

### ***Freddie Mac Agreement***

In connection with the closing under the Freddie Mac Agreement, Radian Guaranty deposited \$205 million of investment securities into a collateral account, which remains on our condensed consolidated balance sheets as a result of the rights that Radian Guaranty has with respect to those funds. Subject to certain conditions in the Freddie Mac Agreement, amounts in the collateral account may be released to Radian Guaranty from Freddie Mac over time to the extent that loss mitigation activity becomes final in accordance with the terms of the Freddie Mac Agreement.

### ***Financial Guaranty***

As of March 31, 2014, Radian Asset Assurance maintained claims paying resources of \$1.6 billion, which included statutory policyholders' surplus, contingency reserves, unearned premium reserves, the present value of installment premiums and loss and LAE reserves. As of March 31, 2014, the statutory policyholders' surplus of Radian Asset Assurance was approximately \$1.2 billion. In July 2013, Radian Asset Assurance paid an ordinary dividend of \$36 million to Radian Guaranty. We estimate that Radian Asset Assurance will have the capacity to pay another ordinary dividend of approximately \$32 million to Radian Guaranty in the third quarter of 2014. See Capital and Liquidity in Note 1 of Notes to Unaudited Condensed Consolidated Financial Statements for information regarding Radian Asset Assurance's recent request to the NYSDFS to pay an extraordinary dividend to Radian Guaranty.

The principal demands for liquidity in our financial guaranty business include the payment of operating expenses (including those allocated from Radian Group), claim and commutation payments, taxes and dividends to Radian Guaranty.

Radian Asset Assurance could be required under certain circumstances to pay its CDS counterparty the outstanding par amount with respect to four insured TruPs bonds (a "liquidity claim"). A liquidity claim may arise if an event of default under the TruPs bond (e.g., a failure to pay interest or a breach of a covenant requiring the maintenance of a certain level of performing collateral) existed as of the termination date of the CDS contract. The current termination dates of these CDS contracts occur in 2018 or 2019, but will automatically extend for additional one-year periods (but no later than the maturity date of the TruPs CDOs) unless the counterparty elects not to extend the termination date. If Radian Asset Assurance were required to pay a liquidity claim, the counterparty would be obligated under the CDS to pay Radian Asset Assurance cash periodically in an amount equal to any future amounts paid in respect of principal and interest on the insured TruPs bond. We do not currently expect a liquidity claim to occur. At March 31, 2014, the net par outstanding of the insured TruPs bonds that are potentially subject to a liquidity claim was \$322.9 million and had a weighted average rating of BBB-.

In addition, Radian Asset Assurance continues to have similar liquidity claim exposure in relation to four additional TruPs CDO transactions pursuant to Radian Asset Assurance's rights in a limited purpose vehicle ("LPV") created in connection with the termination of several transactions in 2012. CDS transactions entered into by the LPV related to these TruPs CDOs include provisions that provide the LPV's counterparty with substantially the same economic rights upon the occurrence of circumstances where a liquidity claim would have been payable by Radian Asset Assurance under certain terminated transactions. Although Radian Asset Assurance does not have the obligation to pay a liquidity claim on these TruPs CDOs, if one of these circumstances were to occur or would be expected to occur, Radian Asset Assurance's future projected and actual salvage recovery from the LPV, which was approximately \$78.6 million as of March 31, 2014, may be materially reduced or eliminated.

The principal sources of liquidity in our financial guaranty business are premium collections, credit enhancement fees on credit derivative contracts and net investment income. We believe that the cash flows generated by our financial guaranty subsidiaries will provide these subsidiaries with the funds necessary to satisfy their claim payments and operating expenses for the foreseeable future. We believe that we have the ability to fund any operating cash flow shortfall from sales of marketable securities in our investment portfolio maintained at our operating companies and from maturing fixed-income investments. In the event that we are unable to fund excess claim payments and operating expenses through the sale of these marketable securities and from maturing fixed-income investments, we may be required to incur unanticipated capital losses or delays in connection with the sale of less liquid marketable securities held by our operating companies.

### Reconciliation of Consolidated Net Income (Loss) to Cash Used in Operations

The following table reconciles consolidated net income (loss) to cash flows used in operations for the periods indicated:

<u>(In thousands)</u>	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Net income (loss)	\$ 202,759	\$ (187,500)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Net (gains) losses on investments and other financial instruments, change in fair value of derivatives and net impairment losses recognized in earnings	(115,235)	178,850
Net receipts (payments) related to derivative contracts and VIE debt (1)	2,775	(4,821)
Equity in loss (earnings) of affiliates	13	(1)
Net cash received (paid) for commutations, terminations, and recaptures (1)	1,105	(52,400)
Commutation-related charges	—	5,300
Deferred tax benefit	(533)	(24,266)
Depreciation and amortization, net	15,461	18,893
Change in:		
Unearned premiums	5,917	35,267
Deferred policy acquisition costs	3,218	10,301
Reinsurance recoverables	15,242	10,434
Reserve for losses and LAE	(262,295)	(189,263)
Other assets	2,840	(3,543)
Other liabilities	(8,277)	36,778
Cash flows used in operations	<u>\$ (137,010)</u>	<u>\$ (165,971)</u>

(1) Cash item.

Cash flows used in operating activities decreased for 2014 compared to 2013, primarily as a result of a decrease in payments for commutations, terminations and recaptures in 2014.

### Stockholders' Equity

Stockholders' equity was \$1.1 billion at March 31, 2014, compared to \$0.9 billion at December 31, 2013. The increase in stockholders' equity resulted primarily from our net income of \$202.8 million for 2014 partially offset by the reclassification to temporary equity of currently redeemable convertible senior notes previously included in equity. See Note 10 of Notes to Unaudited Condensed Consolidated Financial Statements for additional information.

### Ratings

Radian Group and our principal operating subsidiaries have been assigned the ratings set forth in the chart below. We believe that ratings often are considered by others in assessing our credit strength and the financial strength of our insurance subsidiaries and, in the past have been a significant factor in determining Radian Guaranty's eligibility with the GSEs.

	<b>Moody's (1)</b>	<b>S&amp;P (2)</b>
Radian Group	Caa1	B-
Radian Guaranty	Ba3	BB-
Radian Insurance Inc.	(3)	(3)
Radian Mortgage Assurance Inc. ("RMAI") (4)	Ba3	BB-
Radian Asset Assurance	Ba1	B+

(1) Moody's outlook for Radian Group and all our rated mortgage insurance subsidiaries is currently Positive. Moody's outlook for Radian Asset Assurance is currently Negative.

(2) S&P's outlook for Radian Group and Radian Guaranty is currently Positive. The outlook for all other subsidiaries is currently Stable.

(3) Not currently rated.

(4) Currently, RMAI is not writing new business and has no RIF.

### *Recent Ratings Actions*

On February 27, 2014, S&P upgraded Radian Guaranty's credit rating from B to BB- and improved its outlook for Radian Guaranty and Radian Group to "Positive," reflecting S&P's expectations, including the following: (1) our operating performance will continue to improve; (2) the risk of adverse reserve development is reduced; and that (3) positive statutory earnings will incrementally improve the quality of capital at Radian Guaranty.

### **Critical Accounting Policies**

U.S. Securities and Exchange Commission ("SEC") guidance defines Critical Accounting Policies as those that require the application of management's most difficult, subjective or complex judgments, often because of the need to make estimates about the effect of matters that are inherently uncertain and that may change in subsequent periods. In preparing our consolidated financial statements in accordance with GAAP, management has made estimates, assumptions and judgments that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. In preparing these financial statements, management has utilized available information, including our past history, industry standards and the current and projected economic and housing environment, among other factors, in forming its estimates, assumptions and judgments, giving due consideration to materiality. Because the use of estimates is inherent in GAAP, actual results could differ from those estimates. In addition, other companies may utilize different estimates, which may impact comparability of our results of operations to those of companies in similar businesses. A summary of the accounting policies that management believes are critical to the preparation of our consolidated financial statements is set forth below.

### ***Reserve for Losses and LAE***

We establish reserves to provide for losses and LAE and the estimated costs of settling claims in both our mortgage insurance and financial guaranty segments in accordance with the accounting standard regarding accounting and reporting by insurance enterprises. Although this standard specifically excludes mortgage insurance from its guidance relating to the reserve for losses, we establish reserves for mortgage insurance as described below, using the guidance contained in this standard supplemented with other accounting guidance, due to the lack of specific guidance for mortgage insurance.

Estimating the loss reserves in both our mortgage insurance and financial guaranty business segments involves significant reliance upon assumptions and estimates with regard to the likelihood, magnitude and timing of each potential loss. The models, assumptions and estimates we use to establish loss reserves may prove to be inaccurate, especially during an extended economic downturn or a period of extreme market volatility and uncertainty. As such, we cannot be certain that our reserve estimate will be adequate to cover ultimate losses on incurred defaults.

Commutations, recaptures and other negotiated terminations of our insured risks in both our mortgage insurance and financial guaranty segments provide us with an opportunity to exit exposures for an agreed upon payment, or payments, sometimes at an amount less than the previously estimated ultimate liability. Once all exposures relating to such policies are extinguished, all reserves for losses and LAE and other balances relating to the insured or reinsured policy generally are eliminated. Upon completion of a commutation, recapture or other negotiated termination, all such related balances, including deferred policy acquisition costs and unearned premiums, are generally reversed, with any remaining net gain or loss typically recorded through provision for losses. We take into consideration the specific contractual and economic terms for each individual agreement when accounting for our commutations, recaptures or other negotiated terminations, which may result in differences in the accounting for these transactions.



### *Mortgage Insurance*

In the mortgage insurance segment, the default and claim cycle begins with the receipt of a default notice from the servicer. Reserves for losses are established upon receipt of notification by servicers that a borrower has missed two monthly payments, which is when we consider a loan to be in default for financial statement and internal tracking purposes. We also establish reserves for associated LAE, consisting of the estimated cost of the claims administration process, including legal and other fees and expenses associated with administering the claims process. We maintain an extensive database of claim payment history and use models based on a variety of loan characteristics, including the status of the loan as reported by its servicer and the type of loan product, to determine the likelihood that a default will reach claim status. Our process includes forecasting the impact of our loss mitigation efforts in protecting us against fraud, underwriting negligence, breach of representation and warranties, inadequate documentation of submitted claims and other items that may give rise to insurance rescissions or cancellations and claim denials, to help determine the rate at which defaulted loans are expected to move to claim (“default to claim rate”). Lastly, we project the amount that we will pay if a default becomes a claim (referred to as “claim severity”), which is also impacted by loss mitigation activity associated with claim curtailments due to servicer noncompliance with our insurance policies and servicing guidelines. When there is a claim under primary mortgage insurance, the coverage percentage is applied to the claim amount, which consists of the unpaid loan principal, plus past due interest (for which our liability is contractually capped at a maximum of two years) and certain expenses associated with the default, to determine our maximum liability. Based on these estimates, we arrive at our estimate of loss reserves as of that time.

With respect to loans that are in default, considerable judgment is exercised as to the adequacy of reserve levels. Loss reserves are increased as defaulted loans age, up to a maximum of 240 days in default because historically, as defaulted loans age, they have been more likely to result in foreclosure, and therefore, have been more likely to result in a claim payment. In the past, as the default proceeded towards foreclosure, there was generally more certainty regarding these estimates. However, in the current environment in which many foreclosures have been delayed or not yet pursued, significant uncertainty remains with respect to the ultimate resolution of aged defaults. This uncertainty requires management to use considerable judgment in estimating the rate at which these loans will result in claims. If a default cures, the reserve for that loan is removed from the reserve for losses and LAE. Once a claim is submitted, reserves are further increased to reflect the fact that the default has moved closer to resulting in a claim payment.

We also establish reserves for defaults that we estimate have been incurred but have not been reported to us on a timely basis by the servicer, as well as for previously rescinded policies and denied claims that we estimate will be reinstated and subsequently paid. We generally give the insured up to 90 days to challenge our decision to rescind coverage before we consider a policy to be rescinded and remove it from our defaulted inventory; therefore, we currently expect only a limited percentage of policies that were rescinded to be reinstated. We currently expect a significant percentage of claims that were denied to be resubmitted as a perfected claim and ultimately paid. Most often, a claim denial is the result of a servicer’s inability to provide the loan origination file or other servicing documents for review. Under the terms of our master insurance policy with our lending customers, our insureds have up to one year after the acquisition of borrower’s title to provide to us the necessary documents to perfect a claim. All estimates are periodically reviewed and adjustments are made as they become necessary.

We do not establish reserves for loans that are in default if we believe that we will not be liable for the payment of a claim with respect to that default. For example, for those defaults in which we are in a “second loss position” (i.e., we are not required to make a payment until a certain aggregate amount of losses have already been recognized on a given set of loans), we initially calculate the reserve for defaulted loans in the transaction as if there were no deductible. If the existing deductible for a given structured transaction is greater than the aggregate reserve amount for the defaults contained within the transaction, we do not establish a reserve for the defaults, or if appropriate, we record a partial reserve. We do not establish loss reserves for expected future claims on insured mortgages that are not in default. See “—Reserve for Premium Deficiency” below for an exception to this general principle.

For purposes of reserve modeling, loans are aggregated into groups using a variety of factors. The attributes used to define the groups include, but are not limited to, the default status of the loans (i.e., number of days in default), product type (i.e., Prime, Alt-A or Subprime), type of insurance (i.e., primary or pool), policy origination year, loss position (i.e., with or without a deductible) and the state where the property is located (segregated into three state groups in order to adjust for differences in foreclosure timing). We use an actuarial projection methodology referred to as a “roll rate” analysis that uses historical claim frequency information to determine the projected ultimate default to claim rates for each product and default status. The default to claim rate also includes our estimates with respect to expected insurance rescissions and claim denials, which have the effect of reducing our default to claim rates. Since 2009, we have experienced an elevated level of insurance rescissions and claim denials for various reasons, including, without limitation, underwriting negligence, fraudulent applications and appraisals, breach of representations and warranties and inadequate documentation, primarily related to our legacy portfolio. We expect our rescission and denial rates to remain at elevated levels as long as defaults related to our legacy portfolio represent a significant percentage of our total default portfolio. After estimating the default to claim rate, we estimate the severity of each product type, type of insurance and state grouping based on the average of recently observed severity rates. These average severity estimates are then applied to individual loan coverage amounts to determine reserves. Senior management regularly reviews the modeled frequency, rescission, denial and severity estimates, which are based on historical trends as described. If recent emerging or projected trends differ significantly from the historical trends used to develop the modeled estimates, management evaluates these trends in determining how they should be considered in its reserve estimates.

Our aggregate weighted average default to claim rate assumption (net of denials and rescissions) used in estimating our reserve for losses was 46% at March 31, 2014, compared to 47% at December 31, 2013. We develop our default to claim rate estimates on defaulted loans based on the age of the underlying defaulted loans, as measured by the number of monthly payments missed. As of March 31, 2014, our aggregate weighted average default to claim rate estimate on our total first-lien portfolio, net of estimated future denials and rescissions and excluding pending claims, was 39% and ranged from 19% for insured loans that had missed two to three monthly payments to 48% for such loans that had missed 12 or more monthly payments. Our estimate of expected insurance rescissions and claim denials (net of expected reinstatements) embedded in our default to claim rate is generally based on our experience over the past year, with consideration given for differences in characteristics between those rescinded policies and denied claims and the loans remaining in our defaulted inventory.

In addition, as part of our claims review process, we assess whether defaulted loans were serviced appropriately in accordance with our insurance policies and servicing guidelines. To the extent a servicer has failed to satisfy its servicing obligations, our policies provide that we may curtail the claim payment for such default, and in some circumstances, cancel coverage or deny the claim. Since 2011, claim curtailments have increased both in frequency and in size, which has contributed to a reduction in the severity of our claim payments during this period. While we cannot give assurance regarding the extent or level at which such claim curtailments will continue, we expect this trend to continue in light of well publicized issues in the servicing industry and our existing legacy portfolio of aged defaults.

The elevated levels of our loss mitigation actions (the rate of rescissions and denials since 2009 and claim curtailments more recently) have led to an increased risk of litigation. Under our master insurance policy, any suit or action arising from any right of the insured under the policy must be commenced within two years after such right first arose and within three years for certain other policies, including certain pool insurance policies. Recently, we have faced an increasing number of challenges from certain lender customers regarding our loss mitigation actions, which have resulted in some reversals of our decisions regarding rescissions, denials and curtailments. Although we believe that our loss mitigation actions are justified under our policies, if we are not successful in defending these actions in any potential legal or other actions, including negotiated settlements, we may need to reassume the risk on, and increase loss reserves for, those policies or pay additional claims. The assumptions embedded in our estimated default to claim rate on our in-force default inventory include an adjustment to our estimated rescission and denial rate to account for the fact that we expect a certain number of policies to be reinstated and ultimately to be paid, as a result of valid challenges by such policy holders. As discussed above, we also establish reserves for IBNR defaults related to previously rescinded policies and denied or curtailed claims, which we believe are likely to be reinstated (in the case of previously rescinded policies) or resubmitted and paid (in the case of previously denied claims).

Generally, we estimate our claim liability related to the potential future reinstatement of previously denied claims and rescinded policies by estimating an initial gross reinstatement rate at the time of denial or rescission, which then declines over a 12- or 24-month time frame as certain denials and rescissions are reinstated. As of March 31, 2014, for previously denied claims, this initial gross reinstatement assumption begins at approximately 60% and declines to 0% after 12 months, while for previously rescinded policies, the initial assumed reinstatement rate begins at approximately 20% and declines to 0% after 24 months. Our IBNR reserve estimate also includes the projected potential impact from future estimated rescissions on reinstated denials. At any particular point in time, our IBNR reserve estimate with respect to previously rescinded policies or denied claims is affected not only by our initial reinstatement assumption, but also by the length of time since the denial or rescission, our estimated likelihood of such reinstatements resulting in a paid claim, the expected claim curtailments on such paid claims, as well as the potential outcome of any discussions with our lender and servicer customers regarding such rescissions or denials.

Until a liability associated with such activities or discussions becomes probable and can be reasonably estimated, we consider our claim payments or our rescissions, denials and curtailments to be resolved for financial reporting purposes. Under the accounting standard regarding contingencies, an estimated loss is accrued only if we determine that the loss is probable and can be reasonably estimated. For populations of disputed rescissions, denials and curtailments where we determine that a settlement is probable and that a loss can be reasonably estimated, we reflect our best estimate of the expected loss related to the populations under discussion in our financial statements, primarily as a component of our IBNR reserve. While our reserves include our best estimate of such losses, the outcome of the discussions or potential legal proceedings that could ensue is uncertain, and it is reasonably possible that a loss exists in excess of the amount accrued.

Included in our loss reserves is an estimate related to a potential additional payment to Freddie Mac under the Freddie Mac Agreement, which is dependent upon the loss mitigation activity on the population of loans subject to that agreement. Our reserve related to this potential additional payment is based on the estimated rescissions, denials, curtailments, and cancellations for this population of loans, determined using assumptions that are consistent with those utilized to determine our overall loss reserves.

We considered the sensitivity of first-lien loss reserve estimates at March 31, 2014 by assessing the potential changes resulting from a parallel shift in severity and default to claim rate. For example, assuming all other factors remain constant, for every one percentage point change in primary claim severity (which we estimate to be 28% of unpaid principal balance at March 31, 2014), we estimated that our loss reserves would change by approximately \$49 million at March 31, 2014. For every one percentage point change in pool claim severity (which we estimate to be 44% of unpaid principal balance at March 31, 2014), we estimated that our loss reserves would change by approximately \$2 million at March 31, 2014. For every one percentage point change in our overall net default to claim rate (which we estimate to be approximately 46% at March 31, 2014), we estimated an approximately \$32 million change in our loss reserves at March 31, 2014.

#### *Financial Guaranty*

In our financial guaranty segment, we recognize a net claim liability on our non-derivative transactions prior to an event of default (insured event) when there is evidence that credit deterioration has occurred for a particular policy and that the present value of the expected claim loss exceeds the unearned premium revenue. The expected claim loss is based on the probability-weighted present value of expected net cash outflows to be paid under, or in connection with, the policy. In measuring the net claim liability, we develop the present value of expected net cash outflows by using our own assumptions about the likelihood of various possible outcomes, including potential settlements or commutations, based on information currently available. We determine the existence of credit deterioration on directly insured policies based on periodic reporting from the insured party, indenture trustee or servicer and based on our surveillance efforts. These expected cash outflows are discounted using a risk-free rate. Our assumptions about the likelihood of outcomes, expected cash outflows and the appropriate risk-free rate are updated each reporting period. For assumed policies, we primarily use information provided by the ceding company, but also consider our specific knowledge of the credit for determining expected loss.

The risk management function in our financial guaranty business is responsible for the identification, analysis, measurement and surveillance of credit, market, legal and operational risk associated with our financial guaranty insurance contracts. Risk management is also primarily responsible for claims prevention and loss mitigation strategies. This discipline is applied during the ongoing monitoring and surveillance of each exposure in the portfolio.

There are both performing and under-performing credits in our financial guaranty portfolio. Performing credits generally have investment grade internal ratings, denoting nominal to moderate credit risk. However, net claim liabilities may be established for performing credits if the expected losses on the credits exceed the unearned premium revenues for the contracts based on the present value of the expected net cash outflows. If our risk management department concludes that a directly insured transaction should no longer be considered performing, it is placed in one of three designated watch list categories for deteriorating credits: Special Mention, Intensified Surveillance or Case Reserve. Assumed exposures in financial guaranty's reinsurance portfolio are generally placed in one of these categories if the ceding company for such transaction downgrades it to an equivalent watch list classification. However, should our financial guaranty risk management group disagree with the risk rating assigned by the ceding company, we may assign our own risk rating rather than use the risk rating assigned by the ceding company.

### ***Reserve for Premium Deficiency***

Insurance enterprises are required to establish a PDR if the net present value of the expected future losses and expenses for a particular product line exceeds the net present value of expected future premiums and existing reserves for that product line. We reassess our expectations for premiums, losses and expenses for our financial guaranty and mortgage insurance businesses at least quarterly and update our premium deficiency analysis accordingly. Expected future expenses include consideration of maintenance costs associated with maintaining records relating to insurance contracts and with the processing of premium collections. We also consider investment income in the premium deficiency calculation through the use of our pre-tax investment yield to discount certain cash flows for this analysis.

For our mortgage insurance business, we group our mortgage insurance products into two categories: first-lien and second-lien. To assess the need for a PDR on our first-lien insurance portfolio, we develop loss projections based on modeled loan defaults related to our current RIF. This projection is based on recent trends in default experience, severity and rates of defaulted loans moving to claim (such default to claim rates are net of our estimates of rescissions and denials), as well as recent trends in the rate at which loans are prepaid. As of March 31, 2014, our modeled loan default projections for our first-lien insured portfolio assume that the rate at which current loans will default has improved and will gradually return to normal historical levels over the next two years.

For our first-lien insurance business, because the combination of the net present value of expected premiums and previously established reserves (net of reinsurance recoverables) exceeds the net present value of expected losses and expenses, a first-lien PDR was not required as of March 31, 2014 or December 31, 2013. Assuming all other factors remained constant, if our assumed paid claim rate increased from approximately 7.0% to approximately 12.2%, we would be required to establish a PDR.

For our second-lien insurance business, we project future premiums and losses for this business using historical results to help determine future performance for both prepayments and claims. An estimated expense factor is then applied, and the result is discounted using a rate of return that approximates our pre-tax investment yield. This net present value, less any existing reserves, is recorded as a premium deficiency and the reserve is updated at least quarterly based on actual results for that quarter, along with updated transaction level projections.

Evaluating the expected profitability of our existing mortgage insurance business and the need for a PDR for our first-lien business involves significant reliance upon assumptions and estimates with regard to the likelihood, magnitude and timing of potential losses and premium revenues. The models, assumptions and estimates we use to evaluate the need for a PDR may prove to be inaccurate, especially during an extended economic downturn or a period of extreme market volatility and uncertainty such as currently exists. We cannot be certain that we have correctly estimated the expected profitability of our existing first-lien mortgage portfolio or that the second-lien PDR established will be adequate to cover the ultimate losses on our second-lien business.

For our financial guaranty business, to determine whether a premium deficiency charge is necessary, we compare projected earned premiums and investment income to projected future losses, LAE, unamortized deferred acquisition costs and maintenance costs. If the sum of the costs exceeds the amount of the revenues, the excess is first charged against deferred acquisition costs and is referred to as a premium deficiency charge. For our financial guaranty business, no PDR was necessary as of March 31, 2014 or December 31, 2013.

## ***Fair Value of Financial Instruments***

Our estimated fair value measurements are intended to reflect the assumptions market participants would use in pricing an asset or liability based on the best information available. Assumptions include the risks inherent in a particular valuation technique (such as a pricing model) and the risks inherent in the inputs to the model. Changes in economic conditions and capital market conditions, including but not limited to, credit spread changes, benchmark interest rate changes, market volatility and changes in the value of underlying collateral or of any third-party guaranty or insurance, could cause actual results to differ materially from our estimated fair value measurements. We define fair value as the current amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In the event that our investments or derivative contracts were sold, commuted, terminated or settled with a counterparty or transferred in a forced liquidation, the amounts received or paid may be materially different from those determined in accordance with the accounting standard regarding fair value measurements. Differences may also arise between our recorded fair value and the settlement or termination value with a counterparty based upon consideration of information that may not be available to another market participant. Those differences, which may be material, are recorded as realized gains (losses) in our condensed consolidated statements of operations in the period in which the transaction occurs.

When determining the fair value of our liabilities, we are required to incorporate into the fair value of those liabilities an adjustment that reflects our own non-performance risk. Our CDS spread is an observable quantitative measure of our non-performance risk and is used by typical market participants to determine the likelihood of our default. Assuming all other factors are held constant, as our CDS spread tightens or widens, it has the effect of increasing or decreasing, respectively, the fair value of our liabilities with a corresponding impact on our results of operations.

In accordance with GAAP, we established a three-level valuation hierarchy for disclosure of fair value measurements based on the transparency of inputs to the valuation of an asset or liability as of the measurement date. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level I measurements) and the lowest priority to unobservable inputs (Level III measurements). The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the measurement in its entirety. The three levels of the fair value hierarchy are defined below:

- Level I — Unadjusted quoted prices for identical assets or liabilities in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level II — Prices or valuations based on observable inputs other than quoted prices in active markets for identical assets and liabilities; and
- Level III — Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable. Level III inputs are used to measure fair value only to the extent that observable inputs are not available.

For markets in which inputs are not observable or are limited, we use significant judgment and assumptions that a typical market participant would use to evaluate the market price of an asset or liability. Given the level of judgment necessary, another market participant may derive a materially different estimate of fair value. These assets and liabilities are classified in Level III of our fair value hierarchy.

At March 31, 2014, our total Level III assets were approximately 4.1% of total assets measured at fair value and total Level III liabilities accounted for 100.0% of total liabilities measured at fair value.

Available for sale securities, trading securities, VIE debt, derivative instruments and certain other assets are recorded at fair value as described in Note 4 of Notes to Unaudited Condensed Consolidated Financial Statements. All derivative instruments and contracts are recognized in our consolidated balance sheets as either derivative assets or derivative liabilities. All changes in fair value of trading securities, VIE debt, derivative instruments and certain other assets are included in our condensed consolidated statements of operations. All changes in the fair value of available for sale securities are recorded in accumulated other comprehensive income (loss).

The following are descriptions of our valuation methodologies for financial assets and liabilities measured at fair value.

### ***Investments***

*U.S. government and agency securities*—The fair value of U.S. government and agency securities is estimated using observed market transactions, including broker-dealer quotes and actual trade activity as a basis for valuation. U.S. government and agency securities are categorized in either Level I or Level II of the fair value hierarchy.

*State and municipal obligations*—The fair value of state and municipal obligations is estimated using recent transaction activity, including market and market-like observations. Evaluation models are used, which incorporate bond structure, yield curve, credit spreads and other factors. These securities are generally categorized in Level II of the fair value hierarchy or in Level III when market-based transaction activity is unavailable.

*Money market instruments*—The fair value of money market instruments is based on daily prices, which are published and available to all potential investors and market participants. As such, these securities are categorized in Level I of the fair value hierarchy.

*Corporate bonds and notes*—The fair value of corporate bonds and notes is estimated using recent transaction activity, including market and market-like observations. Spread models are used that incorporate issuer and structure characteristics, such as credit risk and early redemption features, where applicable. These securities are generally categorized in Level II of the fair value hierarchy or in Level III when market-based transaction activity is unavailable.

*RMBS, CMBS and Other ABS*—The fair value of these instruments is estimated based on prices of comparable securities and spreads and observable prepayment speeds. These securities are generally categorized in Level II of the fair value hierarchy or in Level III when market-based transaction activity is unavailable. The fair value of any Level III securities is generally estimated by discounting estimated future cash flows.

*Foreign government and agency securities*—The fair value of foreign government and agency securities is estimated using observed market yields used to create a maturity curve and observed credit spreads from market makers and broker-dealers. These securities are categorized in Level II of the fair value hierarchy.

*Hybrid securities*—These instruments are convertible securities. The estimated fair value is derived, in part, by utilizing dealer quotes and observed bond and stock prices. For certain securities, the underlying security price may be adjusted to account for observable changes in the conversion and investment value from the time the quote was obtained. These securities are categorized in Level II of the fair value hierarchy.

*Equity securities*—The fair value of these securities is generally estimated using observable market data in active markets or bid prices from market makers and broker-dealers. Generally, these securities are categorized in Level I or II of the fair value hierarchy, as observable market data are readily available. A small number of our equity securities, however, are categorized in Level III of the fair value hierarchy due to a lack of market-based transaction data or the use of model-based evaluations.

*Other investments*—These securities primarily consist of deposit investments and short-term certificates of deposit (“CDs”), which are categorized in Level II and Level III of the fair value hierarchy, and a guaranteed investment contract held by one of our consolidated VIEs, which is categorized in Level III of the fair value hierarchy. The fair value of the Level III securities is generally estimated by discounting estimated future cash flows.

We are responsible for the determination of the value of all investments carried at fair value and the supporting methodologies and assumptions. To assist us in this responsibility, we utilize independent third-party valuation service providers to gather, analyze and interpret market information and estimate fair values based upon relevant methodologies and assumptions for various asset classes and individual securities. We perform monthly quantitative and qualitative analysis on the prices received from third parties to determine whether the prices are reasonable estimates of fair value. Our analysis includes: (i) a review of the methodology used by third-party pricing services; (ii) a comparison of pricing services’ valuations to other independent sources; (iii) a review of month-to-month price fluctuations; and (iv) a comparison of actual purchase and sale transactions with valuations received from third parties. These processes are designed to ensure that our investment values are accurately recorded, that the data inputs and valuation techniques utilized are appropriate and consistently applied and that the assumptions are reasonable and consistent with the objective of determining fair value.

#### *Derivative Instruments and Related VIE Assets/Liabilities*

We define fair value as the current amount that would be exchanged to sell an asset or transfer a liability, other than in a forced liquidation. In determining an exit market, we consider the fact that most of our derivative contracts are unconditional and irrevocable and contractually prohibit us from transferring them to other capital market participants. Accordingly, there is no principal market for such highly structured insured credit derivatives. In the absence of a principal market, we value these insured credit derivatives in a hypothetical market where market participants include other monoline mortgage and financial guaranty insurers with similar credit quality to us, as if the risk of loss on these contracts could be transferred to these other mortgage and financial guaranty insurance and reinsurance companies. We believe that in the absence of a principal market, this hypothetical market provides the most relevant information with respect to fair value estimates.

We determine the fair value of our derivative instruments primarily using internally-generated models. We utilize market observable inputs, such as credit spreads on similar products, whenever they are available. When one of our transactions develops characteristics that are inconsistent with the characteristics of transactions that underlie the relevant market-based index that we use in our credit spread valuation approach, and more relevant inputs or projections become available and would represent the view of a typical market participant, we change to an approach that is based on that more relevant available information. This change in approach is generally prompted when the credit component, and not market factors, becomes the dominant driver of the estimated fair value for a particular transaction. There is a high degree of uncertainty about our fair value estimates since our contracts are not traded or exchanged, which makes external validation and corroboration of our estimates difficult, particularly given the current market environment, in which very few, if any, contracts are being traded or originated.

Our derivative liabilities valuation methodology incorporates our own non-performance risk by including our observable CDS spread as an input into the determination of the fair value of our derivative liabilities. Considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates may not be indicative of amounts we could realize in a current market exchange or negotiated termination. Our derivative liability valuation is not counterparty specific and is intended to estimate the average exchange price between typical participants. The use of different market assumptions or estimation methodologies may have a material effect on the estimated fair value amounts or negotiated terminations. In a negotiated termination, certain factors unique to the counterparty may have a greater impact on the amount exchanged than in an estimated fair value amount between typical market participants and another market participant could have materially different views given the level of judgment associated with the valuation.

#### *Corporate CDOs*

The fair value of each of our corporate CDO transactions is estimated based on the difference between: (1) the present value of the expected future contractual premiums we charge; and (2) the fair premium amount that we estimate that another financial guarantor would require to assume the rights and obligations under our contracts. The fair value estimates reflect the fair value of the asset or liability, which is consistent with the “in-exchange” approach, in which fair value is determined based on the price that would be received or paid in a current transaction as defined by the accounting standard regarding fair value measurements. These credit derivatives are categorized in Level III of the fair value hierarchy.

*Present Value of Expected Future Contractual Premiums*—Our contractual premiums are subject to change primarily for two reasons: (1) all of our contracts provide our counterparties with the right to terminate upon our default; and (2) 88% of the aggregate net par outstanding of our corporate CDO transactions (as of March 31, 2014) provide our counterparties with an additional right to terminate these transactions that is currently exercisable at any time. In determining the expected future premiums of these transactions, we adjust the contractual premiums for such transactions to reflect the estimated fair value of those premiums based on our estimate of the probability of our counterparties exercising this termination right and the impact it would have on the remaining expected lifetime premium. We also cap the total estimated fair value of the contracts subject to termination such that none of these contracts are in a derivative asset position. As of March 31, 2014, 8% of the aggregate net par outstanding of our corporate CDO transactions was capped in this manner. The discount rate we use to determine the present value of expected future premiums is our CDS spread plus a risk-free rate. This discount rate reflects the risk that we may not collect future premiums due to our inability to satisfy our contractual obligations, which provides our counterparties the right to terminate the contracts.

*Determining the Fair Premium Amount*—For each corporate CDO transaction, we perform three principal steps in determining the fair premium amount:

- first, we define a tranche on the CDX index (defined below) that equates to the risk profile of our specific transaction (we refer to this tranche as an “equivalent-risk tranche”);
- second, we determine the fair premium amount on the equivalent-risk tranche for those market participants engaged in trading on the CDX index (we refer to each of these participants as a “typical market participant”); and
- third, we adjust the fair premium amount for a typical market participant to account for the difference between the non-performance or default risk of a typical market participant and the non-performance or default risk of a financial guarantor of similar credit quality to us (in each case, we refer to the risk of non-performance as “non-performance risk”).

*Defining the Equivalent-Risk Tranche*—Direct observations of fair premium amounts for our transactions are not available because these transactions cannot be traded or transferred pursuant to their terms and there is currently no active market for these transactions. However, CDS on tranches of a standardized index (the “CDX index”) are widely traded and observable and provide relevant market data for determining the fair premium amount of our transactions, as described more fully below.

The CDX index is an index based on a synthetic corporate CDO that comprises a list of corporate obligors and is segmented into multiple tranches of synthetic senior unsecured debt of these obligors ranging from the equity tranche (i.e., the most credit risk or first-loss position) to the most senior tranche (i.e., the least credit risk). We refer to each of these tranches as a “standard CDX tranche.” A tranche is defined by an attachment point and detachment point, representing the range of portfolio losses for which the protection seller would be required to make a payment.

Our corporate CDO transactions possess similar structural features to the standard CDX tranches, but often differ with respect to the referenced corporate entities, the term, the attachment points and the detachment points. Therefore, in order to determine the equivalent-risk tranche for each of our corporate CDO transactions, we determine the attachment and detachment points on the CDX index that have comparable estimated probabilities of loss as the attachment and detachment points in our transactions. We begin by performing a simulation analysis of referenced entity defaults in our transactions to determine the probability of portfolio losses exceeding our attachment and detachment points. The referenced entity defaults are primarily determined based on the following inputs: the market observed CDS credit spreads of the referenced corporate entities, the correlations between each of the referenced corporate entities and the term of the transaction.

For each referenced corporate entity in our corporate CDO transactions, the CDS spreads associated with the term of our transactions (“credit curve”) define the estimated expected loss for each entity (as applied in a market standard approach known as “risk neutral” modeling). The credit curves on individual referenced entities are generally observable. The expected cumulative loss for the portfolio of referenced entities associated with each of our transactions is the sum of the expected losses of these individual referenced entities. With respect to the correlation of losses across the underlying reference entities, two obligors belonging to the same industry or located in the same geographical region are assumed to have a higher probability of defaulting together (i.e., they are more correlated). An increase in the correlations between the referenced entities generally causes a higher expected loss for the portfolio associated with our transactions. The estimated correlation factors that we use are derived internally based on observable third-party inputs from historical data.

The impact of our correlation assumptions currently does not have a material effect on our fair premium estimates in light of the significant impact of our non-performance risk adjustment as described below.

Once we have established the probability of portfolio losses exceeding the attachment and detachment points in our transactions, we then use the same simulation method to locate the attachment and detachment points on the CDX index with comparable probabilities. These equivalent attachment and detachment points define the equivalent-risk tranche on the CDX index that we use to determine fair premium amounts.

*Determining the Typical Fair Premium Amount*—The equivalent-risk tranches for our corporate CDO transactions often are not identical to any standard CDX tranches. As a result, fair premium amounts generally are not directly observable from the CDX index for the equivalent-risk tranche and must be separately determined. We make this determination through an interpolation in which we use the observed premium rates on the standard CDX tranches that most closely match our equivalent-risk tranche to derive the typical fair premium amount for the equivalent-risk tranche.

*Non-Performance Risk Adjustment on Corporate CDOs*—The typical fair premium amount estimated for the equivalent-risk tranche represents the fair premium amount for a typical market participant—not Radian. Accordingly, the final step in our fair value estimation is to convert this typical fair premium amount into a fair premium amount for a financial guarantor of similar credit quality to us. A typical market participant is contractually bound by a requirement that collateral be posted regularly to minimize the impact of that participant’s default or non-performance. This collateral posting feature makes these transactions less risky to the protection buyer, and therefore, priced differently. None of our contracts require us to post collateral with our counterparties, which exposes our counterparties fully to our non-performance risk. We make an adjustment to the typical fair premium amount to account for both this contractual difference, as well as for the market’s perception of our default probability, which is observable through our CDS spread.

The amount of the non-performance risk adjustment is computed based, in part, on the expected claim payment by Radian. To estimate this expected payment, we first determine the expected claim payment of a typical market participant by using a risk-neutral modeling approach. A significant underlying assumption of the risk-neutral model approach that we use is that the typical fair premium amount is equal to the present value of expected claim payments from a typical market participant. Expected claim payments on a transaction are based on the expected loss on that transaction (also determined using the risk-neutral modeling approach). Radian’s expected claim payment is calculated based on the correlation between the default probability of the transaction and our default probability. The default probability of Radian is determined from the observed Radian Group CDS spread and the default probability of the transaction is determined as described above under “—*Defining the Equivalent-Risk Tranche.*” The present value of Radian’s expected claim payments is discounted using a risk-free interest rate, as the expected claim payments have already been risk-adjusted.



Our non-performance risk adjustment currently results in a material reduction of our typical fair premium amounts, which in turn has a positive impact on the fair value of these derivatives.

#### *Non-Corporate CDOs and Other Derivative Transactions*

Our non-corporate CDO transactions include our guaranty of TruPs CDOs, CDOs of CMBS and CDOs backed by other asset classes such as: (i) municipal securities; (ii) synthetic financial guarantees of ABS; and (iii) project finance transactions. The fair value of our non-corporate CDOs and other derivative transactions is calculated as the difference between the present value of the expected future contractual premiums and our estimate of the fair premium amount for these transactions. The present value of expected future contractual premiums is determined based on the methodology described above for corporate CDOs. As of March 31, 2014, 95% of the aggregate net par outstanding of our non-corporate CDO contracts provide our counterparties with a right to terminate these transactions that is exercisable at any time. We also cap the total estimated fair value of the contracts subject to termination such that none of these contracts are in a derivative asset position. As of March 31, 2014, 12% of the aggregate net par outstanding of our non-corporate CDO transactions was capped in this manner. In all other instances, we utilize internal models to estimate the fair premium amount as described below. These credit derivatives are categorized in Level III of the fair value hierarchy.

*TruPs CDOs and TruPs-Related VIE Liabilities*—Our TruPs transactions are CDS on CDOs where the collateral consists primarily of deeply subordinated securities issued by banks, insurance companies, real estate investment trusts and other financial institutions whose individual spreads are not observable. In each case, we provide credit protection on a specific tranche of each CDO. To determine fair value for these transactions, we use a discounted cash flow valuation approach that captures the credit characteristics of each transaction. We estimate projected claims based on our internal credit analysis, which is based on the current performance of each underlying reference obligation. The present value of the expected cash flows of the TruPs transaction is then determined using a discount rate derived from the observed market pricing for a TruPs transaction with similar characteristics. The present value of the insured cash flows is determined using a discount rate that is equal to our CDS rate plus a risk-free rate.

With respect to four insured TruPs transactions, our counterparties may require that we pay a liquidity claim for the outstanding par amount on the underlying TruPs bonds. For these transactions, an additional fair value adjustment is made. To calculate this adjustment, a probability that we will be required to pay a liquidity claim is assigned based on our internal cash flow projections. A discounted cash flow valuation is also performed for this scenario where we are required to pay a liquidity claim. The fair value is set equal to the probability weighted average of the valuations from two scenarios: one in which our counterparty pays a liquidity claim and one in which the claim is not paid.

In the second quarter of 2012, we agreed with one of our derivative counterparties (the “Counterparty”) to commute our credit protection on six of our directly insured TruPs CDO transactions. A significant portion of the amount paid in consideration for these commutations was deposited with an LPV (considered a VIE in accordance with the accounting guidance regarding VIEs). These funds were segregated to cover the Counterparty’s potential future losses on the TruPs bonds underlying the Terminated TruPs CDOs (the “Terminated TruPs Bonds”) through a CDS entered into by the VIE with the Counterparty. The CDS terminates concurrently with the Terminated TruPs Bonds for which we had provided credit protection, and provides for payment to the Counterparty substantially in accordance with the terms of our original CDS protection for the Terminated TruPs Bonds. In addition, pursuant to an agreement with the Counterparty, if any LPV Capital amount is remaining following the maturity of the CDS, Radian Asset Assurance is entitled to these remaining funds.

We consolidate this VIE and record the VIE’s assets and liabilities at fair value. To determine fair value for the VIE liabilities, we use a discounted cash flow valuation approach that captures the credit characteristics of each transaction. We estimate projected claims based on our internal credit analysis, which is based on the current performance of each underlying reference obligation.

*CDOs of CMBS*—The fair premium amounts for our CDO of CMBS transactions for a typical market participant are derived first by observing the spreads of the CMBX indices that match the underlying reference obligations of our transactions. A mezzanine tranche, which represents our insured tranche, is then priced through a standard CDO model. The CMBX indices represent standardized lists of CMBS reference obligations. A different CMBX index exists for different types of underlying referenced obligations based on vintages and credit rating. For each of our CDO of CMBS transactions, we use the CMBX index that most directly correlates to our transaction with respect to vintage and credit rating. Because the observable CMBS indices do not have a similar mezzanine tranche, we use an internal CDO pricing model in order to adjust fair value for this structural feature. A standard CDO pricing model was calibrated to establish the market pricing at inception. This CDO pricing model is then applied to the current valuation period to derive the fair premium for the mezzanine tranche. The typical fair premium amount represents the estimated fair value of the expected future fair premiums determined by using a discount rate equal to the CDS spread of a typical market participant plus a risk-free rate.

*All Other Non-Corporate CDOs and Other Derivative Transactions*—The fair value estimates for certain derivative instruments are derived using observable market inputs that are indicative of exit price, when available, and are categorized in Level II of the fair value hierarchy. For all of our other non-corporate CDOs and other derivative transactions, observed prices and market indices are not available. As a result, we utilize an internal model that estimates fair premium. The fair premium amount is calculated such that the expected profit (fair premium amount net of expected losses and other expenses) is proportional to an internally-developed risk-based capital amount. Expected losses and our internally developed risk-based capital amounts are projected by our model using the internal credit rating, term and current par outstanding for each transaction.

For each of the non-corporate CDOs and other derivative transactions discussed above, with the exception of our TruPs transactions that are valued using a discounted cash flow analysis, we make an adjustment to the fair premium amounts, as described above under “—*Non-Performance Risk Adjustment on Corporate CDOs*,” to incorporate our own non-performance risk. The non-performance risk adjustment associated with our TruPs transactions is incorporated in the fair value as described above; therefore, no separate adjustment is required. These credit derivatives are categorized in Level III of the fair value hierarchy.

#### *Assumed Financial Guaranty Credit Derivatives*

In making our determination of fair value for these credit derivatives, we use information provided to us by our counterparties to these reinsurance transactions, which are the primary insurers (the “primaries”) of the underlying credits, including the primaries’ fair valuations for these credits. The information obtained from our counterparties is not received with sufficient time for us to properly record the mark-to-market liability as of the balance sheet date. Therefore, the amount recorded as of March 31, 2014 is based on the most recent available financial information, which is reported on a quarterly lag. The lag in reporting is consistent from period to period. The fair value is based on credit spreads obtained by the primaries from market data sources published by third parties (e.g., dealer spread tables for collateral similar to assets within the transactions being valued), as well as collateral-specific spreads provided by trustees or obtained from market sources if such data is available. If observable market spreads are not available or reliable for the underlying reference obligations, then the primaries’ valuations are predominantly based on market indices that most closely resemble the underlying reference obligations, considering asset class, credit quality rating and maturity of the underlying reference obligations. In addition, these valuations incorporate an adjustment for non-performance risk. The primaries’ models used to estimate the fair value of these instruments include a number of factors, including credit spreads, changes in interest rates and the credit ratings of referenced entities. In establishing our fair value for these transactions, we assess the reasonableness of the primaries’ valuations by: (1) reviewing the primaries’ publicly available information regarding their mark-to-market processes, including methodology and key assumptions; and (2) analyzing and discussing the changes in fair value with the primaries where the changes appear unusual or do not appear materially consistent with credit loss related information when provided by the primaries for these transactions. These credit derivatives are categorized in Level III of the fair value hierarchy.

#### *Other Financial Guaranty VIE Debt and Other Assets*

We are the primary beneficiary for two other VIEs for which we have provided financial guarantees. These VIEs primarily consist of manufactured housing loans and VIE debt to note holders in the trust. The fair value of the VIE debt related to these other financial guaranty VIEs is estimated based on prices of comparable securities and spreads observed in the market. The overall net fair value for these transactions is determined using a discounted cash flow analysis. We do not currently estimate any projected claims based on our internal credit analysis, which is based on the current performance of the underlying collateral and the remaining subordination available to support the transaction. The present value of the insured cash flows is determined by using a discount rate that is equal to our CDS rate plus a risk-free rate. We utilize this model to determine the fair value of our exposure to these VIEs and to derive the fair value of the assets in these VIEs, which are reported within other assets on our condensed consolidated balance sheets.

The assets and VIE debt related to these transactions are categorized in Level III of the fair value hierarchy. Our maximum principal exposure to loss from these transactions is \$106.5 million; however, we do not currently expect to pay any claims related to these two VIEs. At March 31, 2014, we recorded \$92.5 million of other assets, \$92.4 million of VIE debt and \$0.02 million of other liabilities associated with these two VIEs.

## ***VIEs***

As a provider of credit enhancement, we have entered into insurance contracts with VIEs and derivative contracts with counterparties where we have provided credit protection directly on variable interests and, in some cases, obtained the contractual rights of our counterparties with respect to the VIEs. VIEs include corporations, trusts or partnerships in which equity investors do not have a controlling financial interest or do not have sufficient equity at risk to finance activities without additional subordinated financial support.

An entity is considered the primary beneficiary and is required to consolidate a VIE if its variable interest: (i) gives it the power to most significantly impact the economic performance of the VIE; and (ii) has the obligation to absorb losses or the right to receive residual benefits that could potentially be significant to the VIE. For all VIEs in which we have a variable interest, we assess whether we are the primary beneficiary. In determining whether we are the primary beneficiary, a number of factors are considered, including the structure of the entity, provisions in our insurance contracts that grant us additional rights to influence or control the economic performance of the VIE upon the occurrence of an event of default, a servicer termination event or the breach of a performance trigger, and our obligation to absorb significant losses. The breach of these performance tests or other events that give rise to our right to influence or control the economic performance of the VIE may occur, particularly if credit performance deteriorates. When we acquire control rights, we perform an analysis to reassess our involvement with these VIEs to determine whether we have become the primary beneficiary.

When evaluating whether we are the primary beneficiary of a VIE, we determine which activities most significantly impact the economic performance of the VIE. As part of our qualitative analysis, we consider whether we have any contractual rights that would allow us to direct those activities. As of March 31, 2014, we are the primary beneficiary of our NIMS transactions and certain financial guaranty structured finance transactions. Our control rights in these VIEs, which we obtained due to an event of default or breach of a performance trigger as defined in the transaction, generally provide us with either a right to replace the VIE servicer or, in some cases, the right to direct the sale of the VIE assets. In those instances where we have determined that we are the primary beneficiary, we consolidate the assets and liabilities of the VIE. We have elected to carry the financial assets and financial liabilities of these VIEs at fair value.

## ***Investments***

We group assets in our investment portfolio into one of three main categories: held to maturity, available for sale or trading securities. Fixed-maturity securities for which we have the positive intent and ability to hold to maturity are classified as held to maturity and are reported at amortized cost. Investments in securities not classified as held to maturity or trading securities are classified as available for sale and are reported at fair value, with unrealized gains and losses (net of tax) reported as a separate component of stockholders' equity as accumulated other comprehensive income (loss). Investments classified as trading securities are reported at fair value, with unrealized gains and losses reported as a separate component of income. Short-term investments consist of money market instruments, CDs and highly liquid, interest-bearing instruments with an original maturity of three months or less at the time of purchase. Amortization of premium and accretion of discount are calculated principally using the interest method over the term of the investment. Realized gains and losses on investments are recognized using the specific identification method.

For certain hybrid financial instruments that would be required to be separated into a host contract and a derivative instrument, the accounting standard regarding derivatives and hedging permits an entity to irrevocably elect to initially and subsequently measure that hybrid financial instrument in its entirety at fair value (with changes in fair value recognized in earnings). We elected to record our convertible securities meeting these criteria at fair value with changes in the fair value recorded as net gains or losses on investments. All hybrid financial instruments are classified as trading securities.

We record an other-than-temporary impairment adjustment on a security if we intend to sell the impaired security, if it is more likely than not that we will be required to sell the impaired security prior to recovery of its amortized cost basis, or if the present value of cash flows we expect to collect is less than the amortized cost basis of the security. If a sale is likely, the security is classified as other-than-temporarily impaired and the full amount of the impairment is recognized as a loss in the statement of operations. Otherwise, losses on securities that are other-than-temporarily impaired are separated into: (i) the portion of loss that represents the credit loss; and (ii) the portion that is due to other factors. The credit loss portion is recognized as a loss in the statement of operations, while the loss due to other factors is recognized in accumulated other comprehensive income (loss), net of taxes. A credit loss is determined to exist if the present value of discounted cash flows expected to be collected from the security is less than the cost basis of the security. The present value of discounted cash flows is determined using the original yield of the security. In evaluating whether a decline in value is other-than-temporary, we consider several factors in addition to the above, including, but not limited to, the following:

- the extent and the duration of the decline in value;

- the reasons for the decline in value (e.g., credit event, interest related or market fluctuations); and
- the financial position, access to capital and near term prospects of the issuer, including the current and future impact of any specific events.

### ***Income Taxes***

We provide for income taxes in accordance with the provisions of the accounting standard regarding accounting for income taxes. As required under this standard, our deferred tax assets and liabilities are recognized under the balance sheet method, which recognizes the future tax effect of temporary differences between the amounts recorded in our condensed consolidated financial statements and the tax bases of these amounts. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the periods in which the deferred tax asset or liability is expected to be realized or settled.

We are required to establish a valuation allowance against our DTA when it is more likely than not that all or some portion of our DTA will not be realized. At each balance sheet date, we assess our need for a valuation allowance. Our assessment is based on all available evidence, both positive and negative. This requires management to exercise judgment and make assumptions regarding whether our DTA will be realized in future periods. Future realization of our DTA will ultimately depend on the existence of sufficient taxable income of the appropriate character (ordinary income or capital gains) within the applicable carryback and carryforward periods provided under the tax law. In making this assessment, the primary negative evidence that we considered are our cumulative losses in recent years and the continued uncertainty regarding our future results. We also considered positive evidence when assessing the need for a valuation allowance, such as future reversals of existing taxable temporary differences, future projections of taxable income, taxable income within the applicable carryback periods and potential tax planning strategies. In assessing our need for a valuation allowance, the weight assigned to the effect of both negative and positive evidence is commensurate with the extent to which such evidence can be objectively verified. Forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence, such as cumulative losses, as we have experienced. We will continue to assess the need to maintain a valuation allowance against our net DTAs at each reporting date. Recognition of our DTAs may be based on the continued improvement in operating results and increased certainty regarding our projected incurred losses, and our ability to sustain profitability over an appropriate time period in amounts that are sufficient to support a conclusion that it is more likely than not that all or a portion of our DTAs will be realized. It is reasonably possible that we could meet these criteria in the foreseeable future.

Our provision for income taxes for interim financial periods is based on an estimate of our annual effective tax rate (“ETR”) for the full year of 2014. When estimating our full year 2014 ETR, we adjust our forecasted pre-tax income for gains and losses on our derivative transactions and investments, changes in the accounting for uncertainty in income taxes, changes in our beginning of year valuation allowance, and other adjustments. The impact of these items are accounted for discretely at the federal applicable tax rate. During 2013, given the impact on our pre-tax results of net gains or losses resulting from our derivative transactions and our investment portfolio, and the continued uncertainty regarding our ability to rely on certain short-term financial projections, which directly affected our ability to estimate an effective tax rate for the full year, we recorded our interim period income tax provision (benefit) based on actual results of operations.

### ***Recent Accounting Pronouncements***

In July 2013, the Financial Accounting Standards Board issued an update to the accounting standard regarding income taxes. This update provides guidance concerning the balance sheet presentation of an unrecognized tax benefit when a net operating loss carryforward or a tax credit carryforward (the “Carryforwards”) is available. This accounting standard requires an entity to net its liability related to unrecognized tax benefits against the related deferred tax assets for the Carryforwards. A gross presentation will be required when the Carryforwards are not available under the tax law of the applicable jurisdiction or when the Carryforwards would not be used by the entity to settle any additional income taxes resulting from disallowance of the uncertain tax position. This update is effective for fiscal years and interim periods within such years beginning after December 15, 2013. We adopted this update in the first quarter of 2014. As a result of our implementation of this new FASB guidance, our March 31, 2014 condensed consolidated balance sheet reflects a full valuation allowance against our DTAs as our remaining DTA was reduced by the reclassification of our liability for unrecognized tax benefits. The adoption of this update did not affect the recognition or measurement of uncertain tax positions and did not have a significant impact on our consolidated financial statements or disclosures. See Note 12 of Notes to Unaudited Condensed Consolidated Financial Statements for additional information.

As of the filing date of this report, there were no new accounting pronouncements issued but not yet effective that are expected to have an impact on the Company’s consolidated financial statements.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Market risk represents the potential for loss due to adverse changes in the value of financial instruments as a result of changes in market conditions. Examples of market risk include changes in interest rates, foreign currency exchange rates, credit spreads and equity prices. We perform a sensitivity analysis to determine the effects of market risk exposures on our investment securities. In addition, we perform a sensitivity analysis for certain of our financial guaranty contracts that are required to be carried at fair value, and therefore are subject to market risks, including changes in interest rates and credit spreads. Our sensitivity analysis for interest rates and credit spreads is generally calculated as a parallel shift in yield curve with all other factors remaining constant. This analysis is performed by determining the potential loss in future earnings, fair values or cash flows of market-risk-sensitive instruments resulting from one or more selected hypothetical changes in interest rates, foreign currency exchange rates, credit spreads and equity prices.

#### ***Interest-Rate Risk***

The primary market risk in our investment portfolio is interest-rate risk, namely the fair value sensitivity of a fixed-income security to changes in interest rates. We regularly analyze our exposure to interest-rate risk and have determined that the fair value of our interest-rate-sensitive investment assets is materially exposed to changes in interest rates.

We estimate the changes in fair value of our fixed-income securities by projecting an instantaneous increase and decrease in interest rates. The carrying value of our total investment portfolio at March 31, 2014 and December 31, 2013 was \$4.9 billion, of which 94% was invested in fixed-income securities. We calculate duration of our fixed-income securities, expressed in years, in order to estimate interest rate sensitivity of these securities. At March 31, 2014, a 100 basis point increase in interest rates would reduce the market value of our fixed-income securities by \$190.7 million, while a 100 basis point decrease in interest rates would increase the market value of our fixed-income securities by \$156.9 million. At March 31, 2014, the average duration of the fixed-income portfolio was 3.4 years compared to 3.7 years at December 31, 2013, reflecting an increase in the percentage of short-term securities in the portfolio.

#### ***Credit Risk***

A significant portion of our credit protection is in the form of CDS and other financial guaranty contracts that are marked to market through earnings. These financial guaranty derivative contracts generally insure obligations with considerable subordination beneath our exposure at the time of issuance. The underlying asset classes of these obligations include corporate entities, asset-backed securities, RMBS, CMBS, TruPs and related VIEs. The value of our financial guaranty derivative contracts are affected predominantly by changes in credit spreads. As credit spreads and ratings change, the value of these financial guaranty derivative contracts change and the resulting gains and losses are recorded in our operating results. We have also incorporated the market's perception of our non-performance risk into the market value of our derivative instruments. We have determined that the fair value of our CDS and other financial guaranty contracts is materially exposed to changes in credit spreads, including our own credit spread. We have used and may continue to utilize various forms of credit enhancement in order to mitigate potential losses from changes in the credit ratings of our counterparties or the underlying collateral in our financial guaranty contracts.

Sensitivity to changes in credit spreads can be estimated by projecting a hypothetical instantaneous shift in credit spread curves. The following tables present the pre-tax change in the fair value of our insured derivatives portfolio and our VIE debt as a result of instantaneous shifts in credit spreads, as well as our own credit default spread as of March 31, 2014. These changes were calculated using the valuation methods described in "Critical Accounting Policies—*Fair Value of Financial Instruments*" above, which also includes a discussion of the material limitations of such methods. See also "Management's Discussion and Analysis of Financial Condition and Results of Operations—Results of Operations—Consolidated—*Impact of Radian's Non-performance Risk on Financial Guaranty Results.*" Contracts for which the fair value is calculated using specific dealer quotes or actual transaction prices are excluded from the following tables. Radian Group's five-year CDS spread was 2.88% at March 31, 2014 and reflects the perceived risk that investors associate with us, which we are required to consider when determining our fair values; the CDS spread actually used in the valuation of specific fair value liabilities is typically based on the remaining term of the insured obligation. Non-performance risk is commonly measured by default probability, with a credit spread tightening indicating a lesser probability of default. Radian Group's five-year CDS spread at March 31, 2014 implies a market view that there is a 21.1% probability that Radian Group will default in the next five years, as compared to a 22.9% implied probability of default at December 31, 2013.

**Corporate CDOs (\$ in millions)**

Weighted average credit spread		0.31%
Fair value of net liabilities	\$	2.5

**Increase (Decrease) in Fair Value Net Liability based on:**

	10% tightening of CDO credit spreads	0% change in CDO credit spreads	10% widening of CDO credit spreads
50% tightening of Radian Group's CDS spread	\$ 9.0	\$ 11.7	\$ 14.3
0 basis points change in Radian Group's CDS spread	(1.4)	—	1.4
50% widening of Radian Group's CDS spread	(5.8)	(5.1)	(4.3)

**Non-Corporate CDO related (1) (\$ in millions)**

Weighted average credit spread		1.37%
Fair value of net liabilities	\$	193.3

**Increase (Decrease) in Fair Value Net Liability based on:**

	10% tightening of CDO credit spreads	0% change in CDO credit spreads	10% widening of CDO credit spreads
50% tightening of Radian Group's CDS spread	\$ 67.5	\$ 104.4	\$ 140.6
0 basis points change in Radian Group's CDS spread	(25.9)	—	25.6
50% widening of Radian Group's CDS spread	(44.9)	(21.2)	1.7

(1) Includes TruPs, CDOs of CMBS and other non-corporate CDOs and related VIEs.

Given the relatively high level of volatility in spreads, including our own CDS spread, for our derivative transactions and VIE debt, the sensitivities presented above are higher than our longer term historical experience. The range of a 50% tightening and widening was determined based on our current CDS spread and recent experience.

**Foreign Exchange Rate Risk**

As of March 31, 2014 and December 31, 2013 we did not hold any foreign currency denominated securities in our investment portfolio.

**Equity Market Price**

At March 31, 2014, the market value and cost of the equity securities in our investment portfolio was \$226.8 million and \$161.5 million, respectively. Included in the market value and cost of our equity securities at March 31, 2014 was \$88.9 million and \$83.4 million, respectively, of securities classified as trading securities. At December 31, 2013, the market value and cost of the equity securities in our investment portfolio was \$225.8 million and \$164.9 million, respectively. Included in the market value and cost of our equity securities at December 31, 2013 is \$90.6 million and \$86.8 million, respectively, of securities classified as trading securities. Exposure to changes in equity market prices can be estimated by assessing potential changes in market values on our equity investments resulting from a hypothetical broad-based decline in equity market prices of 10%. With all other factors remaining constant, we estimated that such a decrease would reduce our investment portfolio held in equity investments by \$22.7 million as of March 31, 2014.

We have certain long-term incentive awards issued primarily in 2011 and 2012 that are cash-settled. The compensation expense is based on the estimated fair value of the liability, and is impacted by changes in our stock price and, to a lesser extent, other factors. The related liability is adjusted quarterly based on changes in our current stock price during the period and other factors that we utilize to estimate the ultimate payout of each award. For the three months ended March 31, 2014, our operating expenses included \$13.6 million for these long-term incentive awards compared to \$38.0 million for the three months ended March 31, 2013. Included in these expenses were changes in the estimated fair value of the liability for these long-term incentive awards of \$7.8 million and \$24.6 million, respectively, primarily due to changes in our stock price, which increased by \$0.91 and \$4.60, respectively, during the three-month periods ended March 31, 2014 and March 31, 2013.

#### **Item 4. Controls and Procedures.**

##### **Disclosure Controls and Procedures**

We maintain disclosure controls and procedures designed to ensure that information required to be disclosed in the reports we file or submit under the Securities and Exchange Act of 1934 as amended (the “Exchange Act”) is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Our management, including our Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act) as of March 31, 2014, pursuant to Rule 15d-15(e) under the Exchange Act. Management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures, which by their nature can provide only reasonable assurance regarding management’s control objectives. Management does not expect that our disclosure controls and procedures will prevent or detect all errors and fraud. A control system, irrespective of how well it is designed and operated, can only provide reasonable assurance, and cannot guarantee that it will succeed in its stated objectives.

Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of March 31, 2014, our disclosure controls and procedures were effective to provide reasonable assurance that the information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC’s rules and forms.

##### **Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. Our internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect our transactions and dispositions of our assets; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that our receipts and expenditures are being made only in accordance with authorizations of our management and our directors; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

There was no change in our internal control over financial reporting that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II—OTHER INFORMATION

### Item 1. Legal Proceedings.

We are routinely involved in a number of legal actions and proceedings, the outcome of which are uncertain. The legal proceedings could result in adverse judgments, settlements, fines, injunctions, restitutions or other relief that could require significant expenditures or have other effects on our business. In accordance with applicable accounting standards and guidance, we establish accruals for a legal proceeding only when we determine both that it is probable that a loss has been incurred and the amount of the loss is reasonably estimable. We accrue the amount that represents our best estimate of the probable loss; however, if we can only determine a range of estimated losses, we accrue an amount within the range that, in our judgment, reflects the most likely outcome, and if none of the estimates within the range is more likely, we accrue the minimum amount of the range.

In the course of our regular review of pending legal matters, we determine whether it is reasonably possible that a potential loss relating to a legal proceeding may have a material impact on our liquidity, results of operations or financial condition. If we determine such a loss is reasonably possible, we disclose information relating to any such potential loss, including an estimate or range of loss or a statement that such an estimate cannot be made. On a quarterly and annual basis, we review relevant information with respect to legal loss contingencies and update our accruals, disclosures and estimates of reasonably possible losses or range of losses based on such reviews. We are often unable to estimate the possible loss or range of loss until developments in such matters have provided sufficient information to support an assessment of the range of possible loss, such as quantification of a damage demand from plaintiffs, discovery from other parties and investigation of factual allegations, rulings by the court on motions or appeals, analysis by experts, and the progress of settlement negotiations. In addition, we generally make no disclosures for loss contingencies that are determined to be remote. For matters for which we disclose an estimated loss, the disclosed estimate reflects the reasonably possible loss or range of loss in excess of the amount accrued, if any.

Loss estimates are inherently subjective, based on currently available information, and are subject to management's judgment and various assumptions. Due to the inherently subjective nature of these estimates and the uncertainty and unpredictability surrounding the outcome of legal proceedings, actual results may differ materially from any amounts that have been accrued.

On August 1, 2011, Radian Guaranty filed a lawsuit against Quicken Loans Inc. ("Quicken") in the U.S. District Court for the Eastern District of Pennsylvania. On September 5, 2012, Radian Guaranty filed an amended complaint. Radian Guaranty's complaint, as amended, seeks a declaratory judgment that it properly rescinded mortgage insurance coverage under Radian Guaranty's master insurance policy and delegated underwriting endorsement for approximately 220 home mortgage loans originated by Quicken based upon deficiencies and improprieties in the underwriting process. The approximately 220 home mortgage loans relate to an aggregate RIF of approximately \$13 million. On October 25, 2012, Quicken answered Radian Guaranty's amended complaint and asserted counterclaims against Radian Guaranty for alleged breach of contract and bad faith. On November 19, 2012, Radian Guaranty moved to dismiss Quicken's counterclaims. On October 28, 2013, the court granted Radian Guaranty's motion to dismiss in part and denied it in part. The court ruled that Quicken could not pursue a tort theory of bad faith and that Quicken had not stated a basis to toll the statute of limitations for any claims arising after the lawsuit was filed. The court permitted Quicken's remaining claims to proceed at this stage. Discovery has commenced in this litigation. The parties have agreed to increase the population of loans that are at issue from 220 loans to approximately 507 loans relating to an aggregate RIF of approximately \$29 million. This litigation is in the early stages of the proceedings, and therefore, we are unable to estimate whether a loss is reasonably possible in this matter.



We have been named as a defendant in a number of putative class action lawsuits alleging, among other things, that our captive reinsurance agreements violate the Real Estate Settlement Procedures Act of 1974 (“RESPA”). On December 9, 2011, an action titled *Samp v. JPMorgan Chase Bank, N.A.* (the “Samp case”), was filed in the U.S. District Court for the Central District of California. The defendants are JPMorgan Chase Bank, N.A., its affiliates (collectively, “JPMorgan”), and several mortgage insurers, including Radian Guaranty. The plaintiffs purport to represent a class of borrowers whose loans allegedly were referred to mortgage insurers by JPMorgan in exchange for reinsurance agreements between the mortgage insurers and JPMorgan’s captive reinsurer. Plaintiffs assert violations of RESPA. On October 4, 2012, Radian Guaranty filed a motion to dismiss on a number of grounds, and on May 7, 2013, the court granted the motion and dismissed the plaintiffs’ claims with prejudice. The court ruled that the plaintiffs could not state a claim against Radian Guaranty because it did not insure their loans, and, in addition, ruled that their claims were barred by the statute of limitations. On June 5, 2013, plaintiffs appealed these rulings to the U.S. Court of Appeals for the Ninth Circuit. On November 9, 2013, plaintiffs voluntarily dismissed their appeal.

Each of the cases described below are putative class actions (with alleged facts substantially similar to the facts alleged in the Samp case discussed above) in which Radian Guaranty has been named as a defendant and has insured at least one loan of one of the plaintiffs:

- On December 30, 2011, a putative class action under RESPA titled *White v. PNC Financial Services Group* was filed in the U.S. District Court for the Eastern District of Pennsylvania. On September 29, 2012, plaintiffs filed an amended complaint. On November 26, 2012, Radian Guaranty filed a motion to dismiss the plaintiffs’ claims as barred by the statute of limitations. On June 20, 2013, the court granted Radian Guaranty’s motion and dismissed plaintiffs’ claims, but granted plaintiffs leave to file a second amended complaint. Plaintiffs filed their second amended complaint on July 5, 2013, reasserting a putative claim under RESPA on substantially the same allegations. Radian Guaranty filed a motion to dismiss plaintiffs’ second amended complaint on July 22, 2013.
- On January 13, 2012, a putative class action under RESPA titled *Menichino, et al. v. Citibank, N.A., et al.*, was filed in the U.S. District Court for the Western District of Pennsylvania. Radian Guaranty was not named as a defendant in the original complaint. On December 4, 2012, plaintiffs amended their complaint to add Radian Guaranty as an additional defendant. On February 4, 2013, Radian Guaranty filed a motion to dismiss the claims against it as barred by the statute of limitations. On July 19, 2013, the court granted Radian Guaranty’s motion and dismissed plaintiffs’ claims, but granted plaintiffs leave to file a second amended complaint. Plaintiffs filed their second amended complaint on August 16, 2013, reasserting a putative claim under RESPA on substantially the same allegations. Radian Guaranty filed a motion to dismiss plaintiffs’ second amended complaint on September 17, 2013. The court denied Radian Guaranty’s motion on February 4, 2014, without prejudice to Radian Guaranty’s ability to raise the statute of limitations bar on a motion for summary judgment. On March 26, 2014, the court stayed the *Menichino* case, pending the outcome of an appeal filed by plaintiffs in *Riddle v. Bank of America Corporation, et. al.* (another putative class action under RESPA in which Radian Guaranty is not a party) after the *Riddle* case was dismissed on summary judgment on November 18, 2013.

- On April 5, 2012, a putative class action under RESPA titled *Manners, et al. v. Fifth Third Bank, et al.* was filed in the U.S. District Court for the Western District of Pennsylvania. On November 28, 2012, Radian Guaranty moved to dismiss plaintiffs' claims as barred by the statute of limitations. On July 19, 2013, the court granted Radian Guaranty's motion and dismissed plaintiffs' claims, but granted plaintiffs leave to file a second amended complaint. Plaintiffs filed their second amended complaint on August 16, 2013, reasserting a putative claim under RESPA on substantially the same allegations. Radian Guaranty filed a motion to dismiss plaintiffs' second amended complaint on September 17, 2013. The court denied Radian Guaranty's motion on February 5, 2014, without prejudice to Radian Guaranty's ability to raise the statute of limitations bar on a motion for summary judgment. On March 26, 2014, the court stayed the *Manners* case, pending the outcome of an appeal filed by plaintiffs in *Riddle v. Bank of America Corporation, et. al.* (another putative class action under RESPA in which Radian Guaranty is not a party) after the *Riddle* case was dismissed on summary judgment on November 18, 2013.
- On June 28, 2012, a putative class action under RESPA titled *Cunningham, et al. v. M&T Bank Corporation, et al.* was filed in the U.S. District Court for the Middle District of Pennsylvania. On December 10, 2012, Radian Guaranty moved to dismiss plaintiffs' claims as barred by the statute of limitations, and on February 11, 2013, plaintiffs filed an opposition to the motion to dismiss. On October 30, 2013, the court denied that motion and ordered a brief period of discovery limited to the statute of limitations issue. On January 31, 2014, plaintiffs voluntarily dismissed Radian Guaranty from this lawsuit.

With respect to the ongoing putative class actions discussed above, Radian Guaranty believes that the claims are without merit and intends to vigorously defend itself against these claims. We are not able to estimate the reasonably possible loss or range of loss for these matters because the proceedings are in a very preliminary stage and there is uncertainty as to the likelihood of a class being certified or the ultimate size of a class.

In addition to the litigation discussed above, we are involved in litigation that has arisen in the normal course of our business. We are contesting the allegations in each such pending action and management believes, based on current knowledge and after consultation with counsel, that the outcome of such litigation will not have a material adverse effect on our consolidated financial condition. However, the outcome of litigation and other legal and regulatory matters is inherently uncertain, and it is possible that one or more of the matters currently pending or threatened could have an unanticipated adverse effect on our liquidity, financial condition or results of operations for any particular period.

In addition to the private lawsuits discussed above, we and other mortgage insurers have been subject to inquiries from the Minnesota Department of Commerce and the Office of the Inspector General of the U.S. Department of Housing and Urban Development ("HUD"), requesting information relating to captive reinsurance. We have cooperated with these requests for information. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") amended RESPA and transferred the authority to implement and enforce RESPA from HUD to the Consumer Financial Protection Bureau ("CFPB"). In January 2012, we and other mortgage insurers received a request for information and documents from the CFPB relating to captive reinsurance arrangements, and in June 2012, we and other mortgage insurers received a Civil Investigative Demand from the CFPB as part of its investigation to determine whether mortgage lenders and private mortgage insurance providers engaged in acts or practices in violation of the Dodd-Frank Act, RESPA and the Consumer Financial Protection Act. On April 4, 2013, we reached a settlement with the CFPB, which was approved by the U.S. District Court for the Southern District of Florida on April 9, 2013. The settlement concludes the investigation with respect to Radian Guaranty without the CFPB making any findings of wrongdoing. As part of the settlement, Radian Guaranty agreed not to enter into new captive reinsurance arrangements for a period of ten years and to pay a civil penalty of \$3.75 million. We have not entered into any new captive reinsurance arrangements since 2007. During the high-claim years that followed the most recent economic downturn, captive arrangements have proven to represent a critical component of our loss mitigation strategy, effectively serving as designed to protect our capital position during a period of stressed losses. As of March 31, 2014 we had received total cash reinsurance recoveries from these captive reinsurance arrangements of approximately \$800 million. In August 2013, Radian Guaranty and other mortgage insurers received a draft Consent Order from the Minnesota Department of Commerce, containing proposed conditions and unspecified penalties, to resolve its outstanding inquiries related to captive reinsurance arrangements involving mortgage insurance in Minnesota. We continue to cooperate with the Minnesota Department of Commerce and are engaged in active discussions with them with respect to their inquiries, including various alternatives for resolving this matter. We cannot predict the outcome of this matter or whether additional actions or proceedings may be brought against us.

## Item 1A. Risk Factors.

*Our insurance subsidiaries are subject to comprehensive state insurance regulations and other requirements, including capital adequacy measures, which if we fail to satisfy, could limit our ability to write new insurance and increase restrictions and requirements placed on our insurance subsidiaries.*

We and our insurance subsidiaries are subject to comprehensive, detailed regulation by the insurance departments in the states where our insurance subsidiaries are licensed to transact business. These regulations are principally designed for the protection of our policyholders rather than for the benefit of investors. Insurance laws vary from state to state, but generally grant broad supervisory powers to examine insurance companies and enforce rules or exercise discretion affecting almost every significant aspect of the insurance business, including the power to revoke or restrict an insurance company's ability to write new business.

The state insurance regulators impose various capital requirements on our insurance subsidiaries. These include risk-to-capital ratios, other risk-based capital measures and surplus requirements that potentially may limit the amount of insurance that our insurance subsidiaries may write. State insurance regulators also possess significant discretion with respect to our insurance subsidiaries. Our failure to maintain adequate levels of capital, among other things, could lead to intervention by the various insurance regulatory authorities, which could materially and adversely affect our business, business prospects and financial condition.

In addition, the GSEs have broad discretion with respect to Radian Guaranty and its ability to remain an eligible mortgage insurer under the GSEs' requirements. The GSEs are in the process of revising their eligibility requirements for mortgage insurers and we expect the GSEs to release the new requirements for public comment as early as the second quarter of 2014 and for these new requirements to become effective following an implementation period. For a discussion of potential changes to the GSEs' eligibility requirements for private mortgage insurers, see "*Radian Guaranty could lose its eligibility status with the GSEs, causing Freddie Mac and Fannie Mae to decide not to purchase mortgages insured by Radian Guaranty, which would significantly impair our mortgage insurance franchise.*"

Under state insurance regulations, Radian Guaranty is required to maintain minimum surplus levels and, in certain states, a minimum ratio of statutory capital relative to the level of net RIF, or "risk-to-capital." Sixteen states (the "RBC States") currently impose a statutory or regulatory risk-based capital requirement (the "Statutory RBC Requirement"). The most common Statutory RBC Requirement is that a mortgage insurer's risk-to-capital ratio may not exceed 25 to 1. In certain of the RBC States, there is a Statutory RBC Requirement that the mortgage insurer must maintain a minimum policyholder position, which is calculated based on both risk and surplus levels (the "MPP Requirement"). The statutory capital requirements for the non-RBC States are de minimis (ranging from \$1 million to \$5 million); however, the insurance laws of these states generally grant broad supervisory powers to state agencies or officials to enforce rules or exercise discretion affecting almost every significant aspect of insurance business, including the power to revoke or restrict an insurance company's ability to write new business. Unless an RBC State grants a waiver or other form of relief, if a mortgage insurer is not in compliance with the Statutory RBC Requirement of such state, it may be prohibited from writing new mortgage insurance business in that state. Radian Guaranty's domiciliary state, Pennsylvania, is not one of the RBC States. In 2013, and during the first quarter of 2014, the RBC States accounted for approximately 55.7% and 57.8%, respectively, of Radian Guaranty's total primary NIW.

As of March 31, 2014, Radian Guaranty's risk-to-capital ratio was 19.2 to 1 and Radian Guaranty was in compliance with all applicable Statutory RBC Requirements. Currently, we expect to maintain Radian Guaranty's risk-to-capital ratio at or below 20 to 1. However, we expect this target level to change upon the modification of GSE eligibility requirements or future changes in applicable regulatory requirements.

Absent new capital contributions or other capital relief, Radian Guaranty's risk-to-capital ratio generally increases as we increase our net RIF or as we incur operating losses. In 2014, our net RIF is expected to increase as we expect to continue to maintain a significant share of the private mortgage insurance market. With respect to incurred losses, the ultimate amount and timing of any future incurred losses will depend, in part, on general economic conditions and other factors, including the health of credit markets, home prices and unemployment rates, all of which are difficult to predict and beyond our control. Our mortgage insurance incurred losses are driven primarily by new mortgage insurance defaults and changes in the assumptions used to determine our loss reserves. Establishing loss reserves in our businesses requires significant judgment by management with respect to the likelihood, magnitude and timing of anticipated losses. If the actual losses we ultimately realize are in excess of the loss estimates we use in establishing loss reserves, we may be required to take unexpected charges to income, which could adversely affect Radian Guaranty's statutory capital position.

Radian Guaranty's capital position also is dependent on the performance of our financial guaranty portfolio. In 2008, we contributed our ownership interest in Radian Asset Assurance to Radian Guaranty. While this reorganization has provided Radian Guaranty with substantial regulatory capital and dividends, it also makes the capital adequacy of our mortgage insurance business dependent, to a significant degree, on the successful run-off of our financial guaranty business. In addition, any decrease in the amount of capital credit that Radian Guaranty otherwise receives with respect to its ownership of Radian Asset Assurance could have a negative impact on Radian Guaranty's capital adequacy for purposes of GSE eligibility. As of March 31, 2014, our mortgage insurance segment maintained claims paying resources of \$2.7 billion, which consists of contingency reserves, statutory policyholders' surplus, unearned premium reserves and loss reserves. If the performance of our financial guaranty portfolio deteriorates, including if we are required to establish (or increase) statutory reserves on defaulted obligations that we have insured, or if we make net commutation payments to terminate insured financial guaranty obligations in excess of the then established statutory reserves for such obligations, the statutory capital of Radian Guaranty also would be negatively impacted. See *"Deterioration in our financial guaranty portfolio could reduce Radian Asset Assurance's statutory surplus and negatively impact its ability to pay dividends to Radian Guaranty."*

We use reinsurance from affiliated companies to support Radian Guaranty's risk-to-capital ratio. Certain of these affiliated reinsurance companies currently are operating at relatively low capital levels and have required, and may in the future require, additional capital contributions from Radian Group. Radian Mortgage Insurance Inc. and Radian Insurance are each required to maintain a minimum statutory surplus of \$20 million to remain authorized reinsurers. Radian Guaranty Reinsurance Inc. ("RGRI"), which provides reinsurance to Radian Guaranty for coverage in excess of 25% of certain loans insured by Radian Guaranty, is a sister company of Radian Guaranty, and therefore, any contributions to this insurer would not be consolidated with Radian Guaranty's capital for purposes of calculating Radian Guaranty's risk-to-capital position. If we are limited in, or prohibited from, using reinsurance arrangements to reduce Radian Guaranty's risk, including as a result of any new eligibility requirements adopted by the GSEs, it would adversely affect Radian Guaranty's risk-to-capital position.

If Radian Guaranty is not in compliance with a state's applicable Statutory RBC Requirement, it may be prohibited from writing new business in that state until it is back in compliance or it receives a waiver of, or similar relief from, the requirement. In those states that do not have a Statutory RBC Requirement, it is not clear what actions the applicable state regulators would take if a mortgage insurer fails to meet the Statutory RBC Requirement established by another state. Accordingly, if Radian Guaranty were to fail to meet the Statutory RBC Requirement in one or more states, it could be required to suspend writing business in some or all of the states in which it does business. In addition, the GSEs and our mortgage lending customers may decide not to conduct new business with Radian Guaranty (or may reduce current business levels) or impose restrictions on Radian Guaranty while its capital position remained at such levels. The franchise value of our mortgage insurance business would likely be significantly diminished if we were prohibited from writing new business or restricted in the amount of new business we could write in one or more states.

Our existing capital resources may not be sufficient to successfully manage Radian Guaranty's capital position. As discussed above, the GSEs are in the process of proposing revised eligibility requirements that are expected to, among other things, contain new capital adequacy requirements for private mortgage insurers that are more onerous than the capital requirements currently in effect. See "*Radian Guaranty could lose its eligibility status with the GSEs, causing Freddie Mac and Fannie Mae to decide not to purchase mortgages insured by Radian Guaranty, which would significantly impair our mortgage insurance franchise.*" In addition, the NAIC is in the process of reviewing the minimum capital and surplus requirements for mortgage insurers and considering changes to the Model Act. While the outcome of this process is not known, it is possible that among other changes, the NAIC will recommend and adopt more stringent capital requirements that could increase the capital requirements for Radian Guaranty in states that adopt the new Model Act. Depending on the ultimate outcome of the NAIC proposals or the new GSE eligibility requirements, we may need to provide additional capital support to, or arrange additional capital relief for, Radian Guaranty, including potentially, entering into new reinsurance arrangements, making greater than anticipated capital contributions from our available holding company liquidity or seeking to raise funds in private or public capital transactions.

Depending on the extent of our future incurred losses along with the amount of new insurance that we write and other factors, the amount of capital contributions that may be required to maintain compliance with applicable regulatory and other requirements, including capital adequacy standards, could be significant and could exceed all of our remaining available capital. In the event we contribute a significant amount of Radian Group's available capital to Radian Guaranty, our financial flexibility would be significantly reduced, making it more difficult for Radian Group to meet its obligations in the future, including future principal payments on our outstanding debt. See "*Radian Group's sources of liquidity may be insufficient to fund its obligations.*"

***Radian Guaranty could lose its eligibility status with the GSEs, causing Freddie Mac and Fannie Mae to decide not to purchase mortgages insured by Radian Guaranty, which would significantly impair our mortgage insurance franchise.***

In order to be eligible to insure loans purchased by the GSEs, mortgage insurers must meet the GSE's eligibility requirements. The current GSE eligibility requirements, among other things, impose limitations on the type of risk that may be insured, standards for the diversification of risk, procedures for claims handling, standards for acceptable underwriting practices, standards for certain reinsurance cessions and financial and capital requirements. If we fail to satisfy one or more of these requirements, Freddie Mac and/or Fannie Mae could restrict Radian Guaranty from conducting certain types of business with them or take actions that may include not purchasing loans insured by Radian Guaranty.

In addition to these requirements, in order to maintain the highest level of eligibility with Freddie Mac and Fannie Mae, mortgage insurers historically were required to maintain an insurer financial strength rating of AA- or Aa3 from at least two of the three ratings agencies by which they were customarily rated. Both Freddie Mac and Fannie Mae have indicated that loss of mortgage insurer eligibility will no longer be automatic due to a failure to meet the financial strength rating requirements, and instead will be subject to review if and when the downgrade occurs. Because Radian Guaranty does not meet the financial strength rating requirements specified in the GSEs' eligibility guidelines, Radian Guaranty currently is operating as an eligible insurer under remediation plans with Freddie Mac and Fannie Mae that describe how we intend to achieve consistent levels of operating profitability and ultimately regain higher financial strength ratings for our mortgage insurers. We cannot be certain whether, or for how long, either of the GSEs will continue to allow Radian Guaranty to operate as an eligible insurer under our existing remediation plans.

The GSEs are in the process of revising their standard mortgage insurer eligibility requirements. We expect the revised eligibility requirements to be released in draft form for public comment as early as the second quarter of 2014 and for these requirements to become effective following an implementation period. Among other changes, the new GSE eligibility requirements are expected to contain new capital adequacy standards for private mortgage insurers that are more onerous than the capital requirements that are currently in effect, including potentially: (i) a risk-to-capital ratio below Radian Guaranty's 19.2 to 1 risk-to-capital ratio as of March 31, 2014; (ii) capital requirements based on a variety of risk characteristics and measures of credit quality; and (iii) a limitation on the amount of capital credit available for subsidiary capital (including Radian Guaranty's capital that is attributable to its ownership of Radian Asset Assurance, our financial guaranty subsidiary). The form of the new eligibility requirements and the timeframe for their implementation remain uncertain, and we cannot give any assurances as to their potential impact on us. If the new GSE eligibility requirements include more onerous capital requirements, including any one or more of the potential requirements referenced above, we may need to provide additional capital support to, or arrange additional capital relief for, Radian Guaranty, including potentially, entering into new reinsurance arrangements, increasing the amount of capital contributions from our available holding company funds or seeking to raise funds in private or public capital transactions. See "*Radian Group's sources of liquidity may be insufficient to fund its obligations.*"

Although we expect to be able to retain Radian Guaranty's eligibility status with the GSEs, we cannot be certain that this will occur. Loss of Radian Guaranty's eligibility status with the GSEs would likely have an immediate and material adverse impact on the franchise value of our mortgage insurance business and our future prospects and would negatively impact our results of operations and financial condition.

***Radian Group's sources of liquidity may be insufficient to fund its obligations.***

Radian Group serves as the holding company for our insurance subsidiaries and does not have any significant operations of its own. Radian Group's principal liquidity demands include funds for: (i) potential additional capital support for our mortgage insurance subsidiaries; (ii) the payment of dividends on our common stock; (iii) the payment of corporate expenses; (iv) interest payments on our outstanding long-term debt; (v) the repayment of our outstanding long-term debt, including \$54.5 million principal amount of outstanding debt due in June 2015, \$195.5 million principal amount of outstanding debt due in June 2017, \$450 million principal amount of convertible debt due in November 2017 and, at our option, any related conversion premium that we elect to settle in cash, and potentially \$400 million of convertible debt due in March 2019 for which the principal amount and any conversion premium may, at our option, be settled in cash; and (vi) potential payments to the U.S. Treasury resulting from the examination of our 2000 through 2007 consolidated federal income tax returns by the IRS. In addition, as discussed under "Recent Developments," on May 6, 2014, we announced an agreement to acquire Clayton Holdings LLC ("Clayton") for \$305 million. In connection with the acquisition, we plan to raise an aggregate amount to fund the purchase price and any related expenses of the transaction, which we anticipate seeking to finance through the issuance of debt and equity. We can provide no assurance that we will be successful in raising these funds on favorable terms or at all, in which case, we may be required to fund the acquisition with available liquidity, which would reduce the amounts available for payment of our expenses and for capital contributions to Radian Guaranty and our other mortgage insurance subsidiaries.

Radian Group currently has immediately available, either directly or through an unregulated subsidiary, unrestricted cash and liquid investments of approximately \$615 million. The \$615 million of available liquidity excludes certain additional cash and liquid investments that have been advanced from our subsidiaries for corporate expenses and interest payments. Substantially all of Radian Group's obligations to pay corporate expenses and interest payments on outstanding debt are reimbursed to Radian Group through the expense-sharing arrangements currently in place with its subsidiaries.

As of March 31, 2014, Radian Guaranty's risk-to-capital ratio was 19.2 to 1. Currently, we expect to maintain Radian Guaranty's risk-to-capital ratio at or below 20 to 1. However, we expect this target level to change upon the modification of GSE eligibility requirements or future regulatory changes, as discussed further below. We estimate that an immaterial amount of additional capital contributions from Radian Group to Radian Guaranty would be required during the next 12 months in order to maintain Radian Guaranty's risk-to-capital ratio at or below 20 to 1. A greater level of capital contributions could be required to maintain Radian Guaranty's risk-to-capital ratio at or below 20 to 1 if Radian Guaranty's incurred losses are higher than anticipated or if our net RIF ultimately exceeds our current projections. See "*Our insurance subsidiaries are subject to comprehensive regulations and other requirements, including capital adequacy measures, which if we fail to satisfy, could limit our ability to write new insurance and increase restrictions and requirements placed on our insurance subsidiaries.*"

Radian Group also could be required to provide further capital support to Radian Guaranty to satisfy new mortgage insurance eligibility standards currently being developed by the FHFA. The GSEs are in the process of revising their standard mortgage insurer eligibility requirements. We expect the revised eligibility requirements to be released for public comment as early as the second quarter of 2014 and for these requirements to become effective following an implementation period. The changes are expected to include certain changes that are more onerous than the current requirements, including potentially: (i) a risk-to-capital ratio below Radian Guaranty's 19.2 to 1 risk-to-capital ratio as of March 31, 2014; (ii) capital requirements based on a variety of risk characteristics and measures of credit quality; and (iii) a limitation on the amount of capital credit available for subsidiary capital (including Radian Guaranty's capital that is attributable to its ownership of Radian Asset Assurance). In addition, the NAIC is in the process of reviewing the minimum capital and surplus requirements for mortgage insurers and considering changes to these and other requirements in the Model Act. While the outcome of this process is not known, it is possible that the NAIC will recommend and adopt more stringent capital requirements that could increase the capital requirements for Radian Guaranty in states that adopt the new Model Act. If the new GSE eligibility requirements or the NAIC proposals include more onerous capital requirements, including any one or more of the potential requirements referenced above, we may need to provide additional capital support to, or arrange additional capital relief for, Radian Guaranty, including potentially, entering into new reinsurance arrangements, increasing the amount of capital contributions from our available holding company liquidity or seeking to raise funds in private or public capital transactions. For example, if Radian Guaranty is required to maintain a maximum risk-to-capital ratio of 18 to 1, absent any other form of risk-to-capital support, we estimate that we would be required to contribute approximately \$200 million to Radian Guaranty during the next 12 months, assuming for purposes of this example that there is no implementation period for these requirements. Although we can provide no assurances, we expect that the new eligibility requirements will include an implementation period. Because we expect that Radian Guaranty will generate capital internally in the future, the length of the implementation period could reduce that amount of additional capital support, if any, that we may need to provide to Radian Guaranty. See "*Radian Guaranty could lose its eligibility status with the GSEs, causing Freddie Mac and Fannie Mae to decide not to purchase mortgages insured by Radian Guaranty, which would significantly impair our mortgage insurance franchise.*"

Radian Group's U.S. consolidated federal income tax returns for tax years 2000 through 2007, which include the federal income tax returns of our wholly-owned subsidiary, RGRI, were examined by the IRS. We are currently contesting proposed adjustments resulting from the IRS examination of these tax years, which relate to the recognition of certain tax losses and deductions that were generated through our investment in a portfolio of non-economic Real Estate Mortgage Investment Conduits ("REMICs") residual interests currently held by RGRI. If these adjustments were sustained, RGRI would be required to pay additional income taxes of approximately \$128 million plus proposed penalties of approximately \$42 million. Additionally, we would incur interest expense on any sustained adjustments. Radian Group has agreed to indemnify RGRI for any tax payments ultimately due to the IRS for the proposed adjustments. This indemnification was made in lieu of an immediate capital contribution to RGRI that otherwise would have been required for RGRI to maintain its minimum statutory surplus requirements in light of remeasurement as of December 31, 2011 of uncertain tax positions related to the portfolio of REMIC residual interests.

Cash flows from our investment portfolio, dividends from Radian Guaranty and permitted payments to Radian Group under tax- and expense-sharing arrangements with our subsidiaries are Radian Group's principal sources of cash. In light of operating losses in Radian Guaranty, we do not anticipate that it will be permitted under applicable insurance laws to issue dividends to Radian Group for the foreseeable future. To the extent Radian Asset Assurance is able to declare dividends, these dividends will be paid to Radian Guaranty and not to Radian Group. The expense-sharing arrangements between Radian Group and our insurance subsidiaries, as amended, have been approved by applicable state insurance departments, but such approval may be revoked at any time.

In light of Radian Group's long- and short-term needs, it is possible that our liquidity demands could exceed currently available holding company funds. If this were to occur, we may need to increase our available liquidity by incurring additional debt, by issuing additional equity or by selling assets, any of which we may be unable to do on favorable terms, if at all.

***Deterioration in our financial guaranty portfolio could reduce Radian Asset Assurance's statutory surplus and negatively impact its ability to pay dividends to Radian Guaranty.***

The performance of our financial guaranty business may affect whether Radian Asset Assurance will be permitted to pay dividends to Radian Guaranty in the future as it has in past years, as well as the amount of any such dividends. At March 31, 2014, Radian Asset Assurance maintained claims paying resources of \$1.6 billion, including statutory surplus of approximately \$1.2 billion. Radian Asset Assurance paid dividends to Radian Guaranty in 2013 totaling \$36 million. We expect that in the third quarter of 2014 Radian Asset Assurance will have the capacity to pay an ordinary dividend of approximately \$32 million to Radian Guaranty.

The timing and amount of any future dividend payments will depend on the dividend capacity of our financial guaranty business, which is governed by New York insurance laws. Under New York insurance laws, Radian Asset Assurance may only pay dividends from statutory earned surplus and it can only pay such "ordinary dividends" without prior approval of the New York State Department of Financial Services ("NYSDFS") when the total of all other dividends declared or distributed by it during the preceding 12 months is the lesser of 10% of its statutory surplus to policyholders or 100% of statutory adjusted net investment income during such period. In addition, the NYSDFS, in its discretion, may approve a dividend distribution greater than would be permitted as an ordinary dividend (generally referred to as an "extraordinary dividend").

Since Radian Asset Assurance ceased writing new business in June 2008, Radian Asset Assurance has reduced its aggregate net par exposure by approximately 80% to \$22.7 billion as of March 31, 2014. This reduction included large declines in many of the riskier segments of Radian Asset Assurance's insured portfolio. In light of this risk reduction and the significant level of capital remaining at Radian Asset Assurance, Radian Asset Assurance filed a request with the NYSDFS seeking permission to pay an extraordinary dividend to Radian Guaranty. The NYSDFS currently is considering this request and there can be no assurance if and when such request will be granted in whole or in part, and if granted, that it will not be subject to material conditions.

If the performance of our financial guaranty portfolio deteriorates materially or the amount we pay to terminate any particular financial guaranty exposure is larger than the amount of the statutory reserves for such exposure, Radian Asset Assurance's statutory surplus may be reduced. If this were to occur, Radian Asset Assurance would likely have less capacity to pay dividends to Radian Guaranty and could be prohibited from paying dividends altogether, which could have a negative impact on Radian Guaranty's available liquidity.



## **Item 5. Other Information.**

### ***Agreement to Acquire Clayton Holdings LLC (“Clayton”)***

On May 6, 2014, Radian Group entered into a Unit Purchase Agreement (the “Purchase Agreement”) with Clayton, Paul T. Bossidy and Cobra Green LLC (“Cobra Green”), with a related guarantee of the obligations of Cobra Green by Greenfield Acquisition Partners V, L.P., an affiliate of Cobra Green. Under the Purchase Agreement, at closing Radian Group will pay aggregate cash consideration of \$305 million, which includes repayment of Clayton’s outstanding debt, to purchase all of the outstanding equity interests in Clayton, subject to customary purchase price adjustments. Radian Group anticipates funding the entire purchase price and related expenses through net proceeds received from the issuance of debt and equity.

Clayton is a leading provider of outsourced solutions to the mortgage industry, providing a full suite of outsourced services, information-based analytics and specialty consulting for buyers and sellers of, and investors in, mortgage-related loans and securities and other debt instruments.

We expect to complete the Clayton acquisition during the summer of 2014, subject to satisfaction of customary closing conditions, including expiration of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, receipt of certain state licensing approvals, accuracy of representations and warranties, compliance with covenants and agreements and continued employment by Clayton’s chief executive officer and its president. See Note 17 of Notes to Unaudited Condensed Consolidated Financial Statements and “Item 2. Management’s Discussion and Analysis—Overview—Recent Developments—*Purchase Agreement*” of this Quarterly Report on Form 10-Q for additional information.

The foregoing description of the Purchase Agreement does not purport to be complete and is qualified in its entirety by reference to the Purchase Agreement, which is filed as Exhibit 2 to this Quarterly Report on Form 10-Q and is incorporated herein by reference hereto.

### ***Segment Reporting (Unaudited)***

The information below is presented as an update to the information presented in Note 3 of our 2013 Form 10-K for the year ended December 31, 2013.

Effective January 1, 2014, our senior management, including our Chief Executive Officer (our chief operating decision maker), uses adjusted pretax operating income (loss) as our primary measure to facilitate evaluation of the fundamental financial performance of the Company’s business segments and to allocate resources to the segments. See Note 2 of Notes to Unaudited Condensed Consolidated Financial Statements—Segment Reporting for more information, including the definition of adjusted pretax operating income (loss).

As a result, the Company is providing additional information regarding 2013 segment profitability on a basis comparable to the measure being used in 2014. Such summarized financial information concerning our operating segments, as of and for the periods indicated, is as follows:

<b>(In thousands)</b>	<b>Three Months Ended</b>				<b>Year Ended</b>
	<b>March 31, 2013</b>	<b>June 30, 2013</b>	<b>September 30, 2013</b>	<b>December 31, 2013</b>	<b>December 31, 2013</b>
<b>Mortgage Insurance</b>					
Net premiums written - insurance	\$ 217,286	\$ 251,159	\$ 250,799	\$ 231,754	\$ 950,998
Net premiums earned - insurance	\$ 182,992	\$ 197,952	\$ 200,120	\$ 200,356	\$ 781,420
Net premiums earned on derivatives	—	—	—	—	—
Net investment income	15,102	15,266	14,868	16,379	61,615
Other income	1,712	2,159	1,250	903	6,024
Total revenues	199,806	215,377	216,238	217,638	849,059
Provision for losses	131,956	136,410	152,012	144,270	564,648
Estimated present value of net credit (recoveries) losses incurred	(299)	323	(74)	29	(21)
Change in reserve for premium deficiency	(629)	1,251	(2,325)	(198)	(1,901)
Policy acquisition costs	11,732	6,501	5,839	4,413	28,485
Other operating expenses	65,780	51,295	59,590	60,294	236,959
Interest expense	2,669	3,704	4,447	7,175	17,995
Total expenses	211,209	199,484	219,489	215,983	846,165
Equity in net income of affiliates	—	—	—	—	—
Adjusted pretax operating (loss) income	\$ (11,403)	\$ 15,893	\$ (3,251)	\$ 1,655	\$ 2,894

<b>(In thousands)</b>	<b>Three Months Ended</b>				<b>Year Ended</b>
	<b>March 31, 2013</b>	<b>June 30, 2013</b>	<b>September 30, 2013</b>	<b>December 31, 2013</b>	<b>December 31, 2013</b>
<b>Financial Guaranty</b>					
Net premiums written - insurance	\$ (10,101)	\$ 70	\$ 43	\$ (193)	\$ (10,181)
Net premiums earned - insurance	\$ 9,596	\$ 15,172	\$ 11,864	\$ 12,842	\$ 49,474
Net premiums earned on derivatives	4,992	4,857	4,170	3,879	17,898
Net investment income	11,771	12,349	11,864	10,489	46,473
Other income	59	75	64	13	211
Total revenues	26,418	32,453	27,962	27,223	114,056
Provision for losses	103	3,881	5,162	(6,660)	2,486
Estimated present value of net credit (recoveries) losses incurred	(2,845)	(618)	3,347	(393)	(509)
Change in reserve for premium deficiency	—	—	—	—	—
Policy acquisition costs	5,463	3,505	2,119	2,092	13,179
Other operating expenses	14,320	9,686	11,384	12,179	47,569
Interest expense	13,212	15,716	15,123	12,572	56,623
Total expenses	30,253	32,170	37,135	19,790	119,348
Equity in net income of affiliates	1	—	—	—	1
Adjusted pretax operating (loss) income	\$ (3,834)	\$ 283	\$ (9,173)	\$ 7,433	\$ (5,291)

The reconciliation of adjusted pretax operating (loss) income to consolidated pretax (loss) income and consolidated net (loss) income is as follows:

(In thousands)	Three Months Ended				Year Ended
	March 31, 2013	June 30, 2013	September 30, 2013	December 31, 2013	December 31, 2013
<b>Consolidated</b>					
Adjusted pretax operating (loss) income:					
Mortgage insurance	\$ (11,403)	\$ 15,893	\$ (3,251)	\$ 1,655	\$ 2,894
Financial guaranty	(3,834)	283	(9,173)	7,433	(5,291)
Total adjusted pretax operating (loss) income	(15,237)	16,176	(12,424)	9,088	(2,397)
Change in fair value of derivative instruments	(167,670)	86,535	10,778	38,586	(31,771)
Less: Estimated present value of net credit recoveries (losses) incurred	3,144	295	(3,273)	364	530
Less: Net premiums earned on derivatives	4,992	4,857	4,170	3,879	17,898
Change in fair value of derivative instruments expected to reverse over time	(175,806)	81,383	9,881	34,343	(50,199)
Net losses on investments	(5,505)	(130,254)	(7,132)	(6,829)	(149,720)
Net impairment losses recognized in earnings	—	—	—	(3)	(3)
Net (losses) gains on other financial instruments	(5,675)	1,188	902	(1,151)	(4,736)
Consolidated pretax (loss) income	(202,223)	(31,507)	(8,773)	35,448	(207,055)
Income tax (benefit) provision	(14,723)	1,665	3,909	(921)	(10,070)
Consolidated net (loss) income	\$ (187,500)	\$ (33,172)	\$ (12,682)	\$ 36,369	\$ (196,985)

**Item 6. Exhibits.**

<u>Exhibit No.</u>	<u>Exhibit Name</u>
*2	Unit Purchase Agreement, dated as of May 6, 2014, by and among (i) Radian Group Inc., (ii) Clayton Holdings LLC and (iii) Cobra Green LLC, a Delaware limited liability company, and Paul T. Bossidy.
*12	Statement of Ratio of Earnings to Fixed Charges
*31	Rule 13a - 14(a) Certifications
**32	Section 1350 Certifications
*101	Pursuant to Rule 405 of Regulation S-T, the following financial information from Radian Group Inc.'s Quarterly Report on Form 10-Q for the quarter ended March 31, 2014, is formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets as of March 31, 2014 and December 31, 2013, (ii) Condensed Consolidated Statements of Operations for the three months ended March 31, 2014 and 2013, (iii) Condensed Consolidated Statements of Comprehensive Income (Loss) for the three months ended March 31, 2014 and 2013, (iv) Condensed Consolidated Statements of Changes in Common Stockholders' Equity for the three months ended March 31, 2014 and 2013, (v) Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2014 and 2013, and (vi) the Notes to Unaudited Condensed Consolidated Financial Statements.

\* Filed herewith.

\*\* Furnished herewith.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**Radian Group Inc.**

May 6, 2014

/s/ C. ROBERT QUINT

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**C. Robert Quint**  
**Executive Vice President and Chief Financial Officer**

/s/ CATHERINE M. JACKSON

---

**Catherine M. Jackson**  
**Senior Vice President, Controller**

## EXHIBIT INDEX

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\* Filed herewith.

\*\* Furnished herewith.

**UNIT PURCHASE AGREEMENT**

**by and among**

**RADIAN GROUP INC.,**

**as the Purchaser,**

**CLAYTON HOLDINGS LLC,**

**AS THE COMPANY,**

**AND**

**the OTHER PARTIES HERETO**

**Dated as of May 6, 2014**

This Purchase Agreement has been attached as an exhibit to the accompanying Quarterly Report on Form 10-Q in order to provide investors and security holders with information regarding its terms. It is not intended to provide any other information about Radian or Clayton or any of their respective subsidiaries or affiliates. The covenants, representations and warranties contained in the Purchase Agreement were made only for purposes of that agreement and, in the case of representations and warranties, as of specific dates, may be subject to a contractual standard of materiality different from what a stockholder might view as material, may have been used for purposes of allocating risk between the respective parties rather than establishing matters as facts, may have been qualified by or subject to certain disclosures and exceptions not reflected in the Purchase Agreement and generally were for the benefit of the parties to that agreement. Investors should not rely on the representations, warranties or covenants or any description thereof as characterizations of the actual state of facts or condition of Radian, Clayton or any of their respective subsidiaries or affiliates. Moreover, information concerning the subject matter of the representations, warranties and covenants may change after the date of the Purchase Agreement, which subsequent information may or may not be fully reflected in the registrant's public disclosures.

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## UNIT PURCHASE AGREEMENT

**THIS UNIT PURCHASE AGREEMENT** (this “*Agreement*”) is entered into as of May 6, 2014, by and among (i) Radian Group Inc., a Delaware corporation (“*Purchaser*”), (ii) Clayton Holdings LLC, a Delaware limited liability company (the “*Company*”), (iii) Cobra Green LLC, a Delaware limited liability company (“*Cobra Green*”), and Paul T. Bossidy (each such party, a “*Unitholder*,” and collectively, the “*Unitholders*”), and Cobra Green, in its role as the Unitholder Representative (the “*Unitholder Representative*”). Each of Purchaser, the Company and each Unitholder is referred to herein as a “*Party*” and collectively as the “*Parties*.” Capitalized terms used herein and not otherwise defined have the meanings set forth in Schedule II hereto.

### RECITALS

**WHEREAS**, Cobra Green and Paul T. Bossidy (“*Bossidy*”) own, in the aggregate, one hundred percent (100%) of the outstanding Class A Units of the Company (the “*Class A Units*”);

**WHEREAS**, Bossidy also owns one hundred percent (100%) of the outstanding Class B Units of the Company (the “*Class B Units*”);

**WHEREAS**, each of Cobra Green and Bossidy desires to sell to Purchaser, and Purchaser desires to acquire from Cobra Green and Bossidy, all of the outstanding Class A Units held by such Unitholder, and Bossidy desires to sell to Purchaser, and Purchaser desires to acquire from Bossidy, all of the outstanding Class B Units held by him, in each case, subject to the terms and conditions set forth herein (collectively, the “*Transaction*”); and

**WHEREAS**, simultaneously with the execution of this Agreement, each of Paul Bossidy and Joseph D’Urso (the “*Executives*”) is entering into a letter agreement with Purchaser or one of its Subsidiaries setting forth the material terms of each such Executive’s employment with Purchaser or one of its Subsidiaries (each, a “*Letter Agreement*”), dated as of the date hereof, to be effective as of (and subject to the occurrence of) the Closing, and which shall supersede each Executive’s employment agreement with the Company.

### AGREEMENTS

**NOW, THEREFORE**, in consideration of the premises and the mutual covenants, representations and warranties contained herein and intending to be legally bound hereby, the Parties hereto hereby agree as follows:

## ARTICLE I

### SALE AND PURCHASE OF CLASS A UNITS AND CLASS B UNITS

1.1 ***Sale and Purchase of Class A Units and Class B Units.*** On the terms and subject to the conditions contained herein, in consideration for the aggregate purchase price specified in Section 1.2, on the Closing Date, (a) each Unitholder severally agrees to sell to Purchaser, and Purchaser agrees to purchase from each such Unitholder, the Class A Units shown opposite such Unitholder’s name on Schedule I, free and clear of all Liens, and (b) Bossidy agrees to sell to Purchaser, and Purchaser agrees to purchase from Bossidy, the Class B Units shown opposite Bossidy’s name on Schedule I

1.2 ***Purchase Price.*** On the terms and subject to the conditions set forth herein, in consideration of the Class A Units and Class B Units being sold hereunder, on the Closing Date, Purchaser shall pay to the Unitholders an aggregate amount equal to the sum of: (a) Three Hundred Five Million dollars (\$305,000,000) (the “*Enterprise Value*”); plus or minus, as applicable, (b) the Estimated Purchase Price Adjustment; minus (c) the Escrow Amount; minus (d) the Indebtedness; and minus (e) the Selling Expenses (the sum of the foregoing clauses (a)-(e), the “*Closing Cash Payment*”). At the Closing, Purchaser shall pay the Closing Cash Payment by (i) *first*, paying Bossidy an amount equal to the Aggregate Incentive Pool (such amount to be determined by the Board at least two (2) Business Days prior to the Closing) and (ii) *second*, paying each Unitholder an amount equal to its Pro Rata Share of the remainder of the Closing Cash Payment (after giving effect to the payment of the Aggregate Incentive Pool), in each case, by wire transfer of immediately available funds pursuant to instructions delivered and signed by the Unitholders, in a form reasonably acceptable to Purchaser (the “*Payment Instruction*”), at least two (2) Business Days prior to the Closing. The aggregate amount equal to the sum of: (A) the Closing Cash Payment; plus (B) the Escrow Amount to the extent disbursed to Unitholders pursuant to the Escrow Agreement; plus or minus, as applicable, (C) any adjustment made pursuant to Section 1.5; plus (D) the Indebtedness; and plus (E) the Selling Expenses shall be referred to herein as the “*Purchase Price*.”

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### 1.3 *Escrow Account.*

(a) At the Closing, Purchaser shall deliver to Wells Fargo Bank, National Association, as escrow agent (the “*Escrow Agent*”), under the escrow agreement dated the Closing Date, by and among Purchaser, the Unitholder Representative and the Escrow Agent, substantially in the form of Exhibit A hereto (the “*Escrow Agreement*”), an amount equal to Ten Million Eight Hundred Fifty Thousand dollars (\$10,850,000) (the “*Escrow Amount*”). The Escrow Amount shall be held in an escrow account (the “*Escrow Account*”) in accordance with the terms of the Escrow Agreement and released and paid on the first (1st) anniversary of the Closing (the “*Escrow Termination Date*”) in accordance with the terms of the Escrow Agreement. The Escrow Agreement will provide that the Escrow Amount will be used in connection with any amount payable to Purchaser pursuant to Section 1.5(e)(i) and to satisfy claims for Losses made by Purchaser required to be indemnified pursuant and subject to Article VIII hereof. All Parties hereto agree for all Tax purposes that: (i) the right of the Unitholders to the Escrow Amount shall be treated as deferred contingent purchase price eligible for installment treatment under Section 453 of the Code and any corresponding provision of foreign, state or local Law, as appropriate, (ii) Purchaser shall be treated as the owner of the Escrow Account, and all interest and earnings earned from the investment and reinvestment of the Escrow Amount, or any portion thereof, shall be allocable to Purchaser pursuant to Section 468B(g) of the Code and Proposed Treasury Regulation Section 1.468B-8), (iii) if and to the extent any amount of the Escrow Amount is actually distributed to the Unitholders, interest shall be imputed on such amount as required by Section 483 or 1274 of the Code, and (iv) in no event shall the aggregate amount payable to the Unitholders from the Escrow Account exceed Fifteen Million dollars (\$15,000,000). Clause (iv) of the preceding sentence is intended to ensure that the right of the Unitholders to the Escrow Amount and any interest and earnings earned thereon is not treated as a contingent payment without a stated maximum selling price under Section 453 of the Code and the Treasury Regulations promulgated thereunder. No Party shall take any action or filing position inconsistent with the foregoing.

(b) If at any time all or any portion of the Escrow Amount is released to the Unitholder Representative in accordance with the terms of the Escrow Agreement, then the Unitholder Representative shall (i) promptly re-determine (x) the Aggregate Incentive Pool, (y) the Incentive Payments and (z) the Special Bonus and (ii) subject to the immediately succeeding sentence, distribute such amount among the Unitholders, the Participants and Joseph D’Urso in accordance with the terms of the LLC Agreement, the Management Incentive Plan and the D’Urso Employment Agreement (as determined by the Unitholder Representative), each as in effect immediately prior to the Closing; *provided* that any such distributions to the Participants and Joseph D’Urso shall be made subject to Purchaser’s receipt of an acknowledgement, in a form reasonably satisfactory to Purchaser, from each Participant and Joseph D’Urso. The Unitholder Representative shall wire any amount payable to any Participant and/or Joseph D’Urso pursuant to the immediately preceding sentence to the Company and, promptly upon receipt thereof, the Company shall, and Purchaser shall cause the Company to, pay such amounts to the Participants and Joseph D’Urso through its payroll (subject to any required withholding) (it being expressly agreed that the Participants and Joseph D’Urso shall be third-party beneficiaries of this Section 1.3(b), each of whom may enforce the provisions of this Section 1.3(b)). Any amounts payable to the Unitholders pursuant to this Section 1.3(b) shall be paid by wire transfer of immediately available funds to the account(s) designated in writing by each such Unitholder.

1.4 *Estimated Purchase Price Adjustment.* No later than three (3) Business Days prior to the Closing Date, the Company shall deliver to Purchaser (i) an estimated unaudited consolidated balance sheet of the Company and its Subsidiaries as of 11:59 p.m. EST on the day immediately preceding the Closing Date, *provided* that such estimated unaudited consolidated balance sheet shall give effect to (x) the MSLS Distribution, regardless of whether the MSLS Distribution has been consummated prior to such time and (y) any cash distributions initiated by the Company pursuant to Section 6.6(ii) at or prior to the Closing, regardless of whether any cash so distributed has been debited from the Company’s bank accounts as of 11:59 p.m. EST on the day immediately preceding the Closing Date, and (ii) a statement (the “*Estimated Preliminary Statement*”), in each case prepared in good faith and in accordance with the Financial Statements, setting forth an estimate of the Closing Date Net Working Capital Amount (the “*Estimated Closing Date Net Working Capital Amount*”). If the Estimated Closing Date Net Working Capital Amount exceeds Seven Million Five Hundred Thousand dollars (\$7,500,000) (the “*Target Net Working Capital Amount*”), the Closing Cash Payment will be increased dollar-for-dollar by the amount of such excess and if the Estimated Closing Date Net Working Capital Amount is less than the Target Net Working Capital Amount, the Closing Cash Payment shall be reduced dollar-for-dollar by the amount of such shortfall, as provided for in Section 1.2. The amount by which the Estimated Closing Date Net Working Capital Amount exceeds or is less than, as applicable, the Target Net Working Capital Amount shall be referred to herein as the “*Estimated Purchase Price Adjustment.*”

### 1.5 *Purchase Price Adjustment.*

(a) Purchaser shall deliver, or cause to be delivered, to the Unitholder Representative, as soon as practicable, but in no event more than sixty (60) days after the Closing Date, (i) an unaudited consolidated balance sheet of the Company and its Subsidiaries as of 11:59 p.m. EST on the day immediately preceding the Closing Date (which shall give effect to (x) the MSLS Distribution, regardless of whether the MSLS Distribution has been consummated prior to such time and (y)

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any cash distributions initiated by the Company pursuant to Section 6.6(ii) at or prior to the Closing, regardless of whether any cash so distributed has been debited from the Company's bank accounts as of 11:59 p.m. EST on the day immediately preceding the Closing Date (the “**Closing Balance Sheet**”) and (ii) a preliminary statement (the “**Preliminary Statement**”) prepared in good faith and setting forth the calculation of the Closing Date Net Working Capital Amount as derived from the Closing Balance Sheet, in each case of clauses (i) and (ii), along with reasonable supporting detail to evidence the calculations of such amounts. The Closing Balance Sheet, the Closing Date Net Working Capital Amount and all of the calculations set forth therein shall be prepared in accordance with the Financial Statements.

(b) The Unitholder Representative shall have sixty (60) days to review the Preliminary Statement from the date of its receipt thereof (the “**Review Period**”). During the Review Period, the Unitholder Representative shall have reasonable access during normal business hours to the books and records, personnel and advisors of the Company and its Subsidiaries to the extent required in connection with such review. If the Unitholder Representative objects to any aspect of the Preliminary Statement, the Unitholder Representative must deliver a written notice of objection (the “**Objection Notice**”) to Purchaser on or prior to the expiration of the Review Period setting forth in reasonable detail the basis for any such objection. If the Unitholder Representative delivers an Objection Notice to Purchaser prior to the expiration of the Review Period as provided in this Section 1.5(b), Purchaser and the Unitholder Representative shall, for a period of thirty (30) days thereafter (the “**Resolution Period**”), attempt in good faith to resolve the matters contained therein, and any written resolution, signed by each of Purchaser and the Unitholder Representative, as to any such matter shall be final, binding, conclusive and non-appealable for all purposes hereunder. In the event the Unitholder Representative does not deliver an Objection Notice to Purchaser as provided in this Section 1.5(b) prior to the expiration of the Review Period, the Unitholders shall be deemed to have agreed to the Preliminary Statement in its entirety, which Preliminary Statement or undisputed portions thereof (as the case may be) shall be final, binding, conclusive and non-appealable for all purposes hereunder.

(c) If, at the conclusion of the Resolution Period, Purchaser and the Unitholder Representative have not reached an agreement with respect to all disputed matters contained in the Objection Notice, then within ten (10) Business Days thereafter, Purchaser and the Unitholder Representative shall submit for resolution those of such matters remaining in dispute to KPMG, or if such firm is unavailable or unwilling to so serve, to a mutually acceptable nationally recognized independent accounting or financial consulting firm (the “**Neutral Arbitrator**”). The Neutral Arbitrator shall act as an arbitrator to resolve (based solely on the written and oral presentations of Purchaser and the Unitholder Representative and not by independent review) only those matters submitted to it in accordance with the first sentence of this Section 1.5(c). Purchaser and the Unitholder Representative shall direct the Neutral Arbitrator to render a resolution of all such disputed matters within thirty (30) days after its engagement or such other period agreed upon in writing by Purchaser and the Unitholder Representative. The resolution of the Neutral Arbitrator shall be set forth in a written statement delivered to each of the Parties and shall be final, binding, conclusive and non-appealable for all purposes hereunder. The Preliminary Statement, once modified and/or agreed to in accordance with Section 1.5(b) or this Section 1.5(c), shall become the “**Final Statement**.”

(d) All fees and expenses relating to the work performed by the Neutral Arbitrator shall be allocated equally between the Unitholders (based on their respective Pro Rata Shares on a several and not joint basis), on the one hand, and Purchaser, on the other hand, with any such fees and expenses due from the Unitholders to be paid out of the Escrow Amount. Except as provided in the preceding sentence, all other costs and expenses incurred by the Parties in connection with resolving any dispute hereunder before the Neutral Arbitrator shall be borne by the Party incurring such cost and expense.

(e) Amounts payable pursuant to the determination of the Closing Date Net Working Capital Amount on the Final Statement will be paid and/or disbursed as follows:

(i) If the Closing Date Net Working Capital Amount as stated on the Final Statement is less than the Estimated Closing Date Net Working Capital Amount, then the Unitholder Representative and Purchaser shall promptly execute and deliver a written instruction to the Escrow Agent to effectuate disbursement of the amount of any such shortfall between the Estimated Closing Date Net Working Capital Amount and the Closing Date Net Working Capital Amount from the Escrow Amount to Purchaser in accordance with the terms of the Escrow Agreement.

(ii) If the Closing Date Net Working Capital Amount as stated on the Final Statement is greater than the Estimated Closing Date Net Working Capital Amount, then, within three (3) Business Days after the date on which the Preliminary Statement becomes the Final Statement, the Unitholder Representative shall (A) promptly re-determine (x) the Aggregate Incentive Pool, (y) the Incentive Payments and (z) the Special Bonus and (B) subject to the immediately succeeding sentence, distribute such excess amount among the Unitholders, the Participants and Joseph D’Urso in accordance with the terms of the LLC Agreement, the Management Incentive Plan and the D’Urso Employment Agreement (as determined by the Unitholder Representative), each as in effect immediately prior to the Closing; *provided* that any such distributions to the Participants and Joseph D’Urso shall be made subject to Purchaser’s receipt of an acknowledgement, in a form reasonably satisfactory to Purchaser, from each Participant and Joseph D’Urso. The Unitholder Representative shall wire any amount

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payable to any Participant and/or Joseph D'Urso pursuant to the immediately preceding sentence to the Company and, promptly upon receipt thereof, the Company shall, and Purchaser shall cause the Company to, pay such amounts to the Participants and Joseph D'Urso through its payroll (subject to any required withholding) (it being expressly agreed that the Participants and Joseph D'Urso shall be third-party beneficiaries of this Section 1.5(e)(ii), each of whom may enforce the provisions of this Section 1.5(e)(ii)). Any amounts payable to the Unitholders pursuant to this Section 1.5(e)(ii) shall be paid by wire transfer of immediately available funds to the account(s) designated in writing by each such Unitholder.

#### 1.6 **Tax Treatment.**

(a) The Parties acknowledge that the transactions effected pursuant to this Agreement are intended to be treated for federal income tax purposes and any relevant state or local income tax purposes as follows, consistent with the principles set forth in Situation 2 of Revenue Ruling 99-6, 1999-1 CB 432 (Jan. 15, 1999):

(i) the Company shall be treated as terminating pursuant to Section 708(b)(1)(A) of the Code;

(ii) with respect to the Unitholders, the sale and purchase of the Class A Units and the Class B Units shall be treated as a sale of the Class A Units and Class B Units to Purchaser, with gain or loss reported by the Unitholders in accordance with Section 741 of the Code; and

(iii) with respect to Purchaser, the sale and purchase of the Class A Units and Class B Units shall be treated as the Company making a liquidating distribution of all of its assets and all of its liabilities to the Unitholders in exchange for the Class A Units and Class B Units and, immediately following such liquidating distribution, Purchaser acquiring, by purchase, all of the Company's assets and liabilities from the Unitholders.

(b) Within ninety (90) days following the completion of the Final Statement, Purchaser shall prepare and deliver to the Unitholder Representative a proposed allocation of the Purchase Price and any additional amounts treated as consideration for applicable Tax purposes (the "**Total Consideration**") among the assets of the Company, which allocation shall be reasonable and in accordance with the principles of Section 1060 of the Code and the Treasury Regulations promulgated thereunder (the "**Proposed Allocation**"). Purchaser and the Unitholder Representative shall endeavor in good faith to agree, within sixty (60) days after the delivery of the Proposed Allocation, on an allocation of the Total Consideration among the assets of the Company (the "**Allocation**"). If Purchaser and the Unitholder Representative have agreed on an Allocation by such date, Purchaser and the Unitholder Representative shall (except as may be required by a "determination" within the meaning of Section 1313(a) of the Code or any similar state, local or foreign Tax law) (i) report the allocation of the Total Consideration among the assets of the Company in accordance with such Allocation and (ii) act in accordance with such Allocation (x) in the preparation and filing of all Tax Returns and (y) in the course of any tax proceeding. Purchaser and the Unitholder Representative shall promptly inform one another of any challenge by any Taxing Authority of which it becomes aware to such Allocation and agree to consult and keep one another informed with respect to the status of, and any discussion, proposal or submission with respect to, such challenge. If Purchaser and the Unitholder Representative have not agreed on an Allocation by such date, Purchaser and the Unitholder Representative shall endeavor in good faith to resolve such disagreement. If Purchaser and the Unitholder Representative are unable to resolve such disagreement within fifteen (15) days, each of Purchaser and the Unitholder Representative shall use its own allocation. Any adjustments made to the Purchase Price shall be allocated among the assets of the Company in the same manner as set forth in this Section 1.6(b).

(c) Each Party agrees that, for all Tax purposes, the transactions contemplated by this Agreement will be reported in a manner that is consistent with this Section 1.6, and none of them (nor any of their respective Affiliates) will take any Tax position inconsistent therewith on any Tax Return or otherwise unless otherwise required pursuant to a "determination" within the meaning of Section 1313(a) of the Code.

## ARTICLE II

### CLOSING AND TERMINATION

2.1 **Closing; Closing Date.** Subject to the terms and conditions of this Agreement, the closing of the Transaction (the "**Closing**") shall take place at 10:00 a.m., Boston time, at the offices of Goodwin Procter LLP, 53 State Street, Boston, MA 02109, no later than two (2) Business Days following the satisfaction or waiver of all conditions precedent specified under Article VII hereof (except for those conditions which by their terms are to be satisfied at Closing but subject to the satisfaction or waiver of such conditions), or on such other date, place and time as Purchaser and the Unitholder Representative may agree in writing (the "**Closing Date**").

#### 2.2 **Closing Deliveries.** .

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(a) At Closing, the Company shall deliver or cause to be delivered to Purchaser:

(i) an officer's certificate, dated as of the Closing Date, duly executed by an authorized officer of the Company, relating to the satisfaction of the Closing conditions set forth in Section 7.2(a) and Section 7.2(b);

(ii) a good standing certificate for the Company from the Secretary of State of the State of Delaware, dated as of a date within five (5) Business Days of the Closing Date;

(iii) written resignations of each manager of the Company and its Subsidiaries requested by Purchaser; and

(iv) such other documents and instruments as may be reasonably required by Purchaser to consummate the transactions contemplated by this Agreement.

(b) At Closing, each Unitholder or the Unitholder Representative, as the case may be, shall deliver or cause to be delivered to Purchaser:

(i) duly executed unit powers in proper form for each Class A Unit and each Class B Unit owned by such Party effectuating the assignment of such units to Purchaser;

(ii) the Escrow Agreement, duly executed by a duly authorized representative of the Unitholder Representative;

(iii) (x) a duly executed statement, substantially in the form of the sample statement set forth in Treasury Regulation Section 1.1445-2(b)(2)(iv)(A) or (B) (as applicable), to the effect that such Unitholder is not a "foreign person" within the meaning of Section 1445 of the Code and the Treasury Regulations thereunder and (y) a duly completed and executed IRS Form W-9; and

(iv) such other documents and instruments as may be reasonably required by Purchaser to consummate the transactions contemplated by this Agreement.

(c) At Closing, Purchaser shall deliver (or cause to be delivered) or shall pay (or cause to be paid) by wire transfer of immediately available funds pursuant to written instructions delivered to Purchaser prior to the Closing, as the case may be:

(i) to each Unitholder, such Unitholder's allocable share of the Closing Cash Payment, as determined pursuant to Section 1.2;

(ii) to the Escrow Agent, the Escrow Amount;

(iii) to each Person owed Indebtedness (other than (A) Indebtedness under the Clayton Credit Agreement if Purchaser elects (and the lender consents) to keep such Indebtedness outstanding immediately following the Closing, (B) the D'Urso Employment Agreement and (C) the Management Incentive Plan), cash in an amount equal to the Indebtedness owed to such Person (other than Indebtedness attributable to lease obligations properly capitalized under GAAP (if any)) as specified in a payoff letter received from such Person or Persons;

(iv) subject to Purchaser's receipt of an acknowledgement, in a form reasonably satisfactory to Purchaser, from each Participant and Joseph D'Urso, to the Company, cash in an amount equal to the Indebtedness owed to the Participants and Joseph D'Urso pursuant to the Management Incentive Plan and the D'Urso Employment Agreement, which such amount the Company shall promptly thereafter pay to the Participants and Joseph D'Urso through its payroll (subject to any required withholding);

(v) to each Person or Persons owed any Selling Expenses, cash in an amount equal to the Selling Expenses owed to such Person or Persons as directed by the Unitholder Representative;

(vi) to the Unitholder Representative, an officer's certificate, dated as of the Closing Date, duly executed by an authorized officer of Purchaser, relating to the satisfaction of the Closing conditions set forth in Section 7.3(a) and Section 7.3(b);

(vii) to the Unitholder Representative, the Escrow Agreement, duly executed by a duly authorized officer of Purchaser; and

(viii) to the Unitholder Representative or the Company, as the case may be, such other

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documents and instruments as may be reasonably required by the Unitholder Representative or the Company to consummate the transactions contemplated by this Agreement.

**2.3 Termination of the Agreement.** This Agreement may be terminated prior to the Closing as follows:

(a) at the election of the Unitholder Representative or Purchaser on or after the close of business on September 6, 2014 (the “**Termination Date**”), if the Closing shall not have occurred by the close of business on such date; *provided, however*, that the terminating Party is not in breach in any material respect of any of its obligations hereunder or the cause of the failure of the Closing to occur on or before the Termination Date; or

(b) by mutual written consent of the Unitholder Representative and Purchaser; or

(c) by either Purchaser or the Unitholder Representative if (1) a Governmental Entity shall have (i) issued a non-appealable final judgment, order, injunction, decree or ruling (“**Order**”) or taken any other action; or (ii) enacted, enforced or deemed applicable to the Transaction a Law in final form, in each case having the effect of permanently restraining, enjoining, prohibiting or making illegal the consummation of the Transaction ( *provided* that the Party seeking to terminate pursuant to this Section 2.3(c) shall have used commercially reasonable efforts to have any such Order or other action vacated or lifted); or (2) if any approval required to be obtained pursuant to Section 7.1(a) has been denied by the relevant Governmental Entity and such denial has become final and nonappealable; or

(d) by Purchaser, (i) upon a breach of any representation, warranty, covenant or agreement of the Company or the Unitholders set forth in this Agreement such that, individually or together with all such other then uncured breaches by the Company or the Unitholders, the conditions set forth in Section 7.2(a) or Section 7.2(b) would not be satisfied (a “**Unitholder Terminating Breach**”); *provided* that, if such Unitholder Terminating Breach is curable prior to the expiration of thirty (30) days from notice to the Unitholder Representative of its occurrence through the exercise of commercially reasonable efforts, and for so long as the Company or the applicable Unitholder continues to exercise such commercially reasonable efforts, Purchaser may not terminate this Agreement under this Section 2.3(d) until the expiration of such thirty (30) day period without such Unitholder Terminating Breach having been cured (but in no event shall the preceding proviso be deemed to extend the date set forth in Section 2.3(a)); or (ii) if satisfaction of any of the conditions set forth in Section 7.2 is or becomes impossible (other than through the failure of Purchaser to comply with its obligations under this Agreement); *provided, further*, that Purchaser shall not be entitled to terminate this Agreement pursuant to this clause Section 2.3(d) at any time during which Purchaser would be unable to satisfy the conditions in Section 7.3(a) or Section 7.3(b) hereof due to a breach of this Agreement by Purchaser; or

(e) by the Unitholder Representative, (i) upon a breach of any representation, warranty, covenant or agreement of Purchaser set forth in this Agreement such that, individually or together with all such other then uncured breaches by Purchaser, the conditions set forth in Section 7.3(a) or Section 7.3(b) would not be satisfied (an “**Purchaser Terminating Breach**”); *provided* that, if such Purchaser Terminating Breach is curable prior to the expiration of thirty (30) days from notice to Purchaser of its occurrence through the exercise of Purchaser’s commercially reasonable efforts, and for so long as Purchaser continues to exercise such commercially reasonable efforts, the Unitholder Representative may not terminate this Agreement under this Section 2.3(e) until the expiration of such thirty (30) day period without such Purchaser Terminating Breach having been cured (but in no event shall the preceding proviso be deemed to extend the date set forth in Section 2.3(a)); or (ii) if satisfaction of any of the conditions set forth in Section 7.3 is or becomes impossible (other than through the failure of the Company or any Unitholder to comply with its obligations under this Agreement); *provided, further* that the Unitholder Representative shall not be entitled to terminate this Agreement pursuant to this Section 2.3(e) at any time during which any Unitholder or the Company would be unable to satisfy the conditions in Section 7.2(a) or Section 7.2(b) hereof due to a breach of this Agreement by any Unitholder or the Company.

**2.4 Procedure Upon Termination.** In the event of termination of this Agreement by the Unitholder Representative or Purchaser, or both, pursuant to Section 2.3 hereof, written notice thereof shall forthwith be given to the other Party or Parties, and this Agreement shall terminate, and the Transaction shall be abandoned, without further action by any Party.

**2.5 Effect of Termination.** In the event that this Agreement is validly terminated in accordance with Section 2.3 and Section 2.4, then, subject to the provisions of this Section 2.5, the Company, the Unitholders, the Unitholder Representative and Purchaser shall be relieved of their respective duties and obligations arising under this Agreement after the date of such termination, and such termination shall be without liability to the Company, the Unitholders, the Unitholder Representative or Purchaser; *provided, however*, that no such termination shall relieve any Party hereto from liability for any willful and material breach of this Agreement by such Party prior to the date of termination; *provided, further*, that the obligations of the Parties set forth in this Section 2.5 and in Article IX hereof shall survive any such termination and shall be enforceable hereunder.

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## ARTICLE III

### REPRESENTATIONS AND WARRANTIES OF THE COMPANY

Subject to the exceptions disclosed in the disclosure schedule delivered by the Company to Purchaser and attached hereto as Schedule III (the “*Disclosure Schedule*”), the Company represents and warrants to Purchaser as follows, in each case as of the date hereof and as of the Closing Date as though made at and as of the Closing, unless otherwise specifically set forth herein:

#### 3.1 *Status, Authority, Conflicts.*

(a) The Company is a limited liability company duly organized, validly existing and in good standing under the laws of the State of Delaware, has all necessary limited liability company power and authority to carry on its business as now conducted and to own or lease and operate its properties and assets, and is duly qualified to do business as a foreign entity under the laws of each jurisdiction where such qualification is necessary, except where the failure to be so qualified would not reasonably be expected to have a Material Adverse Effect. The Company has provided true and complete copies of the Governing Documents of the Company, as in effect as of the date of this Agreement, to Purchaser prior to the date hereof.

(b) The Company has all necessary limited liability company power and authority to enter into the Transaction Documents to which it is a party and to carry out its obligations under such Transaction Documents. The execution, delivery and performance of the Transaction Documents to which the Company is a party and the consummation of the Transaction have been duly and validly authorized by the Company and no other proceedings on the part of the Company are necessary to authorize the Transaction or the Transaction Documents to which the Company is a party. This Agreement has been duly and validly executed and delivered by the Company, and assuming the due execution and delivery by each of the other Parties, constitutes the valid and binding agreement of the Company enforceable against the Company in accordance with the terms and conditions of this Agreement, subject to applicable bankruptcy, insolvency, reorganization, moratorium, liquidation, fraudulent conveyance, and other similar Laws and principles of equity affecting creditors' rights and remedies generally (the “*General Enforceability Exceptions*”).

(c) Except as set forth in Schedule 3.1(c), the execution and delivery of this Agreement by the Company and the other Transaction Documents to which the Company is a party and the consummation and performance by the Company of its obligations hereunder will not (i) result in a violation or breach of any provision of the Governing Documents of the Company; (ii) result in a violation or breach of any provision of any Law or Order applicable to the Company or any of its Subsidiaries; or (iii) (A) require notice to or the Consent of any Person under; (B) conflict with, result in a violation or breach of, constitute a default under (or an event which, with notice or lapse of time, or both, would constitute a default under); (C) result in the termination of, a right of termination under or acceleration of, payment conditioned upon a change of control of the Company or approval or consummation of the transactions contemplated by this Agreement under; or (D) result in the creation of any Lien upon any of the properties or assets of the Company or any of its Subsidiaries under; in each of clauses (iii)(A)-(D), any Material Contract; except, in the cases of clauses (ii) and (iii), where the violation, breach, conflict, default, termination, right of termination, acceleration, payment, Lien or failure to give notice would not reasonably be expected to be material to the Company or any of its Subsidiaries. No consent, approval, non-objection, Permit, Order, declaration or filing with, or notice to, any Governmental Entity is required by or with respect to the Company or any of its Subsidiaries in connection with the execution and delivery of this Agreement and the consummation of the Transaction, except as would not, individually or in the aggregate, be material to the Company or any of its Subsidiaries, and except for such filings as may be required under the HSR Act and as set forth in Schedule 3.1(c).

3.2 *Capitalization of the Company.* The Class A Units and the Class B Units listed on Schedule I are the only outstanding equity interests in the Company and are held of record, free and clear of all Liens, by the Unitholders in the individual amounts listed on Schedule I. Such equity interests are duly authorized and validly issued and have been offered, issued, sold, and delivered in compliance with applicable securities Laws. Except for the equity interests of the Company owned by Cobra Green and Bossidy set forth on Schedule I, there are not issued or outstanding (a) any other equity interests of the Company, (b) any options, warrants, or other rights to purchase from the Company any other equity interests of the Company, (c) any securities convertible into or exchangeable for equity interests of the Company, or (d) any other commitments of any kind for the issuance of options, warrants, or other securities of the Company. Except as set forth in the Governing Documents of the Company, there are no preemptive rights with respect to the issuance or sale of any equity interests of the Company and no commitments or understandings of any kind obligating the Company to issue, transfer, sell, purchase, redeem or otherwise acquire, or to register under applicable securities Laws, any such equity interests. There are no restrictions on the voting or transfer of the Company's equity interests other than those arising from federal and state securities Laws or arising from the Transaction Documents or arising from the Governing Documents of the Company.

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### 3.3 *Subsidiaries.*

(a) All of the outstanding equity interests in the Subsidiaries (i) have been duly authorized and validly issued and (where applicable) are fully paid and non-assessable and (ii) are free and clear of any and all Liens other than Permitted Liens. All of the outstanding equity interests of each of the Subsidiaries are beneficially owned, directly or indirectly, by the Company. There are not outstanding, (x) any options, warrants, or other rights to purchase from any Subsidiary any equity interests of any Subsidiary, (y) any securities convertible into or exchangeable for equity interests of any Subsidiary, or (z) any other commitments of any kind for the issuance of equity interests or options, warrants, or other securities of any Subsidiary. There are no preemptive rights with respect to the issuance or sale of any equity interests of any Subsidiary or any commitments or understandings of any kind obligating any Subsidiary to issue, transfer, sell, purchase, redeem or otherwise acquire, or to register under applicable securities Laws, any such equity interests. Each Subsidiary is a duly organized and validly existing corporation, partnership or limited liability company under the Laws of its jurisdiction of organization, has all necessary corporate, limited liability company or equivalent power and authority to carry on its business as now conducted and to own or lease and operate its properties and assets, and is duly qualified to do business as a foreign entity and is in good standing under the Laws of each jurisdiction where such qualification is necessary, except where the failure to be so qualified would not reasonably be expected to have a Material Adverse Effect. The Company has provided true and complete copies of the Governing Documents of each Subsidiary, as in effect as of the date of this Agreement, to Purchaser prior to the date hereof.

(b) Schedule 3.3(b) sets forth a true and complete list of each Subsidiary and such Subsidiary's jurisdiction of incorporation or organization, the names of such Subsidiary's beneficial owners, and the number of outstanding equity interests held by such Subsidiary's beneficial owners. Except for the Subsidiaries, the Company does not own any equity interest in, or any interest convertible into, or exercisable or exchangeable for any equity interest in, any other Person.

### 3.4 *Financial Information.*

(a) Schedule 3.4(a) contains the audited consolidated balance sheets of the Company and its Subsidiaries for the fiscal years ended December 31, 2012 and December 31, 2013 (the audited consolidated balance sheet for the fiscal year ended December 31, 2013, the "**Balance Sheet**") and the related audited consolidated statements of operations, changes in members' equity and cash flows for the fiscal years then ended (collectively, the "**Financial Statements**"). The Financial Statements have been prepared in accordance with GAAP and present fairly, in all material respects, the financial condition, results of operations, changes in members' equity and cash flows of the Company and its Subsidiaries, as of the date thereof and for the periods covered thereby. The Financial Statements have been prepared from, and are in accordance with, the books and records of the Company and its Subsidiaries.

(b) The Company maintains a system of internal accounting controls sufficient to comply with all legal and accounting requirements applicable to the business of the Company and its Subsidiaries. The Company has not received notice of any claim, investigation, examination or proceeding alleging that the Company has engaged in questionable accounting or auditing practices. The books and records kept by the Company and its Subsidiaries are in all material respects complete and accurate and have been maintained in the Ordinary Course of Business and in accordance with applicable Laws and accounting requirements.

(c) Neither the Company nor any of its Subsidiaries is a party to, or has any commitment to become a party to, any joint venture, off-balance sheet partnership or any similar Contract or arrangement, where the result, purpose or intended effect of such Contract or arrangement is to avoid disclosure of any material transaction involving, or material liabilities of, the Company or any of its Subsidiaries in the Financial Statements.

(d) Except for (i) those liabilities that are reflected or reserved against in the Balance Sheet and (ii) those liabilities incurred since December 31, 2013 in the Ordinary Course of Business, neither the Company nor any of its Subsidiaries has any liability of any nature whatsoever (whether absolute, accrued, contingent or otherwise and whether due or to become due).

3.5 *Absence of Certain Changes.* Except as set forth in Schedule 3.5, since December 31, 2013, (i) there has been no Material Adverse Effect or any event, condition, fact, change, effect or development, individually or in the aggregate, that is reasonably likely to have a Material Adverse Effect, (ii) the Company and its Subsidiaries have conducted their respective businesses in the Ordinary Course of Business in all material respects and (iii) neither the Company nor any of its Subsidiaries has:

(a) acquired or disposed of any assets or properties in any transaction with any Affiliate of the Company, or disposed of, transferred, mortgaged, encumbered or leased any material assets or properties in any transaction with any other Person;

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(b) adopted any amendment of the Governing Documents of the Company or any of its Subsidiaries or taken any action with respect to any reorganization, liquidation or dissolution;

(c) (i) granted to any salaried employee or any class of other employees (x) any increase in base compensation or bonus opportunity, except to the extent granted prior to the date hereof in the Ordinary Course of Business in accordance with existing personnel policies or (y) any severance or termination pay, except, in each case, as required under any Benefit Plan in effect on the date hereof or by applicable Law, (ii) entered into any employment agreement with any employee; (iii) entered into, adopted, or amended, any Benefit Plan, or any plan that would have constituted a Benefit Plan if in effect as of the date hereof; (iv) granted or accelerated the vesting of any equity-based awards for the benefit of any current or former employee, officer, director or consultant; or (v) provided any funding for any rabbi trust or similar arrangement;

(d) suffered any strike or other labor trouble with employees or been the subject of any effort to reorganize the Company's or any of its Subsidiaries' workforce, or any part thereof, into a bargaining unit or entered into any new, or amended any existing, collective bargaining agreement or similar agreement with respect to the Company or its Subsidiaries;

(e) incurred, assumed or guaranteed any Indebtedness other than in an aggregate amount not exceeding \$150,000 incurred in the Ordinary Course of Business;

(f) entered into, amended, changed, or terminated, or suffered any amendment, change, or termination of, any Material Contract;

(g) canceled or compromised any material claim or waived or released any material right or instituted, settled, or agreed to settle any Legal Proceeding; or consented to the issuance of any Order restricting or otherwise affecting its business or operations;

(h) (i) adjusted, split, combined or reclassified any equity interests, (ii) set any record or payment dates for the payment of any dividends or distributions on any equity interest or made, declared or paid any dividend or distribution on any equity interest (except for dividends paid in the Ordinary Course of Business by any of the Subsidiaries of the Company to the Company or any other Subsidiary of the Company), (iii) redeemed, purchased or otherwise acquired any equity interests, securities convertible into its equity interests or any rights, warrants, calls, subscriptions or options to acquire its equity interests, (iv) issued or authorized the issuance of any of its equity interests, securities convertible into its equity interests or any rights, warrants, calls, subscriptions or options to acquire its equity interests (including any equity-based compensation), (v) sold, leased, transferred, mortgaged, encumbered or otherwise disposed of any equity interest of any Subsidiary or (vi) entered into any agreement, understanding or arrangement with respect to the sale or voting of its equity interests;

(i) made any acquisition of assets, investment or capital expenditures not included in the capital expenditure budget of the Company and its Subsidiaries set forth in Schedule 3.5 in excess of \$25,000 individually or \$100,000 in the aggregate; acquired direct or indirect control over any business or Person, whether by stock purchase, merger, consolidation or otherwise; or entered into any new line of business;

(j) paid, discharged or satisfied any material claims, liabilities or obligations (absolute, accrued, asserted or unasserted, contingent or otherwise), other than the payment, discharge or satisfaction of any liabilities in the Ordinary Course of Business;

(k) made or changed any material Tax election, changed any method of Tax accounting, settled or compromised any material Tax Proceeding, liability for Taxes or right to a refund of Taxes, filed an amended Tax Return or a claim for a refund of Taxes, or entered into any "closing agreement" within the meaning of Section 7121 of the Code (or any similar provision of state, local or foreign Law);

(l) made any change in accounting methods or systems of internal accounting controls (or the manner in which it accrues for liabilities), except as required by changes in GAAP;

(m) taken any action that would or would be reasonably likely to result in any of the conditions set forth in Article VII not being satisfied or prevented or materially delayed the consummation of the transactions contemplated hereby; or

(n) made any commitment to take, or adopted any resolutions of the board of managers of the Company in support of, any of the actions prohibited by this Section 3.5(iii).

### 3.6 ***Title to Assets.***

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(a) Neither the Company nor any of its Subsidiaries own any real property. Schedule 3.6(a) sets forth all lease agreements to which the Company or any of its Subsidiaries are bound as parties with respect to any Leased Real Property (the “**Real Property Leases**”). True and complete copies of all Real Property Leases have been made available to Purchaser prior to the date hereof. All Real Property Leases are valid, binding, and in full force and effect and are enforceable against the Company or one of its Subsidiaries, as the case may be, and, to the Knowledge of the Company, the other parties thereto, in accordance with their terms and subject to the General Enforceability Exceptions. The Company and/or its Subsidiaries have complied in all material respects with the terms of the Real Property Leases and there are no material defaults existing under the Real Property Leases on the part of the Company or any of its Subsidiaries or, to the Knowledge of the Company, of any other party thereto. The Company and/or its Subsidiaries own title to, or have valid leasehold or license interests in, all of the real property and tangible and intangible personal properties utilized by the Company and/or its Subsidiaries in the ownership or operation of their respective businesses.

(b) Except as set forth on Schedule 3.6(b)(i), no Liens (other than Permitted Liens set forth on Schedule 3.6(b)(ii)) exist on any of the Company’s or its Subsidiaries’ assets, properties, or the Leased Real Property. All Personal Property Leases are valid, binding, and in full force and effect and are enforceable against the Company or one of its Subsidiaries, as the case may be, and, to the Knowledge of the Company, the other party thereto, in accordance with their terms, subject to the General Enforceability Exceptions. There are no material defaults existing under any of the Personal Property Leases on the part of the Company or any of its Subsidiaries or, to the Knowledge of the Company, of any party thereto.

### 3.7 **Contracts.**

(a) Schedule 3.7(a) lists each of the following Contracts of the Company and/or its Subsidiaries (together with all Real Property Leases listed in Schedule 3.6(a), collectively, the “**Material Contracts**”):

(i) Each Contract or series of related Contracts (A) that resulted in payments by or to the Company or any of its Subsidiaries in excess of \$500,000 during calendar year 2013 or expressly requires such payments in any calendar year commencing on or after January 1, 2014, or (B) that has a term of longer than three (3) years, which, in each case, cannot be cancelled by the Company or such Subsidiary without penalty or without more than 180 days’ notice or;

(ii) All Contracts that relate to the sale of any of the Company’s or any of its Subsidiaries’ assets for consideration in excess of \$50,000;

(iii) All Contracts that relate to the acquisition of any business, a material amount of stock or assets of any other Person or any real property (whether by merger, sale of stock, sale of assets or otherwise), in each case, other than as reflected in the capital expenditure budget of the Company and its Subsidiaries set forth in Schedule 3.5;

(iv) All Contracts relating to Indebtedness, in each case having an outstanding principal amount in excess of \$150,000;

(v) All collective bargaining agreements or Contracts with any labor organization, union or association to which the Company or any of its Subsidiaries is a party;

(vi) Any alliance, cooperation, joint venture or shareholders’ partnership agreement or similar Contract involving a sharing of profits or losses relating to the Company or any of its Subsidiaries;

(vii) All Contracts limiting the freedom of the Company or any of its Subsidiaries to engage in any line of business or to compete with any other Person or prohibiting the Company or any of its Subsidiaries from soliciting customers, clients or employees, in each case whether in any specified geographic region or business or generally, other than any Contract with a vendor or supplier that resulted in payments by the Company or any of its Subsidiaries of less than \$250,000 during calendar year 2013 or that does not expressly require such payments in any calendar year commencing on or after January 1, 2014, *provided* that such vendor and supplier Contracts below such dollar threshold do not bind Purchaser or any of its Affiliates (other than the Company and its Subsidiaries) from and after the Closing;

(viii) All Contracts that contain any (A) exclusive dealing obligation, (B) “clawback” or similar undertaking requiring the reimbursement or refund of any fees, (C) “most favored nation” or similar provision, (D) provision that grants any right of first refusal or right of first offer or similar right or that limits or purports to limit the ability of the Company or any of its Subsidiaries to own, operate, sell, transfer, pledge or otherwise dispose of any assets or business, or (E) any obligation with respect to an “earn-out,” contingent purchase price or similar contingent payment obligation or other comparable liability after the date hereof, other than, in the case of clauses (B) and (C), any Contract that resulted in payments by the Company or any of its Subsidiaries of less than \$250,000 during calendar year 2013 or that does not expressly require

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such payments in any calendar year commencing on or after January 1, 2014, *provided* that such Contracts under clauses (B) and (C) below such dollar threshold do not bind Purchaser or any of its Affiliates (other than the Company and its Subsidiaries) from and after the Closing; and

(ix) All Contracts relating to any interest rate, derivatives or hedging transaction, other than such agreements entered into in the Ordinary Course of Business.

(b) The Company has made available to Purchaser a copy of each Material Contract prior to the date hereof. Except as set forth on Schedule 3.7(b), all Material Contracts are valid, binding, and in full force and are enforceable against, the Company or one of its Subsidiaries, as the case may be, and, to the Knowledge of the Company, the other parties thereto, in accordance with their terms, subject to the General Enforceability Exceptions. Except as set forth on Schedule 3.7(b), neither the Company nor any of its Subsidiaries, as the case may be, is (with or without the lapse of time or the giving of notice, or both) in material breach or default in any respect under any Material Contract, and, to the Knowledge of the Company, no other party to any Material Contract is (with or without the lapse of time or the giving of notice, or both) in breach or default in any respect thereunder.

### 3.8 *Employee Benefit Matters.*

(a) Schedule 3.8(a) sets forth a list of each material Benefit Plan. Except as set forth on Schedule 3.8(a), (i) each Benefit Plan intended to be qualified under Section 401(a) of the Code has received a favorable determination or opinion letter from the IRS regarding its qualification thereunder or may rely on an opinion letter issued by the IRS with respect to a prototype plan adopted in accordance with the requirements for such reliance, or has time remaining for application to the IRS for a determination of the qualified status of such Benefit Plan for any period for which such Benefit Plan would not otherwise be covered by an IRS determination, (ii) each Benefit Plan has been administered in accordance with its terms and requirements of applicable Law in all material respects, (iii) all contributions required to be made to any Benefit Plan, and all premiums due or payable with respect to insurance policies funding any Benefit Plan, for any period through the date hereof have been timely made or paid in full or, to the extent not required to be made or paid on or before the date hereof, have been fully reflected on the Financial Statements, and (iv) no Benefit Plan or employee benefit plan maintained by any ERISA Affiliate, in each case, as of the date hereof or during the six (6) years prior to the date hereof, is subject to Title IV of ERISA or Section 412 of the Code or is a “multiemployer plan,” as defined in Section 3(37) of ERISA.

(b) With respect to each Benefit Plan, the Company has delivered to Purchaser a true, correct and complete copy of: (i) each writing constituting a part of such Benefit Plan, including without limitation all plan documents, employee communications, benefit schedules, trust agreements, and insurance contracts and other funding vehicles, (ii) the most recent Annual Report (Form 5500 Series) and accompanying schedule, if any, (iii) the current summary plan description and any material modifications thereto, if any (in each case, whether or not required to be furnished under ERISA), (iv) the most recent annual financial report, if any, (v) the most recent actuarial report, if any, and (vi) the most recent determination letter from the IRS, if any.

(c) No claim, litigation or formal proceeding (other than routine claims for benefits) is pending or, to the Knowledge of the Company, threatened in writing or asserted in writing, in each case against or in respect of the Benefit Plans.

(d) Neither the execution and delivery of this Agreement, the member approval of this Agreement, nor the consummation of the transactions contemplated hereby will result in any “parachute payment” as defined in Section 280G(b)(2) of the Code.

(e) Neither the execution and delivery of this Agreement nor the consummation of the transactions contemplated hereby will (either alone or in conjunction with any other event) result in, cause the accelerated vesting, funding or delivery of, or increase the amount or value of, any payment or benefit to any employee, officer or director of the Company or any of its Subsidiaries, or result in any limitation on the right of the Company or any of its Subsidiaries to amend, merge, terminate or receive a reversion of assets from any Benefit Plan or related trust.

(f) None of the Benefit Plans provides health care or any other non-pension benefits to any employees after their employment is terminated (other than as required by Part 6 of Subtitle B of Title I of ERISA or similar state law).

(g) Each Benefit Plan that constitutes in any part a nonqualified deferred compensation plan within the meaning of Section 409A of the Code has been operated and maintained in operational and documentary compliance in all material respects with Section 409A of the Code and applicable guidance thereunder.

### 3.9 *Intellectual Property.*

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(a) Schedule 3.9(a) sets forth a complete and accurate list of all patents, registered trademarks, registered copyrights, domain names, service marks, trade names or corporate names and applications for any of the foregoing, in each case owned by the Company or any of its Subsidiaries and material to the conduct of the business of the Company and its Subsidiaries, taken as a whole, as currently conducted.

(b) The Company or a Subsidiary of the Company is the owner of, or has the right to use, free and clear of all Liens, all Intellectual Property material to the business of the Company and its Subsidiaries as currently conducted taken as a whole.

(c) Neither the Company nor any of its Subsidiaries is a party to any pending, or to the Knowledge of the Company, threatened, suit, action or proceeding which involves a claim of infringement, unauthorized use, or violation of any Intellectual Property used or owned by any Person against the Company or its Subsidiaries, or challenging the ownership, use, validity or enforceability of any Intellectual Property owned or used by the Company or its Subsidiaries, except any such suit, action or proceeding that would not reasonably be expected to be, individually or in the aggregate, material to the Company and its Subsidiaries, taken as a whole. To the Knowledge of the Company, (i) neither the Company nor any of its Subsidiaries has interfered with, infringed upon, misappropriated or violated any Intellectual Property of any third Person, and (ii) no third Person has interfered with, infringed upon, misappropriated or violated any Intellectual Property of the Company or any of its Subsidiaries.

(d) Schedule 3.9(d) sets forth a complete and accurate list of all licenses, sublicenses and other agreements to which the Company and/or its Subsidiaries are a party (i) granting any other Person the right to use the Intellectual Property, or (ii) pursuant to which Company or its Subsidiaries are authorized to use any third party Intellectual Property, which are used by the Company or its Subsidiaries in the business of the Company as currently conducted, other than commercial off-the-shelf software.

3.10 **Insurance.** Schedule 3.10 sets forth a list, as of the date hereof, of all material insurance policies maintained by the Company and/or its Subsidiaries (collectively, the “**Insurance Policies**”) and the Company has provided true and complete copies of the Insurance Policies to Purchaser prior to the date hereof. There is no claim for coverage by the Company or any of its Subsidiaries pending under any of such Insurance Policies as to which coverage has been denied or disputed in writing by the underwriters of such Insurance Policies or in respect of which such underwriters have reserved their rights. Such Insurance Policies are in full force and effect on the date of this Agreement and all premiums due on such Insurance Policies have been paid. Neither the Company nor any of its Subsidiaries has received written notice of any threatened termination of, material premium increase with respect to or material alteration of coverage under any of such Insurance Policies.

3.11 **Litigation.** Except as described in Schedule 3.11, there are no Legal Proceedings involving claims (whether direct claims, counter-claims, cross-claims or otherwise) asserted against the Company or its Subsidiaries, or for which the Company or its Subsidiaries may have indemnification or responsibility obligations, for damages in excess of \$15,000 in any particular instance, pending or, to the Knowledge of the Company, threatened, involving (a) the Company or any of its Subsidiaries (other than Quantum Servicing Corporation); or (b) Quantum Servicing Corporation for which the Company or any of its Subsidiaries has retained liability or could have an indemnification obligation. Neither the Company nor any of its Subsidiaries nor any of their respective assets is subject to any Order of any Governmental Authority.

### 3.12 **Operations in Conformity with Law.**

(a) The Company and its Subsidiaries are, and have been since January 1, 2010, in compliance in all material respects with all applicable Laws and Permits, and neither the Company nor any of its Subsidiaries has received any notice asserting a failure to comply in any material respect with any applicable Laws or Permits.

(b) All Permits required for the Company and its Subsidiaries to conduct their business have been obtained and are valid and in full force and effect, except as would not, individually or in the aggregate, be material to the Company or any of its Subsidiaries. Without limiting the generality of the foregoing, the Company is in compliance with any and all licensing requirements necessary for the operation of its REO business as presently conducted. None of the Company or any of its Subsidiaries is, or is required by the nature of its business to be, an approved Seller/Servicer of the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation. The Company or its applicable Subsidiary is a certified federal contractor approved to do business with each of the federal Governmental Entities that is a customer or client of the Company or any of its Subsidiaries, in each case where the Company or its applicable subsidiary is required under applicable Law or Contract to be so certified.

(c) The Company and each of its Subsidiaries has filed (or furnished, as applicable) all reports, forms, correspondence, registrations and statements, together with any amendments required to be made with respect thereto (“**Reports**”), that they were required to file (or furnish, as applicable) since January 1, 2010 with any Governmental Entity, and

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have paid all fees and assessments due and payable in connection therewith, except where the failure to file (or furnish, as applicable) such Report or to pay such fees and assessments, would not reasonably be expected to be, individually or in the aggregate, material to the Company or any of its Subsidiaries. All Reports complied in all material respects with relevant legal requirements, including as to content. There are no unresolved written violations issued by any Governmental Entity with respect to any Report relating to any examinations of the Company or any of its Subsidiaries, except where any such violations would not reasonably be expected to be, individually or in the aggregate, material to the Company or any of its Subsidiaries. The Company has provided to Purchaser prior to the date hereof true and complete copies of all material or non-routine correspondence since January 1, 2011 between the Company or any of its Subsidiaries, on the one hand, and any Governmental Entity, on the other hand (excluding any such correspondence with the Federal National Mortgage Association and/or the Federal Home Loan Mortgage Corporation in its capacity as a customer or client of the Company or any of its Subsidiaries).

(d) Notwithstanding the foregoing, the representations and warranties in this Section 3.12 do not apply to matters covered by Sections 3.8 (Employee Benefit Matters), 3.9 (Intellectual Property), 3.13 (Taxes), and 3.14 (Employee Matters), which matters are covered exclusively in such Sections.

### 3.13 **Taxes.**

(a) Except as set forth on Schedule 3.13:

(i) the Company and its Subsidiaries have duly and timely filed (or obtained extensions as to) all material Tax Returns that are required to have been filed by them (taking into account any extensions for filing) and are true, correct and complete in all material respects;

(ii) the Company and its Subsidiaries have paid or made adequate provision for the payment of all material Taxes (whether or not shown as due on any Tax Returns);

(iii) (A) neither the Company nor any of its Subsidiaries has been audited by any Tax Authority or other governmental authority with respect to the Tax Returns of the Company or such Subsidiary and neither the Company nor any Subsidiary has received any written notice of deficiency or assessment of additional Taxes for which they would be liable, and (B) no deficiency assessment or proposed adjustment of the Taxes for which the Company or any of its Subsidiaries would be liable is pending;

(iv) (A) neither the Company nor any of its Subsidiaries is a party to any action or proceeding by any Tax Authority or other Governmental Entity for assessment or collection of Taxes from the Company or such Subsidiary and (B) neither the Company nor any Subsidiary has granted any waiver of any statute of limitation with respect to, or any extension of a period for the assessment of, any Tax (other than filing extensions to file Tax Returns);

(v) each of the Company and its Subsidiaries has complied in all material respects with applicable Laws relating to the payment and withholding of any Taxes required to be withheld from any payment to an employee, creditor or other third party and all material Taxes required to be withheld by the Company and its Subsidiaries have been duly and timely withheld, and such withheld Taxes have been either duly and timely paid to the proper Governmental Entity or Taxing Authority or properly set aside in accounts for such purpose;

(vi) there are no liens for Taxes on any of the assets of the Company or any of its Subsidiaries other than Liens for Taxes not yet due and payable;

(vii) there have been no entity classification elections filed pursuant to Treasury Regulations Section 301.7701-3 (or any analogous provision of state or local income Tax Law), with respect to the Company or any Subsidiary;

(viii) (A) the Company is, and, since January 1, 2009, has been, properly classified as a partnership for U.S. federal income tax purposes and (B) each of the Subsidiaries is, and since December 30, 2008, has been, properly classified as a partnership or a disregarded entity for U.S. federal income tax purposes, and, in each case, the Company has not taken, nor to the Knowledge of the Company has any other Person taken, a position inconsistent with such classification on any Tax Return, in connection with any Pre-Closing Tax Contest or otherwise ; and

(ix) the Class A Units and the Class B Units constitute all of the partnership interest in the Company for Tax purposes.

(b) The representations and warranties set forth in Sections 3.5, 3.8, 3.14 and this Section 3.13 shall constitute the only representations and warranties by the Company with respect to Taxes, *provided* that the foregoing shall in no way affect Purchaser's rights to indemnification under Section 8.2(a)(vi).

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### 3.14 *Employee Matters*

(a) Except as set forth in Schedule 3.14(a), the Company and each of its Subsidiaries are in compliance in all material respects with all Laws respecting employment and employment practices, terms and conditions of employment and wages and hours.

(b) Neither the Company nor any of its Subsidiaries is subject to any labor strike, lockout, dispute, slow down, stoppage or similar labor dispute. Except as set forth on Schedule 3.14(b), neither the Company nor any of its Subsidiaries has received during the six years immediately prior to the date hereof any notice of, and to the Knowledge of the Company there is not any threatened, labor, or civil rights dispute, controversy, or grievance or any other unfair labor practice proceeding or breach of contract claim or action with respect to claims of, or obligations to, any of the Company's or its Subsidiaries' employees, consultants, officers, or directors.

(c) Each individual who renders services to the Company or any of its Subsidiaries who is classified by the Company or such Subsidiary, as applicable, as having the status of an independent contractor or other non-employee status for any purpose (including for purposes of taxation and tax reporting and under Benefit Plans) is properly so characterized.

(d) Except as set forth on Schedule 3.14(d), (i) there is no collective bargaining or similar agreement with any union, labor organization, works council, or similar representative covering any employee of the Company or any of its Subsidiaries, (ii) no petition for certification or election of any such representative is existing or pending with respect to any employee of the Company or any of its Subsidiaries, and (iii) no such representative has sought certification or recognition with respect to any employee of the Company or any of its Subsidiaries.

3.15 **Brokers.** Except as set forth on Schedule 3.15, all negotiations relating to this Agreement and the transactions contemplated by this Agreement have been carried on without the intervention of any Person acting on behalf of the Company or any of its Subsidiaries in such manner as to give rise to any valid claim against the Company or any of its Subsidiaries or Purchaser for any brokerage or finder's commission, fee, or similar compensation.

3.16 **Affiliate Transactions.** Except as disclosed on Schedule 3.16, no officer, director, equity holder or other Affiliate of the Company or any of its Subsidiaries, or to the Knowledge of the Company, any employee of the Company or any of its Subsidiaries, is a party to any Contract or transaction with the Company or any of its Subsidiaries other than employment related arrangements entered into in the Ordinary Course of Business. No officer, director, equity holder or, to the Knowledge of the Company or any Unitholder, other Affiliate of the Company (other than any Subsidiary of the Company) owns any material properties or assets used in the conduct of the business of the Company and its Subsidiaries.

3.17 **Customers and Suppliers.** Schedule 3.17 attached hereto sets forth (a) a list of the Company's top ten (10) customers from continuing operations (on a consolidated basis) (by gross revenues generated from sales to such customers) (each, a "**Significant Customer**") and (b) a list of the Company's top ten (10) suppliers from continuing operations (on a consolidated basis) (by aggregate cost of purchases from such suppliers) (each, a "**Significant Supplier**"), in each case for the fiscal year ended December 31, 2013. Neither the Company nor any of its Subsidiaries has received any written notice from any Significant Customer to the effect that such Significant Customer will stop, materially decrease the rate of, or materially and adversely change the terms (whether related to payment, price or otherwise) with respect to, buying products or services from the Company or any of its Subsidiaries (whether as a result of the consummation of the Transaction or otherwise), and to the Knowledge of the Company, no Significant Customer has threatened in writing to do any of the foregoing. Neither the Company nor any of its Subsidiaries has received any written notice from any Significant Supplier to the effect that such Significant Supplier will stop, materially decrease the rate of, or materially and adversely change the terms (whether related to payment, price or otherwise) with respect to, supplying materials, products or services to the Company or any of its Subsidiaries (whether as a result of the consummation of the Transaction or otherwise), and to the Knowledge of the Company, no Significant Supplier has threatened in writing to do any of the foregoing.

3.18 **Data Collection and Privacy Policies.** The collection, use, storage, transfer and disclosure of any personally identifiable information (the "**Information Practices**") by the Company and its Subsidiaries, and use by third parties having authorized access to the databases or other records of the Company and its Subsidiaries, conforms in all material respects, and at all times has conformed in all material respects, to all Laws and all contractual commitments governing the Information Practices of the Company and each of its Subsidiaries. The Information Practices of the Company and its Subsidiaries have been materially consistent with all statements or representations (as they may have been amended or supplemented) made to customers, potential customers and third parties regarding such practices. Since January 1, 2010, the Company and its Subsidiaries (a) have not received any written notification alleging that the Company or any of its Subsidiaries have violated any regulation relating to the Information Practices by the Company or any of its Subsidiaries or by third parties having authorized access to databases or other records of the Company and its Subsidiaries, and (b) to the Knowledge of the Company, there have been no material violations of any regulation relating to the Information Practices.

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### 3.19 *Disclaimer of Other Representations and Warranties.*

(a) NEITHER THE COMPANY NOR ANY OF ITS SUBSIDIARIES, REPRESENTATIVES, EMPLOYEES, DIRECTORS, OFFICERS OR UNITHOLDERS HAS MADE, AND SHALL BE DEEMED TO HAVE MADE, ANY REPRESENTATIONS OR WARRANTIES, EXPRESS OR IMPLIED, OF ANY NATURE WHATSOEVER RELATING TO THE COMPANY OR ANY OF ITS SUBSIDIARIES OR THE BUSINESS OF THE COMPANY OR ANY OF ITS SUBSIDIARIES OR OTHERWISE IN CONNECTION WITH THE TRANSACTION, OTHER THAN THOSE REPRESENTATIONS AND WARRANTIES EXPRESSLY SET FORTH IN THIS ARTICLE III.

(b) Without limiting the generality of the foregoing, but without limiting the ability of Purchaser to rely on the representations and warranties expressly set forth in this Article III, neither the Company, any Unitholder nor any other Person (including, without limitation, any representative, employee, officer, director or stockholder of the Company or any of its Subsidiaries) has made, and shall not be deemed to have made, any express or implied representation or warranty, either written or oral, in the materials relating to the business of the Company and its Subsidiaries made available to Purchaser, including due diligence materials, or in any presentation of the business of the Company and its Subsidiaries by management of the Company or others in connection with the Transaction, and no statement contained in any of such materials or made in any such presentation shall be deemed a representation or warranty hereunder or otherwise or deemed to be relied upon by Purchaser in executing, delivering and performing this Agreement and the other transactions contemplated hereby. It is understood that any cost estimates, projections or other predictions, any data, any financial information or any memoranda or offering materials or presentations, including but not limited to any offering memorandum or similar materials made available by the Company and its representatives, are not and shall not be deemed to be or to include representations or warranties of the Company, and are not and shall not be deemed to be relied upon by Purchaser in executing, delivering and performing this Agreement and the transactions contemplated hereby.

## ARTICLE IV

### REPRESENTATIONS AND WARRANTIES OF UNITHOLDERS

Each of the Unitholders, severally and not jointly, hereby represents and warrants to Purchaser those representations and warranties set forth in Article IV. Unless otherwise specifically set forth herein, all representations and warranties made pursuant to this Article IV are made as of the date hereof and as of the Closing Date.

4.1 **Authority and Validity.** Such Unitholder (if an entity) is duly organized, validly existing and in good standing under the laws of its jurisdiction of organization. Such Unitholder (if an entity) has the limited liability company power and authority to execute and deliver this Agreement and the other Transaction Documents to which it is a party and to consummate the Transaction. The execution and delivery of this Agreement and the consummation of the transactions contemplated by this Agreement have been duly and validly authorized by such Unitholder, and no other proceedings on the part of such Unitholder are necessary to approve this Agreement or to consummate the transactions contemplated by this Agreement. This Agreement has been duly and validly executed and delivered by such Unitholder and (assuming due authorization, execution and delivery by the other Parties hereto) constitutes a valid and binding obligation of such Unitholder, enforceable against such Unitholder in accordance with its terms, except as may be limited by the General Enforceability Exceptions. If such Unitholder is a natural Person and is married, and such Unitholder's Class A Units and/or Class B Units constitutes community property or spousal or other approval is otherwise required for this Agreement to be legal, valid and binding, the execution, delivery and performance of this Agreement and the consummation by such Unitholder of the transactions contemplated hereby have been duly authorized by, and, assuming the due authorization, execution and delivery by Purchaser and each of the other Parties hereto, constitutes the legal, valid and binding obligation of such Unitholder's spouse, enforceable against such spouse in accordance with its terms, except as may be limited by the General Enforceability Exceptions.

4.2 **No Violation.** The execution, delivery and performance of such Unitholder of this Agreement does not, and the consummation of the Transaction by such Unitholder, will not, conflict with, or result in any violation of or default (with or without notice or lapse of time, or both) under, or give rise to a right of termination or cancellation under, any provision of (a) the Governing Documents of such Unitholder if such Unitholder is an entity, (b) any Laws or Orders applicable to such Unitholder or (c) any Contract to which such Party is a party or by which such Unitholder is bound or to which any of such Unitholder's properties or assets is subject, other than, in the case of clauses (b) and (c), such conflicts, violations, defaults, terminations or cancellations that would not reasonably be expected to materially impair or delay such Unitholder's ability to consummate the transactions contemplated by this Agreement. No consent, approval, non-objection, Permit, Order, declaration or filing with, or notice to, any Governmental Entity or any third Person is required by or with respect to such Unitholder in connection with the execution and delivery of the Transaction Documents or the consummation of the transactions contemplated thereby.

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4.3 **Ownership of Class A Units and/or Class B Units.** Each such Unitholder is the legal and beneficial owner of the Class A Units and/or the Class B Units set forth opposite his, her or its name on Schedule I, free and clear of all Liens.

4.4 **Brokers.** Except as set forth on Schedule 4.4, all negotiations relating to this Agreement and the transactions contemplated by this Agreement have been carried on without the intervention of any Person acting on behalf of such Unitholder in such manner as to give rise to any valid claim against the Company or any of its Subsidiaries or Purchaser for any brokerage or finder's commission, fee, or similar compensation.

4.5 **Disclaimer of Other Representations and Warranties.** SUCH UNITHOLDER HAS NOT MADE, AND SHALL NOT BE DEEMED TO HAVE MADE, ANY REPRESENTATIONS OR WARRANTIES, EXPRESS OR IMPLIED, OF ANY NATURE WHATSOEVER RELATING TO SUCH UNITHOLDER OR TO THE COMPANY OR ANY OF ITS SUBSIDIARIES OR THE BUSINESS OF THE COMPANY OR ANY OF ITS SUBSIDIARIES OR OTHERWISE IN CONNECTION WITH THE TRANSACTION, OTHER THAN THOSE REPRESENTATIONS AND WARRANTIES EXPRESSLY SET FORTH IN THIS ARTICLE IV.

## ARTICLE V

### REPRESENTATIONS AND WARRANTIES OF PURCHASER

Purchaser hereby represents and warrants to the Company and each Unitholder as follows:

5.1 **Corporate Organization.** Purchaser is a corporation duly incorporated, validly existing and in good standing under the Laws of the State of Delaware. Purchaser has all requisite corporate power and authority to own or lease all of its properties and assets and to carry on its business as it is now being conducted. Purchaser is duly qualified to do business in each jurisdiction in which the nature of its business or the ownership of its properties makes such qualification necessary, except for where such failures to be so qualified would not, individually or in the aggregate, reasonably be expected to materially delay or impair Purchaser's ability to consummate the Transaction.

5.2 **Authority and Validity.** Purchaser has all requisite power and authority to execute and deliver this Agreement and to consummate the Transaction. The execution and delivery of this Agreement and the consummation of the Transaction have been duly and validly authorized by Purchaser, and no other proceedings on the part of Purchaser are necessary to approve this Agreement or to consummate the Transaction. This Agreement has been duly and validly executed and delivered by Purchaser and (assuming due authorization, execution and delivery by the other Parties) constitutes a valid and binding obligation of Purchaser, enforceable against Purchaser in accordance with its terms, except as may be limited by the General Enforceability Exceptions.

5.3 **No Violation.** The execution, delivery and performance by Purchaser of this Agreement does not, and the consummation of the Transaction by Purchaser will not, conflict with, or result in any violation of or default (with or without notice or lapse of time, or both) under, or give rise to a right of termination or cancellation under, any provision of (a) the Governing Documents of Purchaser, (b) any applicable Laws or applicable Orders or (c) any Contract to which Purchaser is a party or by which Purchaser is bound or to which any of Purchaser's properties or assets is subject, other than, in the case of clauses (b) and (c), such conflicts, violations, defaults, terminations or cancellations that would not reasonably be expected to materially impair or delay Purchaser's ability to consummate the transactions contemplated by this Agreement.

5.4 **Investment Intention.** Purchaser is acquiring the Class A Units and the Class B Units being sold hereunder for its own account, for investment purposes only and not with a view to the distribution (as such term is used in Section 2(11) of the Securities Act of 1933, as amended (the "**Securities Act**") thereof. Purchaser understands that neither the Class A Units nor the Class B Units being sold hereunder have been registered under the Securities Act and cannot be sold unless subsequently registered under the Securities Act or an exemption from such registration is available. Purchaser is an "accredited investor" as defined in Rule 501(a) of the Securities Act.

5.5 **Financial Capability; Solvency.** Purchaser has, as of the date hereof and will have as of the Closing Date, sufficient funds to be able to pay full Enterprise Value and any expenses incurred by Purchaser in connection with the Transaction. Purchaser has not incurred any obligation, commitment, restriction or liability of any kind, which would impair or adversely affect such resources and capabilities. No transfer of property is being made and no obligation is being incurred in connection with the Transaction with the intent to hinder, delay or defraud either present or future creditors of Purchaser, the Company or any of their respective Subsidiaries. Immediately after giving effect to the transactions contemplated hereby, Purchaser and its Subsidiaries (including, without limitation, the Company and its Subsidiaries) will be Solvent. As used herein, "**Solvent**" means, with respect to any Person, that (a) the assets of such Person, at a present fair saleable valuation, exceeds the sum of its debts (including a reasonable estimate of all contingent and unliquidated debts); (b) such Person has

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adequate capital to carry on its business as currently conducted; and (c) such Person does not intend or believe it will incur debts beyond its ability to pay as such debts mature.

5.6 **Brokers.** All negotiations relating to this Agreement and the Transaction have been carried on without the intervention of any Person acting on behalf of Purchaser in such manner as to give rise to any valid claim against the Company, any of its Subsidiaries or any Unitholder for any brokerage or finder's commission, fee, or similar compensation.

5.7 **Litigation.** There is no Legal Proceeding pending that relates to this Agreement or the transactions contemplated hereby or, to the knowledge of Purchaser, threatened, against or affecting Purchaser or any of its Affiliates that challenges the validity or enforceability of this Agreement or seeks to enjoin or prohibit consummation of, or seeks other material equitable relief with respect to, the transactions contemplated by this Agreement or that would reasonably be expected to materially impair or delay Purchaser's ability to consummate the transactions contemplated by this Agreement.

5.8 **Inspection; No Other Representations.** Purchaser is an informed and sophisticated Person, and has engaged expert advisors experienced in the evaluation and acquisition of companies such as the Company and its Subsidiaries as contemplated hereunder. Purchaser has undertaken such investigation and has been provided with and has evaluated such documents and information as it has deemed necessary to enable it to make an informed decision with respect to the execution, delivery and performance of this Agreement and the transactions contemplated hereby. Without limiting the generality of the foregoing, Purchaser acknowledges that (a) the Company does not make any representation or warranty with respect to (i) any projections, estimates or budgets delivered to or made available to Purchaser of future revenues, future results of operations (or any component thereof), future cash flows or future financial condition (or any component thereof) of the Company and its Subsidiaries or the future business and operations of the Company and its Subsidiaries (including, without limitation, any future sales of any of the Company's Subsidiaries' products or services) or (ii) any other information or documents made available to Purchaser or its counsel, accountants or advisors with respect to the Company, any of its Subsidiaries or any of their respective businesses, assets, liabilities or operations, except as expressly set forth in Article III, or any Unitholder, except as expressly set forth in Article IV and (b) Purchaser has not relied nor will it rely upon any of the information described in subclauses (i) and (ii) of clause (a) above or any other information, representation or warranty, except those representations or warranties set forth in Article III and Article IV hereof, in negotiating, executing, delivering and performing this Agreement and the transactions contemplated hereby. Purchaser understands and agrees that it is acquiring the Company and its Subsidiaries in the condition the Company and its Subsidiaries are in on the Closing Date based upon Purchaser's own inspection, examination and determination of all matters related thereto, and without reliance upon any express or implied representations or warranties of any nature, whether in writing, orally or otherwise, made by or on behalf of or imputed to the Company, any of its Subsidiaries, the Unitholder Representative or any Unitholder, except for the representations and warranties made by the Company which are expressly set forth in Article III and by each Unitholder which are expressly set forth in Article IV. Purchaser acknowledges and agrees that the representations and warranties set forth in this Agreement (as qualified by the Schedules) supersede, replace and nullify in every respect the data set forth in any other document, material or statement, whether written or oral, made available to Purchaser.

5.9 **Disclaimer of Other Representations and Warranties.** PURCHASER HAS NOT MADE, AND SHALL NOT BE DEEMED TO HAVE MADE, ANY REPRESENTATIONS OR WARRANTIES, EXPRESS OR IMPLIED, OF ANY NATURE WHATSOEVER RELATING TO PURCHASER OR ANY OF ITS AFFILIATES OR OTHERWISE IN CONNECTION WITH THE TRANSACTION, OTHER THAN THOSE REPRESENTATIONS AND WARRANTIES EXPRESSLY SET FORTH IN THIS ARTICLE V.

## ARTICLE VI

### ADDITIONAL AGREEMENTS

#### 6.1 **Further Assurances.**

(a) Subject to the terms hereof, from the date of this Agreement until the Closing Date or the earlier termination of this Agreement (the "**Pre-Closing Period**"), the Company, the Unitholders and Purchaser shall each use its commercially reasonable efforts to (a) take, or cause to be taken, all actions, and do, or cause to be done, and to assist and cooperate with the other Parties in doing, all things necessary, proper or advisable to consummate and make effective the Transaction as promptly as practicable; (b) obtain from any Governmental Entity or any other third party any Consents or Orders required to be obtained or made by the Company, the Unitholders or Purchaser in connection with the authorization, execution and delivery of this Agreement, the other Transaction Documents and the consummation of the Transaction, including those set forth in Schedule 3.1(c); (c) as promptly as practicable, make all necessary filings, and thereafter make and cooperate with the other Parties with respect to any other required submissions, with respect to this Agreement and the Transaction required under (i) any applicable U.S. federal or state or foreign securities Laws, (ii) the HSR Act and any related governmental request thereunder (it being agreed that the Company and Purchaser shall use commercially reasonable efforts, within ten (10) Business

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Days after the execution of this Agreement, to make the necessary filing with the appropriate Governmental Entity in accordance with the HSR Act and thereafter to seek early termination with respect thereto) and any other competition notifications applicable to the Transaction, and (iii) any other applicable Law; and (d) execute or deliver any additional instruments reasonably necessary to consummate the Transaction in accordance with the terms hereof; and (e) as promptly as practicable, make all necessary filings, and thereafter make and cooperate with the other Parties with respect to, and promptly provide to the applicable state licensing authorities any and all information required in connection with, obtaining the consents and approvals (or new licenses) contemplated by Sections 7.2(g) and (h) (it being understood that failure to comply with this clause (e) shall be deemed a material breach of this Agreement for purposes of Section 2.3(a)). Each Party shall supply as promptly as practicable any additional information or documentation that may be requested pursuant to the HSR Act or any other applicable Law; *provided, however*, that any information or documentation provided pursuant to this sentence may be redacted as necessary to address reasonable attorney-client privilege concerns.

(b) Each Party shall, in connection with the actions referenced in Section 6.1(a) to obtain all requisite approvals and authorizations for the Transaction under the HSR Act or any other applicable Law, (i) cooperate with each other in connection with any communication, filing or submission; (ii) keep the other Parties and/or its counsel informed of any communication received by such Party from, or given by such Party to, the FTC, the DOJ or any other Governmental Entity, in each case regarding the Transaction; and (iii) permit the other Party and/or its counsel to review in advance any submission, filing or communication (and documents submitted therewith) intended to be given by it to, and consult with each other in advance of any meeting or conference with, the FTC, the DOJ or any other Governmental Entity, and to the extent permitted by the FTC, the DOJ or such other Governmental Entity, give the other Party and/or its counsel the opportunity to attend and participate in such meetings and conferences.

(c) For the avoidance of doubt, the failure to obtain any Consent or Order set forth in Schedule 3.1(c) shall not in and of itself serve as the basis for Purchaser to seek indemnification under Article VIII, *provided* that the Company and the Unitholders used commercially reasonable efforts to obtain such Consent or Order pursuant to this Section 6.1 and otherwise did not breach this Agreement or take any other action that would be indemnifiable under Article VIII.

**6.2 Notification.** Prior to the Closing or the earlier termination of this Agreement, the Company and the Unitholder Representative shall promptly disclose to Purchaser any event, development or occurrence which would result in the condition set forth in Section 7.2(a) becoming incapable of being satisfied (any such disclosure, an “*MAE Notice*”), affirmatively state that such matter would result in the condition set forth in Section 7.2(a) being incapable of being satisfied and promptly provide Purchaser with any information reasonably requested by Purchaser with respect to the matters specified in any MAE Notice. Purchaser shall have the right to terminate this Agreement for failure to satisfy the closing condition set forth in Section 7.2(a) by providing written notice to the Unitholder Representative prior to the Closing electing to so terminate this Agreement; *provided* that if Purchaser does not elect to terminate this Agreement prior to the Closing, then Purchaser shall be deemed to have irrevocably waived its right to indemnification under Article VIII with respect to the specific matters expressly described in the MAE Notice.

### **6.3 Confidentiality.**

(a) Purchaser acknowledges that the information provided to it in connection with this Agreement and the Transaction is subject to the terms of the letter agreement by and between the Company and Purchaser, dated January 21, 2014 (the “*Non-Disclosure and Confidentiality Agreement*”), the terms of which are incorporated herein by reference. Effective upon, and only upon, the Closing, the Non-Disclosure and Confidentiality Agreement shall terminate. In the event that this Agreement terminates pursuant to Section 2.3, however, the Non-Disclosure and Confidentiality Agreement shall continue in full force and effect in accordance with its terms. The Parties hereto agree that any information provided by Purchaser or its Affiliates to the Company, the Unitholders or their respective Affiliates in connection with this Agreement and the Transaction, including information regarding integration and future business planning, shall be protected in the same manner that information provided by the Company to Purchaser is protected from disclosure and use under the Non-Disclosure and Confidentiality Agreement, *mutatis mutandis*.

(b) From the Closing until the third (3<sup>rd</sup>) anniversary of the Closing Date, each of the Unitholders agrees that it shall not disclose to any Person not employed by Purchaser or an Affiliate of Purchaser or not engaged to render services to Purchaser or an Affiliate of Purchaser, or use for the benefit of itself or others, any confidential information or trade secrets of the Company or its Subsidiaries; *provided, however*, that this Section 6.3(b) shall not preclude any Unitholder from use or disclosure of such information (i) if use or disclosure of such information is required by applicable Law, (ii) if use or disclosure of such information is required in connection with any bona fide claim against or involving such Unitholder, (iii) if such information is readily ascertainable from public information other than as a result of a breach of the confidentiality obligations herein by any Unitholder, (iv) if such Unitholder receives such information on a non-confidential basis from a source other than Purchaser, the Company or any of its Subsidiaries or any of their respective officers, directors, managers, employees, agents or

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representatives, *provided* that such source is not known (after due inquiry) by such Unitholder to be subject to a contractual, legal, fiduciary or other obligation of confidentiality with respect to such information, or (v) if such information is or was independently developed by such Unitholder without the use of or reference to any such information; *provided, further*, that in the case of clauses (i) and (ii), the applicable Unitholder shall provide Purchaser, to the extent practicable, with adequate prior notice to allow Purchaser to seek an appropriate protective order, and shall reasonably cooperate with Purchaser (at Purchaser's sole expense) in connection therewith; *provided, further*, that nothing in this Section 6.3(b) shall limit or restrict the disclosure or use of any such confidential information by any Unitholder who is an officer, director, manager or employee of the Company or any of its Subsidiaries in the performance of such Unitholder's duties as such on behalf of the Company and/or any of such Subsidiaries.

**6.4 *Publicity.*** The Parties hereto will, and will cause each of their respective Affiliates and representatives to, maintain the confidentiality of this Agreement and the transactions contemplated hereby and will not, and will cause each of their respective Affiliates not to, issue or cause the publication of any press release or other public announcement with respect to this Agreement or the transactions contemplated hereby without the prior written consent of the Unitholder Representative and Purchaser, which consent shall not be unreasonably withheld; *provided, however*, that (a) upon the execution of this Agreement each party may release its own press release in the form previously agreed and upon the Closing the Unitholder Representative and Purchaser shall release a mutually agreed upon joint press release, (b) a Party may, without the prior consent of Purchaser and Unitholder Representative, issue or cause publication of any such press release or public announcement to the extent that such party reasonably determines, after consultation with outside legal counsel, such action to be required by Law or by the rules of any applicable self-regulatory organization or stock exchange, in which event such Party will use its commercially reasonable efforts to consult with Purchaser and the Unitholder Representative and allow reasonable time to comment on such press release or public announcement in advance of its issuance and (c) nothing in this Section 6.4 shall prohibit any institutional Unitholder from disclosing any information relating to the transactions contemplated by this Agreement to any current or prospective investor or limited partner of such Unitholder to the extent such disclosure is customarily made in the ordinary course of such Unitholder's business.

#### **6.5 *Tax Matters.***

(a) All transfer, documentary, sales, use, stamp, registration and other similar Taxes, and all conveyance fees, recording charges and other fees and charges (including any penalties and interest) incurred in connection with the consummation of the Transaction ("**Transfer Taxes**"), shall be borne equally by Purchaser, on the one hand, and the Unitholders, on the other hand. All necessary Tax Returns and other documentation with respect to all such Transfer Taxes shall be timely filed by the party primarily responsible for such filing under applicable Law.

(b) (i) The Unitholder Representative shall have the right to elect to cause to be prepared, at the expense of the Unitholders (based on their respective Pro Rata Shares on a several and not joint basis, with any such expenses due from the Unitholders to be paid out of the Escrow Amount), all income, franchise or other similar Tax Returns of the Company and its Subsidiaries for all Tax periods ending on or before the Closing Date (including any Tax Return required to be filed by the Company in respect of Quantum Servicing Corporation, a Delaware corporation) and any other Tax Returns of the Company or any of its Subsidiaries for all Tax periods ending on or before the Closing Date if the Unitholders may be obligated to indemnify Purchaser for such Taxes under this Agreement ("**Pre-Closing Tax Returns**"), by providing reasonable prior notice to Purchaser and the Company. Such Tax Returns shall be prepared in a manner consistent with past practice. If the Unitholder Representative has elected to prepare such Tax Returns, the Unitholder Representative shall provide Purchaser drafts of the Pre-Closing Tax Returns for its review and approval at least thirty (30) days prior to the filing of such Tax Returns, and Purchaser shall timely file or cause to be timely filed all such Tax Returns of the Company and each of its Subsidiaries.

(ii) If the Unitholder Representative has not elected to prepare such Tax Returns, Purchaser shall, at the expense of the Unitholders (based on their respective Pro Rata Shares on a several and not joint basis, with any such expenses due from the Unitholders to be paid out of the Escrow Amount), prepare such Tax Returns consistent with the provisions of this Section 6.5(b), and shall provide such Tax Returns to the Unitholder Representative for its review and approval at least thirty (30) days prior to filing.

(iii) Purchaser shall prepare or cause to be prepared any Tax Returns of the Company and any of its Subsidiaries for all Tax periods that begin on or before and end after the Closing Date (all such Tax Returns, the "**Straddle Returns**"). Such Straddle Returns shall be prepared in a manner consistent with past practice. Purchaser shall provide drafts of such Straddle Returns to the Unitholder Representative for its review and approval at least thirty (30) days prior to filing.

(iv) In the event of a dispute with respect to any Pre-Closing Tax Returns or Straddle Returns (whether prepared by the Unitholder Representative or Purchaser) described in this Section 6.5(b), the Parties shall negotiate in good faith to resolve such dispute for thirty (30) days. Any dispute that cannot be resolved through negotiations between

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Purchaser and the Unitholder Representative shall be taken to the Neutral Arbitrator. All fees and expenses relating to the work performed by the Neutral Arbitrator shall be allocated equally between the Unitholders (based on their respective Pro Rata Shares on a several and not joint basis), on the one hand, and Purchaser, on the other hand, with any such fees and expenses due from the Unitholders to be paid out of the Escrow Amount. The determination of the Neutral Arbitrator shall be binding on the Parties.

(c) Prior to the Escrow Termination Date and for so long as the remaining Escrow Amount (reduced for any settled or pending Indemnification Claims) exceeds the amount of the Tax at issue, the Unitholder Representative shall have the right to control, at the expense of the Unitholders (based on their respective Pro Rata Shares on a several and not joint basis, with any such expenses due from the Unitholders to be paid out of the Escrow Amount), and Purchaser shall have the right to participate in (at its own expense), any audit, litigation or other proceeding with respect to Taxes and Tax Returns of the Company or any of its Subsidiaries for which the Unitholders would be obligated to indemnify Purchaser under this Agreement or that relate to a Tax refund or credit for which the Unitholders are entitled to under this Agreement (a “**Pre-Closing Tax Contest**”); *provided, however*, that the Unitholder Representative shall not settle or compromise any such Pre-Closing Tax Contest without Purchaser’s prior written consent (not to be unreasonably withheld, conditioned or delayed) if such settlement or compromise would have the effect of increasing a Tax liability of the Company or its Subsidiaries that is not indemnified by the Unitholders under this Agreement. Purchaser shall provide the Unitholder Representative with prompt notice of any written inquiries by a Taxing Authority relating to a Pre-Closing Tax Contest within five (5) days of the receipt of such notice. If the Unitholder Representative elects not to control such Pre-Closing Tax Contest (or if the Pre-Closing Tax Contest arises after the Escrow Termination Date or at a time when the Tax at issue exceeds the remaining Escrow Amount (reduced for any settled or pending Indemnification Claims) then Purchaser shall control such matter, at the expense of the Unitholders (based on their respective Pro Rata Shares on a several and not joint basis, with any such expenses due from the Unitholders to be paid out of the Escrow Amount), provided in such case that (x) the Unitholder Representative shall have the right to participate in any such matter (at the expense of the Unitholders (based on their respective Pro Rata Shares on a several and not joint basis, with any such expenses due from the Unitholders to be paid out of the Escrow Amount)) and (y) Purchaser shall keep the Unitholder Representative reasonably informed of the details and status of such matter (including providing the Unitholder Representative with copies of all written correspondence regarding such matter). Purchaser shall not settle any such proceedings without the written consent of the Unitholder Representative (not to be unreasonably withheld, conditioned or delayed) if such settlement or compromise would have the effect of increasing a Tax liability that the Unitholders are required to indemnify under this Agreement.

(d) The Unitholder Representative and Purchaser shall cooperate fully, as and to the extent reasonably requested by the other Party, in connection with the filing of any Tax Returns for the Company and its Subsidiaries, the filing and prosecution of any Tax claims, and any audit, litigation or other proceeding with respect to Taxes of the Company or any of its Subsidiaries. Such cooperation shall include making employees available on a mutually convenient basis to provide assistance in the preparation of the Pre-Closing Tax Returns and additional information and explanation of any material provided hereunder.

(e) Without the prior written consent of the Unitholder Representative, neither Purchaser, the Company nor any of their Affiliates shall make or change any Tax election, adopt or change any accounting method, file any Tax Return (including amended Tax Returns), surrender any right to claim a refund of Taxes or take any other action outside the ordinary course of business, in each case, if such election, adoption, change, amendment, surrender or action could have the effect of increasing the Tax liability of the Unitholders or any of their respective direct or indirect owners.

(f) For the portion of the Closing Date after the time of Closing, other than transactions expressly contemplated hereby, Purchaser shall cause the Company and its Subsidiaries to carry on its business only in the ordinary course in the same manner as heretofore conducted.

(g) To the extent permitted or required by applicable Law, the taxable year of each of the Company and its Subsidiaries that includes the Closing Date shall be treated as closing on (and including) the Closing Date. To the extent not permitted or required by applicable Law, for all purposes of this Agreement, in the case of any Straddle Period, the allocation of such Taxes to the Pre-Closing Tax Period shall be determined based on an interim closing of the books as of the close of business on the Closing Date, except for property Taxes, ad valorem Taxes and other similar Taxes calculated without regard to income or receipts which shall be prorated on a daily basis.

**6.6 Conduct of the Business Prior to the Closing.** During the Pre-Closing Period, the Company shall, and shall cause its Subsidiaries to, (a) conduct their respective businesses in the Ordinary Course of Business, except as required by Law or as otherwise expressly contemplated by this Agreement, (b) use commercially reasonable efforts to preserve intact its business and all of its material assets, franchises, licenses, operations and properties, keep available the services of its current officers and significant employees and independent contractors, and maintain its current relations and goodwill with vendors,

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customer base, regulators, employees and other Persons having material business relationships with the Company and/or its Subsidiaries. Without limiting the generality of the foregoing, during the Pre-Closing Period, except as consented to in writing by Purchaser (which consent shall not be unreasonably withheld, conditioned or delayed), the Company shall not, and shall not permit any of its Subsidiaries to, take any action that would cause any of the changes, events or conditions described in Section 3.5 to occur. Notwithstanding the foregoing, Purchaser is hereby deemed to consent to (i) the Company's distribution of its equity and debt interests in MSLS Holdings to Cobra Green or one or more Affiliates of Cobra Green at or prior to the Closing in accordance with the steps set forth on Schedule 6.6 (the "**MSLS Distribution**") and (ii) the Company's distribution of all cash and cash equivalents of the Company and its Subsidiaries in excess of \$2,500,000 in the aggregate to the Unitholders at or prior to the Closing (it being understood that any cash and cash equivalents (other than restricted cash) that is not so distributed (including, for the avoidance of doubt, such \$2,500,000) shall be treated as a Current Asset for all purposes under this Agreement).

#### **6.7 Pre-Closing Period Access to Information.**

(a) Subject to Section 6.7(b), except as required pursuant to any confidentiality agreement or similar Contract between the Company or any of its Subsidiaries and a third Person or pursuant to applicable Law (*provided* that in such case the Parties shall cooperate in good faith to identify a reasonable alternative to make such information available to Purchaser and its representatives), during the Pre-Closing Period, the Company will: (i) provide Purchaser and its representatives (including any Person who is considering providing financing to Purchaser to finance all or any portion of the Enterprise Value that is subject to a written confidentiality agreement with customary restrictions on use and disclosure of information with respect to the Company and its Subsidiaries, and their respective representatives) with reasonable access, upon reasonable prior notice and during normal business hours at mutually convenient times, to the officers, employees, agents and accountants of the Company and its Subsidiaries and their assets and properties and books and records; and (ii) furnish Purchaser and such other Persons with all such information and data (including, without limitation, copies of Contracts, Benefit Plans and other books and records) concerning the business and operations of the Company and its Subsidiaries as Purchaser or any of such other Persons reasonably may request in connection with such investigation.

(b) Any such access and/or investigation by Purchaser and its representatives shall not unreasonably interfere with any of the businesses or operations of the Company or its Subsidiaries. Neither Purchaser nor any of its representatives shall have any contact whatsoever, prior to the Closing Date, with respect to the Company or any of its Subsidiaries or the Transaction with any agent, broker, partner, lessor, vendor, customer, supplier, employee or consultant of the Company or any of its Subsidiaries, except (i) for the management team members with which it has been engaged in discussions and diligence, and (ii) in consultation with the Company and then only with the express prior written approval of the Company (not to be unreasonably withheld). All requests by Purchaser for access or information shall be submitted or directed exclusively to Raymond James & Associates, Inc., Messrs. Bossidy, D'Urso, Kushel or Harris, or any other individual or individuals to be designated in writing by the Company.

**6.8 Post-Closing Preservation of Records.** In order to facilitate the resolution of any claims made against or incurred by the Company and/or any of its Subsidiaries prior to the Closing, or to the extent reasonably necessary for tax, regulatory, contractual or other legitimate, noncompetitive purposes, for a period of seven (7) years after the Closing, Purchaser shall:

(a) retain the books and records (including personnel files) of the Company and its Subsidiaries relating to periods prior to the Closing in a manner reasonably consistent with Purchaser's Record Management Policy and Records Retention Schedule; and

(b) upon reasonable notice, afford the Unitholder Representative reasonable access (including the right to make photocopies), during normal business hours, to such books and records.

**6.9 No Solicitation.** From the date hereof until the earlier of the termination of this Agreement pursuant to Section 2.3 or the Closing, each Unitholder and the Company shall, and shall cause the Company and its Subsidiaries and each of their respective directors, officers, partners, controlled Affiliates, members, managers, trustees, employees and agents and advisors to the extent acting on behalf of such Unitholder, Company or Affiliate (all such parties, collectively, the "**Company Representatives**") to, cease any and all existing activities, discussions or negotiations with any Person other than Purchaser with respect to, and to deal exclusively with Purchaser and its designated Affiliates and representatives regarding, any and all acquisitions of, sales of, and investments in, the Company or any of its Subsidiaries or their respective businesses, securities or assets, whether by way of merger, consolidation or other business combination with any other Person, purchase or exchange of equity interests, purchase of assets or otherwise (an "**Alternative Transaction**") and, without the prior consent of Purchaser, the Unitholders and the Company shall not, and shall cause the Company's Subsidiaries and the Company Representatives not to, directly or indirectly:

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(a) solicit, initiate, encourage or otherwise engage in any negotiations, discussions or other communications with any other Person relating to any Alternative Transaction;

(b) provide information or documentation to any other Person with respect to the Company or any of its Subsidiaries or any of their respective businesses or assets in respect of any Alternative Transaction; or

(c) enter into any Contract with any other Person in respect of any Alternative Transaction.

#### 6.10 **Director and Officer Indemnification and Insurance.**

(a) Purchaser agrees that all rights to indemnification, advancement of expenses and exculpation by the Company and its Subsidiaries for acts or omissions occurring at or prior to the Closing now existing in favor of each Person who is now, or has been at any time prior to the date hereof or who becomes prior to the Closing Date, an officer, director, or manager, as applicable, of the Company or any of its Subsidiaries, as provided in the Governing Documents of the Company or such Subsidiary, in each case as in effect on the date of this Agreement, or pursuant to any other Contract in effect on the date hereof, shall survive the Closing and shall continue in full force and effect in accordance with their respective terms and shall not be amended, repealed or otherwise modified for a period of six (6) years after the Closing Date in any manner that would adversely affect the rights thereunder of such individuals for acts or omissions occurring at or prior to the Closing.

(b) The Company shall, at its own expense, obtain as of the Closing Date "tail" insurance policies with a claims period of six (6) years from the Closing Date with at least the same coverage and amounts, and containing terms and conditions that are not less advantageous to the directors, officers and managers of the Company and its Subsidiaries when compared to the insurance maintained by or on behalf of the Company and its Subsidiaries as of the date hereof, in each case, with respect to claims arising out of or relating to events which occurred on or prior to the Closing Date (including in connection with the Transaction). Alternatively, the Company may, at Cobra Green's expense, arrange for the continuation of the same coverage and amounts, and containing the same terms and conditions as is in force under the policy which provides coverage to Cobra Green as of the Closing Date for the directors, officers and managers of the Company and its Subsidiaries, but solely with respect to claims arising out of or relating to events which occurred on or prior to the Closing Date (including in connection with the Transaction) and the maintenance of such coverage for a period of six (6) years from the Closing Date.

(c) The obligations of Purchaser and the Company under this Section 6.10 shall not be terminated or modified in such a manner as to adversely affect any director, officer or manager to whom this Section 6.10 applies without the consent of such affected director, officer or manager (it being expressly agreed that the directors, officers and managers to whom this Section 6.10 applies shall be third-party beneficiaries of this Section 6.10, each of whom may enforce the provisions of this Section 6.10).

(d) In the event Purchaser, the Company or any Subsidiary of the Company or any of their respective successors or assigns (i) consolidates with or merges into any other Person and shall not be the continuing or surviving corporation or entity in such consolidation or merger or (ii) transfers all or substantially all of its properties and assets to any Person, then, and in either such case, proper provision shall be made so that the successors and assigns of Purchaser, the Company or such Subsidiary, as the case may be, shall assume all of the obligations set forth in this Section 6.10.

6.11 **Employment and Benefit Matters.** For the period commencing on the Closing Date and ending on December 31, 2014, Purchaser agrees to maintain the compensation and benefit levels, including base salary, annual cash incentive opportunities, retirement benefits, and health and welfare benefits for the employees of the Company (or any of the Company's Subsidiaries) who remain employed after the Closing Date (the "**Company Employees**") at levels which are, in the aggregate, at least comparable to those in effect for the Company Employees immediately prior to the Closing. Purchaser will treat, and cause the applicable benefit plans to treat, the service of the Company Employees with the Company (or any Subsidiary of the Company) attributable to any period before the Closing Date as service rendered to Purchaser or any Subsidiary of Purchaser for purposes of eligibility and vesting under Purchaser's vacation program, health or welfare plan(s) (other than short-term disability and life insurance plans) maintained by Purchaser, and Purchaser's defined contribution plans, except where credit would result in duplication of benefits. Without limiting the foregoing, to the extent that any Company Employee participates in any health or other group welfare benefit plan of Purchaser following the Closing Date, (a) Purchaser shall cause any pre-existing conditions or limitations, eligibility waiting periods or required physical examinations under any health or similar welfare plan of Purchaser to be waived with respect to the Company Employees and their eligible dependents, to the extent waived under the corresponding plan in which the Company Employee participated immediately prior to the Closing Date, and (b) any deductibles paid by any such Company Employee under any of the Company's or its Subsidiaries' health plans in the plan year in which the Closing Date occurs shall be credited towards deductibles under the health plans of Purchaser or any Subsidiary of Purchaser. The provisions contained in this Section 6.11 are included for the sole benefit of the respective parties to this Agreement, and shall not create (i) any third-party beneficiary or other rights in any Company Employees, employees, or independent contractors or their respective legal representatives or beneficiaries or any other Person

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or (ii) any right to continued employment with the Company, any of its Subsidiaries, or Purchaser. Nothing contained in this Section 6.11 is intended to be or shall be considered to be an amendment or adoption of any Benefit Plan, program, Contract, arrangement or policy of the Company, any of its Subsidiaries or Purchaser nor shall it interfere with Purchaser's, Company's or any of their respective Subsidiaries' right to amend, suspend or modify or terminate any Benefit Plan or to terminate the employment of any employee or service of any independent contractor of the Company or its Subsidiaries for any reason.

6.12 **Certain Waivers.** Effective as of Closing, each Unitholder that is not a Company Employee, on its own behalf and on behalf of its Affiliates, irrevocably and unconditionally waives, releases and discharges any and all claims as against Purchaser and its Affiliates (including, from and after the Closing, the Company and its Subsidiaries) and/or the Company Employees, and agrees not to sue, commence, prosecute or pursue, or cause to be commenced or prosecuted, or voluntarily aid, any claim against Purchaser or its Affiliates (including, from and after the Closing, the Company and its Subsidiaries) and/or the Company Employees, regardless of the jurisdiction in which such claims arise; *provided* that each such Unitholder and its Affiliates, and each of their respective successors and assigns retains, and does not release, such Person's rights, if any, (a) to pursue any and all claims, actions or rights that such Person may now or in future have solely on account of rights of such Person under this Agreement or any other documents entered into in connection therewith, (b) any other claim that may arise in the future based on events or circumstances occurring after the Closing and (c) under this Section 6.12.

6.13 **Non-Competition and Non-Solicitation.**

(a) In order to induce Purchaser to enter into this Agreement, each Unitholder, severally and not jointly, agrees that it will not, and will not permit any of its controlled Affiliates or their respective directors, officers, managers, employees employed by such Unitholder at such time and agents and advisors to the extent acting on behalf of such Unitholder or Affiliate to, directly or indirectly, in each case on its own behalf or for the benefit of any other Person, other than on behalf of Purchaser or its Affiliates (including the Company and its Subsidiaries):

(i) during the period beginning on the date hereof and ending on the second (2<sup>nd</sup>) anniversary of the Closing Date, engage in, have an interest in or otherwise be employed by (whether as an owner, operator, partner, member, manager, employee, officer, director, consultant, advisor, lender, representative or otherwise) any business or organization engaged in the business of providing (A) residential loan review and due diligence services, (B) oversight and monitoring of residential servicer and residential loan performance or (C) REO-to-rental component and securitization services, in each case, to unaffiliated third parties in exchange for fees (collectively, the "**Restricted Services**"); *provided* that (x) ownership of less than five percent (5%) of the outstanding stock of any publicly traded corporation, (y) ownership of MSLS Holdings and its direct and indirect subsidiaries, but only with respect to their activities relating to residential or commercial loan servicing anywhere in Europe and (z) providing any of the Restricted Services to any Affiliate of any investment fund managed by Greenfield Partners, LLC for no consideration (other than management fees and/or the reimbursement of out-of-pocket expenses) shall not be deemed to be violations of this Section 6.13(a)(i) solely by reason thereof;

(ii) during the period beginning on the date hereof and ending on the second (2<sup>nd</sup>) anniversary of the Closing Date, (A) solicit any Person who is or was or whose Affiliate is or was during the twelve (12) months preceding such solicitation a customer of the Company or any of its Subsidiaries for the purpose of providing services competitive with those currently provided by the Company and its Subsidiaries; or (B) enter into or seek to enter into any agreement with any such Person pursuant to which any such Unitholder or its Affiliates would be engaged in providing services competitive with those currently provided by the Company and its Subsidiaries (in each case, other than by virtue of ownership of MSLS Holdings and its direct and indirect subsidiaries, but only with respect to their activities relating to residential or commercial loan servicing anywhere in Europe, which are expressly excluded from the scope of this Section 6.13(a)(ii));

(iii) during the period beginning on the date hereof and ending on the third (3<sup>rd</sup>) anniversary of the Closing Date, contact, approach or solicit for the purpose of offering employment to or hiring or retaining, or actually hire or retain (x) the employees listed on Schedule 6.13(a)(iii)(A), (y) any Person who is employed by the Company or any of its Subsidiaries on the Closing Date and who reports directly to any employee listed on Schedule 6.13(a)(iii)(A) on the Closing Date or (z) any sales employee of the Company or any of its Subsidiaries who is employed by the Company or any of its Subsidiaries on the Closing Date (the Persons described in clauses (x)-(z), each, a "**Restricted Employee**"), or attempt to persuade any such Person not to become employed or retained or continue to be employed or retained by the Company or its Affiliates (including Purchaser and its Affiliates) or to terminate his or her employment or services with the Company or its Affiliates (including Purchaser and its Affiliates); *provided* that the foregoing restrictions contained in this Section 6.13(a)(iii) shall not prohibit general solicitations that are not targeted specifically at the employees that are the subject of this Section 6.13(a)(iii), shall not apply to any Person whose employment is terminated by the Company or any of its Subsidiaries other than for cause and shall not apply to any Person listed on Schedule 6.13(a)(iii)(B); or

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(iv) during the period beginning on the date hereof and ending on the first (1<sup>st</sup>) anniversary of the Closing Date, and other than with respect to any Restricted Employee, contact, approach or solicit for the purpose of offering employment to or hiring or retaining, or actually hire or retain any other Person who is employed by the Company or any of its Subsidiaries on the Closing Date or attempt to persuade any such Person not to become employed or retained or continue to be employed or retained by the Company or its Affiliates (including Purchaser and its Affiliates) or to terminate his or her employment or services with the Company or its Affiliates (including Purchaser and its Affiliates); *provided* that the foregoing restrictions contained in this Section 6.13(a)(iv) shall not prohibit general solicitations that are not targeted specifically at the employees that are the subject of this Section 6.13(a)(iv), shall not apply to any Person whose employment is terminated by the Company or any of its Subsidiaries other than for cause and shall not apply to any Person listed on Schedule 6.13(a)(iii)(B).

(b) It is the intent of the Parties that the provisions of this Section 6.13 shall be enforced to the fullest extent permissible under the laws and public policies applied in each jurisdiction in which enforcement is sought. If any particular provision or portion of this Section 6.13 shall be adjudicated to be invalid or unenforceable, such provision or portion thereof shall be deemed amended to the minimum extent necessary to render such provision or portion valid and enforceable, such amendment to apply only with respect to the operation of such provision or portion in the particular jurisdiction in which such adjudication is made.

(c) The Parties acknowledge that damages and remedies at law for any breach of this Section 6.13 may be inadequate and that Purchaser shall be entitled to seek specific performance and other equitable remedies (including an injunction) and such other relief as a court or tribunal may deem appropriate in addition to any other remedies Purchaser may have in the event of a breach of this Section 6.13.

#### 6.14 *Financing Matters.*

(a) The Company shall, and shall cause its Subsidiaries to, and the Unitholders shall cause the Company to, use commercially reasonable efforts to provide to Purchaser and its Affiliates and representatives such historical, financial and other business information prepared in the Ordinary Course of Business regarding the Company and its Subsidiaries, or capable of being prepared without unreasonable expense or unreasonably interfering with the operation of the Company, as Purchaser or its Affiliates may reasonably request in writing, and provide reasonable cooperation to Purchaser and its Affiliates in connection with any Financing as may be reasonably requested by Purchaser or its Affiliates and that is customary in transactions similar to the Financing, including, subject to the foregoing, (i) using commercially reasonable efforts to cause to be prepared and provided to Purchaser or its Affiliates such financial information, data and financial statements of the Company and its Subsidiaries, which in the case of financial statements, shall be prepared on a reasonable basis from the books and records of the Company and its Subsidiaries presenting fairly in all material respects the financial position of the Company and its Subsidiaries as of the dates presented therein, as may be reasonably requested in connection with any Financing, including in connection with any audit, and (ii) causing executives of the Company and its Subsidiaries, to the extent reasonably required, to assist with the preparation of customary materials for rating agency presentations, offering documents, business projections and similar marketing documents in connection with the Financing; *provided* in each case that such requested cooperation does not unreasonably interfere with the ongoing operations of the Company and its Subsidiaries. Purchaser shall, from time to time, reimburse the Company for any and all reasonable out-of-pocket expenses incurred by the Company and its Subsidiaries (including reasonable fees and disbursements of counsel and accountants) in connection with its compliance with this Section 6.14(a), promptly upon receipt of the Company's written request therefor together with reasonable documentation supporting such request.

(b) As may be reasonably requested by Purchaser from time to time, the Company shall, and shall cause its Subsidiaries to, and the Unitholders shall cause the Company to, at the Purchaser's sole expense, use commercially reasonable efforts to promptly obtain one or more amendments of or waivers to the Clayton Credit Agreement or any related agreement (including the related pledge agreement), to be effective upon the Closing, as reasonably requested by and in accordance with the terms and conditions specified in writing by Purchaser to the Company, and the Company shall, and the Unitholders shall cause the Company to, consult with Purchaser before taking any action with respect to any of the foregoing; *provided* that the Company shall not be obligated under this sentence to take any action that would reasonably be expected to expose the Company or its Subsidiaries to material liability or expenses if the Closing fails to occur. Purchaser shall, from time to time, reimburse the Company for any and all reasonable out-of-pocket expenses incurred by the Company and its Subsidiaries (including reasonable fees and disbursements of counsel and accountants) in connection with its compliance with this Section 6.14(b), promptly upon receipt of the Company's written request therefor together with reasonable documentation supporting such request.

(c) With respect to any outstanding Indebtedness of the Company or any of its Subsidiaries identified by Purchaser in writing at least five (5) Business Days prior to the Closing Date to be repaid in connection with the Closing, (i) the

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Company shall, or shall have caused its Subsidiaries to, and the Unitholders shall cause the Company to, use commercially reasonable efforts to deliver all notices and take other actions required to facilitate the termination of commitments in respect of such Indebtedness, repayment in full of all obligations in respect of such Indebtedness and release of any Liens and guarantees in connection therewith on the Closing Date and (ii) no later than one (1) Business Day prior to the Closing Date, the Company shall, or shall have caused its Subsidiaries to, and the Unitholders shall cause the Company to, use commercially reasonable efforts to furnish to Purchaser customary payoff letters with respect to such Indebtedness (each, a “**Payoff Letter**”) in form and substance reasonably satisfactory to Purchaser from all financial institutions and other Persons to which such Indebtedness is owed, or the applicable agent, trustee or other representative on behalf of such Persons, which Payoff Letters shall (A) indicate the total amount required to be paid to fully satisfy all principal, interest, prepayment premiums, penalties, breakage costs or other outstanding and unpaid obligations related to such Indebtedness as of the Closing Date (the “**Payoff Amount**”) and (B) state that all obligations (including guarantees) in respect thereof and Liens in connection therewith on the assets of the Company or any of its Subsidiaries shall be, substantially concurrently with the receipt of the Payoff Amount on the Closing Date by the Persons holding such Indebtedness, released or arrangements reasonably satisfactory to Purchaser for such release shall have been made as of the Closing, subject, as applicable, to the replacement (or cash collateralization or backstopping) of any then-outstanding letters of credit or similar Indebtedness.

(d) For the avoidance of doubt, (i) the failure (in and of itself) to obtain any amendment, waiver, consent, Payoff Letter or other deliverable under this Section 6.14 shall in no way constitute a breach by the Company, its Subsidiaries or any Unitholder and (ii) any such failure shall not affect Purchaser’s obligations under this Agreement, including, without limitation, its obligation to consummate the Closing as and when provided in Section 2.1.

## ARTICLE VII

### CONDITIONS PRECEDENT

7.1 **Conditions to Each Party’s Obligation.** The respective obligation of each Party to effect the Transaction is subject to the satisfaction at or prior to the Closing of the following conditions:

(a) **HSR Act.** The waiting period applicable to the consummation of the Transaction under the HSR Act shall have expired or been terminated.

(b) **No Injunctions or Restraints; Illegality.** No Order issued by any court or agency of competent jurisdiction or other legal restraint or prohibition preventing the consummation of the Transaction shall be in effect; *provided, however*, the Parties hereto shall use their commercially reasonable efforts to have any such Order vacated or lifted. No statute, rule, regulation, or Order shall have been enacted, entered, promulgated or enforced by any Governmental Entity which prohibits, restricts or makes illegal the consummation of the Transaction.

7.2 **Conditions to Obligation of Purchaser.** The obligation of Purchaser to effect the Transaction is subject to the satisfaction, or waiver by Purchaser, at or prior to the Closing, of the following conditions:

(a) **Representations and Warranties.** (i) The representations and warranties of the Company set forth in Section 3.2 of this Agreement and of each Unitholder set forth in Sections 4.1 and 4.3 of this Agreement shall be true and correct in all respects at and as of the date of this Agreement and at and as of the Closing Date as though made at and as of the Closing Date, and (ii) all other representations and warranties of the Company and each Unitholder set forth in this Agreement shall be true and correct in all respects (without giving effect to any limitation as to “materiality” or “Material Adverse Effect” set forth therein), at and as of the date of this Agreement and at and as of the Closing Date as though made at and as of the Closing Date (except to the extent such representations and warranties speak as of an earlier date, in which case such representations and warranties shall be so true and correct as of such earlier date), except where the failure of such representations and warranties to be true and correct (without giving effect to any limitation as to “materiality” or “Material Adverse Effect” set forth therein), individually or in the aggregate, has not had and would not reasonably be expected to have a Material Adverse Effect.

(b) **Performance of Covenants and Agreements.** The Company and each Unitholder shall have performed all covenants and agreements required to be performed by it under this Agreement in all material respects at or prior to the Closing Date.

(c) **Legal Proceedings.** No action or proceeding by or before any Governmental Entity shall have been instituted or threatened (and not subsequently settled, dismissed or otherwise terminated) which is reasonably expected to restrain, prohibit or invalidate the Transaction.

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(d) **Closing Deliverables.** The Company shall have delivered or caused to be delivered to Purchaser the deliverables set forth in Section 2.2(a) and each Unitholder and/or the Unitholder Representative shall have delivered or caused to be delivered to Purchaser the deliverables set forth in Section 2.2(b).

(e) **Release of Liens.** With respect to any Indebtedness for which Purchaser has requested a Payoff Letter pursuant to Section 6.14(c), all Liens on the assets of the Company or any of its Subsidiaries shall be released substantially concurrently with the receipt of the Payoff Amount on the Closing Date by the Persons holding such Indebtedness, or arrangements reasonably satisfactory to Purchaser for such release shall have been made as of the Closing, subject, as applicable, to the replacement (or cash collateralization or backstopping) of any then-outstanding letters of credit or similar Indebtedness.

(f) **Letter Agreements.** Neither Bossidy nor D'Urso shall have (i) repudiated his respective Letter Agreement, (ii) died, become permanently disabled or resigned or (iii) taken or failed to take any action that would constitute "Cause" under such Letter Agreement (including any exhibit thereto) had such action been taken immediately following the effective time of such Letter Agreement.

(g) **Certain CSS Licenses.** With respect to the mortgage origination/brokerage licenses held by Clayton Support Services LLC, a Delaware limited liability company ("CSS"), as of immediately prior to the Closing, CSS shall have obtained consents and approvals from, or shall have delivered any required notices to, or new licenses shall have been granted to CSS or Purchaser (or any Affiliate thereof) in lieu thereof by, that number of state licensing authorities, in the aggregate, as is necessary in order for CSS to hold valid mortgage origination/brokerage licenses immediately following the Closing in states representing at least forty-six and four-tenths percent (46.4%) of the origination market in the United States in 2012 (based on the origination statistics set forth on Schedule 7.2(g)).

(h) **Certain GRF Licenses.** With respect to the debt collection licenses held by GR Financial, LLC, a Utah limited liability company ("GRF"), as of immediately prior to the Closing, GRF shall have obtained consents and approvals from, or shall have delivered any required notices to, or new licenses shall have been granted to GRF or Purchaser (or any Affiliate thereof) in lieu thereof by, that number of state licensing authorities, in the aggregate, as is necessary in order for GRF to hold valid debt collection licenses immediately following the Closing in states representing at least eighty percent (80%) of the origination market in the United States in 2012 (based on the origination statistics set forth on Schedule 7.2(g)).

**7.3 Conditions to Obligation of the Unitholders.** The obligation of the Unitholders to effect the Transaction is subject to the satisfaction, or waiver by the Unitholder Representative, at or prior to the Closing, of the following conditions:

(a) **Representations and Warranties.** The representations and warranties of Purchaser set forth in this Agreement shall be true and correct in all respects (without giving effect to any limitation as to "materiality" set forth therein), at and as of the date of this Agreement and at and as of the Closing Date as though made at and as of the Closing Date (except to the extent such representations and warranties speak as of an earlier date, in which case such representations and warranties shall be so true and correct as of such earlier date), except where the failure of such representations and warranties to be true and correct (without giving effect to any limitation as to "materiality" set forth therein), individually or in the aggregate, would not reasonably be expected to prevent Purchaser from consummating the Transaction.

(b) **Performance of Covenants and Agreements of Purchaser.** Purchaser shall have performed all covenants and agreements required to be performed by it under this Agreement in all material respects at or prior to the Closing Date.

(c) **Legal Proceedings.** No action or proceeding by or before any Governmental Entity shall have been instituted or threatened (and not subsequently settled, dismissed or otherwise terminated) which is reasonably expected to restrain, prohibit or invalidate the Transaction.

(d) **Closing Deliverables and Actions.** Purchaser shall have delivered or caused to be delivered to the Unitholders and such other Persons referred to in Section 2.2(c) the deliverables set forth in such Section 2.2(c).

## ARTICLE VIII

### INDEMNIFICATION; CERTAIN REMEDIES

8.1 **Survival.** The representations and warranties of the Parties contained in this Agreement shall survive until the Escrow Termination Date; *provided, however*, that (i) the representations and warranties contained in Sections 3.1(a) (Status), 3.1(b) (Authority), 3.1(c) (No Violation), 3.2 (Capitalization of the Company), 3.3 (Subsidiaries), 3.15 (Brokers), 4.1 (Authority and Validity), 4.2 (No Violation), 4.3 (Ownership of Class A Units and/or Class B Units), 4.4 (Brokers), 5.1

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(Corporate Organization), 5.2 (Authority and Validity) and 5.6 (Brokers), shall survive until the expiration of the applicable statute of limitations (the representations and warranties set forth in this clause (i) being referred to herein as the “**Fundamental Representations**”), (ii) the representations and warranties contained in Sections 3.7 (Contracts), 3.11 (Litigation) and 3.12 (Operations in Conformity with Law) shall survive until the eighteen (18) month anniversary of the Closing Date to the extent, and solely to the extent, that a breach of any such representation or warranty results in any action, suit or proceeding against Purchaser or its Affiliates (including the Company and its Subsidiaries) or for which any of them has indemnification obligations, (iii) the representations and warranties contained in Section 3.13 (Taxes) shall survive until the date that is sixty (60) days following the expiration of the applicable statute of limitations and (iv) any claim for Losses that is properly asserted in writing pursuant to this Article VIII prior to the applicable survival date shall survive until such claim is finally resolved and satisfied. All covenants and other agreements contained in this Agreement shall survive the Closing in accordance with their respective terms.

## 8.2 **Indemnification by the Unitholders.**

(a) Subject to Section 8.4 and the other provisions of this Article VIII, from and after the Closing, each Unitholder, severally and not jointly, hereby agrees to indemnify, defend and hold harmless, and agrees to reimburse Purchaser, its Affiliates and each of their respective past, present and future directors, officers, employees, stockholders, members and partners, as applicable, (collectively, the “**Purchaser Indemnified Parties**”) from and against and for any and all losses, liabilities, obligations, damages, costs, judgments, claims, awards and expenses (including reasonable attorneys’ and consultant fees and expenses) (individually, a “**Loss**” and, collectively, “**Losses**”) actually incurred by a Purchaser Indemnified Party based upon, arising out of or resulting from:

(i) any breach of any of the representations or warranties made by the Company in Article III of this Agreement, in each case without giving effect to any “Material Adverse Effect,” “materiality” or Knowledge qualifications contained in such representations and warranties for purposes of determining whether a breach has occurred (*provided* that qualifications regarding “Material Adverse Effect,” “materiality” and Knowledge shall be given effect for purposes of the representations and warranties set forth in Sections 3.1(c) (last sentence only), 3.4, 3.5(i), 3.5(ii), 3.5(iii)(a), (g), (j) and (m), 3.8(a) (first sentence only), 3.9(a), 3.10 and 3.17, and, for the avoidance of doubt the word “Material” shall not be read out of the definition of “Material Contract”); *provided* that, notwithstanding the foregoing, no matter first arising after the date hereof (for the avoidance of doubt, not including any matter arising prior to the date hereof but not discovered until after the date hereof) shall be deemed a breach of the related representation or warranty set forth in Article III if (A) such matter is consistent with the disclosures set forth in the Disclosure Schedules and (B) such matter would not be materially inconsistent with such representation or warranty (read without regard to qualifications regarding “Material Adverse Effect” and “materiality”);

(ii) any breach of or failure to perform, on or prior to the Closing, any covenant or agreement made by the Company in this Agreement;

(iii) any breach of any of the representations or warranties made by such Unitholder in Article IV of this Agreement, in each case without giving effect to any “Material Adverse Effect,” “materiality” or Knowledge qualifications contained in such representations and warranties for purposes of determining whether a breach has occurred, at and as of the date of this Agreement and at and as of the Closing Date as though made at and as of the Closing Date;

(iv) any breach of or failure to perform any covenant or agreement made by such Unitholder in this Agreement;

(v) any proceeding against Purchaser or any of its Affiliates (including the Company and its Subsidiaries) by any holder or purported holder of Class A Units or Class B Units or other equity interests of the Company or any of its Subsidiaries, in their capacity as such, to the extent based on facts or circumstances occurring at any time on or before the Closing (but not including any such proceedings relating to the enforcement of the Unitholders’ rights hereunder);

(vi) any Excluded Taxes or any Controlled Group Liability; or

(vii) the MSLS Distribution or the existence, operations or ownership of MSLS Holdings.

(b) Purchaser acknowledges and agrees that no Unitholder shall have any liability under any provision of this Agreement for any Loss to the extent that such Loss is based upon, arises out of or results from an action taken by Purchaser, the Company or their respective Affiliates after the Closing Date.

## 8.3 **Indemnification by Purchaser.**

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(a) Subject to Section 8.4 and the other provisions of this Article VIII, from and after the Closing Purchaser hereby agrees to reimburse, defend, indemnify and hold each Unitholder, its Affiliates and each of their respective past, present and future directors, officers, employees, stockholders, members and partners, as applicable (collectively, the “**Unitholder Indemnified Parties**”), harmless from and against any and all Losses actually incurred by a Unitholder Indemnified Party based upon, arising out of or resulting from:

- (i) any breach of any of the representations or warranties made by Purchaser in this Agreement; or
- (ii) any breach of or failure to perform any covenant or agreement made by Purchaser in this Agreement.

(b) Notwithstanding anything herein to the contrary, the Escrow Termination Date shall not apply to, and shall in no manner restrict or bar, any claims brought by a Unitholder Indemnified Party following such date arising from or relating to Purchaser’s failure to satisfy any of its or the Company’s post-Closing payment obligations in this Agreement.

#### 8.4 **Limitations on Indemnification.**

(a) Notwithstanding the provisions of this Article VIII, (i) no Unitholder shall have any indemnification obligations for Losses under Sections 8.2(a)(i) and 8.2(a)(iii) unless and until the aggregate amount of all such Losses actually incurred by the Purchaser Indemnified Parties under Sections 8.2(a)(i) and 8.2(a)(iii) exceeds Three Million Two Hundred Fifty Thousand dollars (\$3,250,000) (the “**Basket Amount**”); *provided, however*, that from and after such time as the total amount of Losses actually incurred by the Purchaser Indemnified Parties under Sections 8.2(a)(i) and 8.2(a)(iii) exceeds the Basket Amount, then the Unitholders shall be liable only for the amount that exceeds the Basket Amount, (ii) no Losses may be claimed by the Purchaser Indemnified Parties under Sections 8.2(a)(i) and 8.2(a)(iii) other than Losses in excess of Fifteen Thousand dollars (\$15,000) resulting from any single claim or series of related claims arising out of the same or similar facts, events or circumstances and (iii) in no event shall the aggregate indemnification to be paid by the Unitholders pursuant to Sections 8.2(a)(i) and 8.2(a)(iii) exceed Thirty Million dollars (\$30,000,000) (the “**Cap**”). Notwithstanding anything to the contrary contained herein but subject to the following proviso, the limitations set forth in clauses (i) - (iii) above shall not apply to any Losses based upon or resulting from any inaccuracy in or breach of any Fundamental Representation made by the Company or any Unitholder or any inaccuracy in or breach of the representations and warranties contained in Section 3.13 (Taxes) or to any Losses arising from fraud or Excluded Taxes; *provided, however*, that the aggregate liability of any Unitholder pursuant to Sections 8.2(a)(i), (ii), (iii), (iv) (other than Sections 6.3, 6.12 and 6.13) or (v) of this Agreement shall under no circumstances exceed the proceeds received by such Unitholder pursuant to the terms of this Agreement.

(b) Notwithstanding anything to the contrary contained in this Agreement, the term “severally and not jointly” as used in this Agreement means that each Unitholder’s liability for Losses will be limited as follows: (i) with respect to indemnification claims made by a Purchaser Indemnified Party pursuant to Section 8.2(a)(iii) or Section 8.2(a)(iv) against a particular Unitholder, the breaching Unitholder will be solely liable for all such Losses (if any), and the Purchaser Indemnified Parties will only be able to seek recourse for any such claim against such breaching Unitholder (including by way of its proportionate share of the Escrow Account), and (ii) with respect to indemnification claims made by a Purchaser Indemnified Party pursuant to Section 8.2(a)(i) or Section 8.2(a)(ii): (A) indemnification from the Escrow Amount will be provided by funds deposited in the Escrow Account until the balance of the Escrow Account is reduced to zero dollars (\$0.00) and (B) indemnification in excess of the Escrow Amount will be provided by each Unitholder up to its Pro Rata Share of such Losses (if any), in each such case, subject to the limitations in this Article VIII.

(c) Notwithstanding anything to the contrary contained in this Agreement, no breach of any representation, warranty, covenant or agreement contained herein shall give rise to any right on the part of any Purchaser Indemnified Party or any Unitholder Indemnified Party, after the consummation of the transactions contemplated hereby, to rescind this Agreement or any of the transactions contemplated hereby.

(d) Any indemnification hereunder for Losses with respect to any Taxes resulting from or arising in connection with any breach of or inaccuracy in any representation or warranty with respect to Taxes (whether pursuant to the definition of Excluded Taxes or otherwise) shall be limited to Taxes attributable to Tax periods (or portions thereof) ending on or prior to the Closing Date, other than representations or warranties contained in Section 3.13(a)(vii), (viii) and (ix).

#### 8.5 **Indemnification Procedures.**

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(a) In the event that indemnification may be sought under this Article VIII (an “**Indemnification Claim**”) in connection with (i) any action, suit or proceeding that may be instituted or (ii) any claim that may be asserted, in any such case, by any Person not a party to this Agreement, the Party seeking indemnification hereunder (the “**Indemnified Party**”) shall promptly cause written notice of the assertion of such Indemnification Claim to be delivered to the Party from whom indemnification hereunder is sought (the “**Indemnifying Party**”) prior to the expiration of the applicable survival period set forth in Section 8.1; *provided, however*, that no delay on the part of the Indemnified Party in giving any such notice shall relieve the Indemnifying Party of any indemnification obligation hereunder unless (and then solely to the extent that) the Indemnifying Party is prejudiced by such delay. The Indemnifying Party shall have the right, at its sole option and expense, to be represented by counsel of its choice, which must be reasonably satisfactory to the Indemnified Party, and to defend against, negotiate, settle or otherwise deal with any Indemnification Claim and, if the Indemnifying Party elects to defend against, negotiate, settle or otherwise deal with any Indemnification Claim, it shall as promptly as practicable and within thirty (30) days (or sooner, if the nature of the Indemnification Claim so requires) (the “**Dispute Period**”) notify the Indemnified Party of its intent to do so. Unless and until the Indemnifying Party within the Dispute Period elects to defend against, negotiate, settle or otherwise deal with any Indemnification Claim, the Indemnified Party may, subject to below, defend against, negotiate, settle or otherwise deal with such Indemnification Claim, and all legal and other expenses incurred by the Indemnified Party shall be borne by the Indemnifying Party. If the Indemnifying Party assumes the defense of any Indemnification Claim, the Indemnified Party may participate, at its own expense, in the defense of such Indemnification Claim; *provided, however*, that such Indemnified Party shall be entitled to participate in any such defense with separate counsel at the expense of the Indemnifying Party if (v) so requested by the Indemnifying Party to participate, (w) in the reasonable opinion of counsel to the Indemnified Party, a conflict or potential conflict exists between the Indemnified Party and the Indemnifying Party that would make such separate representation advisable or if there are one or more legal defenses or counterclaims available to it or to other Indemnified Parties which are different from or additional to those available to the Indemnifying Party, (x) the claim involves the seeking of non-monetary relief which, if granted, could reasonably be expected to materially and adversely affect the business of the Indemnified Party or its Affiliates, (y) the amount of potential damages exceeds two hundred percent (200%) of the amount that is available for indemnification hereunder, after taking into account all other claims made or reasonably anticipated, or (z) the Indemnifying Party ceases to diligently defend the Indemnification Claim; *provided, further, however*, that the Indemnifying Party shall not be required to pay for more than one (1) such counsel for all Indemnified Parties in connection with any single Indemnification Claim, other than local counsel. In the event of any of (w) - (z) in the preceding sentence, the Indemnified Party shall have the right to take over the defense of the applicable Indemnification Claim. The Parties hereto agree to reasonably cooperate with each other in connection with the defense, negotiation or settlement of any such Indemnification Claim, and the party in charge of the defense, negotiation or settlement shall keep the other parties reasonably apprised at all times as to the status thereof. Notwithstanding anything in this Section 8.5 to the contrary, neither the Indemnifying Party nor the Indemnified Party shall, without the written consent of the other Party, settle or compromise any Indemnification Claim or permit a default or consent to entry of any judgment unless the claimant and such Party provide to such other Party an unqualified release from all liability in respect of the Indemnification Claim and such settlement, compromise or judgment does not involve any non-monetary penalty or admission of fault or liability on the part of the Indemnified Party or its Affiliates.

(b) In the event that an Indemnified Party has any claim against an Indemnifying Party hereunder, but which such claim does not involve an action, suit, proceeding or claim by a third party not party to this Agreement, which such Indemnified Party determines to assert, then such Indemnified Party shall assert such Indemnification Claim by sending written notice to the Indemnifying Party describing in reasonable detail the nature of such claim and, if then available, the Indemnified Party’s estimate of the amount of Losses attributable to such claim (which estimate shall not otherwise affect the Indemnifying Party’s obligations under this Article VIII).

(c) Within five (5) Business Days after any final and non-appealable decision, judgment or award shall have been rendered by any Governmental Entity of competent jurisdiction, or a settlement or arbitration shall have been consummated, or the Indemnified Party and the Indemnifying Party shall have arrived at a mutually binding agreement (any such event, a “**Final Determination**”) with respect to any Indemnification Claim hereunder, the Indemnifying Party shall pay any amount so determined to the Indemnified Party.

(d) Notwithstanding anything to the contrary contained herein, the foregoing provisions of this Section 8.5 shall not apply to Tax matters, which instead shall be governed by Section 6.5(c).

## 8.6 **Calculation of Losses.**

(a) The amount of any Losses for which indemnification is provided under this Article VIII shall be net of any amounts actually recovered by the Indemnified Party under third-party insurance policies or otherwise with respect to such Losses, net of any deductible or any other expense incurred by the Indemnified Party in obtaining such recovery.

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(b) Notwithstanding anything to the contrary elsewhere in this Agreement, no party shall, in any event, be liable to any other Person for any Losses pursuant to this Article VIII to the extent such Losses constitute punitive damages, except to the extent resulting from a settlement or court award in connection with a claim or action brought by a third party.

(c) Notwithstanding anything to the contrary elsewhere in this Agreement, (i) the Purchaser Indemnified Parties are not entitled to indemnification pursuant to this Article VIII to the extent that any matter, amount, item or other fact for which they are seeking indemnification hereunder was included as a Current Liability in determining the Closing Date Net Working Capital Amount, and (ii) the Purchaser Indemnified Parties' rights to indemnification pursuant to this Article VIII on account of any Losses will be reduced by the amount of any reserve reflected on the Company's consolidated books and records as of the Closing Date established for the general category of items or matters similar in nature to the specific items or matters giving rise to such Loss.

**8.7 Tax Treatment of Indemnity Payments.** The Parties agree to treat any indemnity payment made pursuant to this Article VIII as an adjustment to the purchase price for federal, state, local and foreign income Tax purposes, except as otherwise required by applicable Law.

**8.8 Subrogation.** Upon making any payment for Losses of an Indemnified Party under this Article VIII, the Indemnifying Party will, to the extent of such payment, be subrogated to all rights of the Indemnified Party against any third party with respect to the Loss for which the payment relates. In addition to any other obligation under this Agreement, the Indemnified Party agrees to duly execute and deliver, upon request of the Indemnifying Party, all instruments reasonably necessary to evidence and perfect the subrogation and subordination rights granted pursuant to this Section 8.8.

**8.9 Exclusive Remedy.**

(a) The Parties agree that after the Closing, except in the case of actual fraud (in which case a claim for actual fraud may be asserted solely against the Person (or its Affiliate(s)) who committed such actual fraud, and no other Person shall be liable for the actual fraud committed by such Person) or with respect to matters for which the remedy of specific performance, injunctive relief or other non-monetary equitable remedies are available, the exclusive remedies of the Purchaser Indemnified Parties and the Unitholder Indemnified Parties for any Losses based upon, arising out of or otherwise in respect of the matters set forth in this Agreement are the remedies set forth in Section 6.5 and the indemnification obligations of the Parties set forth in this Article VIII.

(b) Purchaser hereby acknowledges and agrees that prior to the Closing, except in the case of actual fraud (in which case a claim for actual fraud may be asserted solely against the Person (or its Affiliate) who committed such actual fraud, and no other Person shall be liable for the actual fraud committed by such Person), Purchaser shall have no right or remedy to take any action in respect of, and the Company and the Unitholders shall have no liability to Purchaser in respect of, any breach by the Company or any Unitholder, as applicable, of any representations or warranties contained herein or any failure to comply with any of the covenants, conditions or agreements contained herein, except (i) to terminate this Agreement pursuant to Section 2.3 hereof, in which event, the Company and the Unitholders shall thereupon only have liability with respect thereto as provided for in Section 2.5 or (ii) to seek specific performance pursuant to Section 9.13 for injunctive relief.

## ARTICLE IX

### GENERAL PROVISIONS

**9.1 Expenses.** Except as otherwise expressly provided herein (including, without limitation, Section 6.5 hereof), all costs and expenses, including, without limitation, fees and disbursements of counsel, financial advisors and accountants, incurred in connection with this Agreement and the Transaction shall be the responsibility of the Party incurring such costs and expenses, whether or not the Closing shall have occurred; *provided, however*, that Purchaser shall be responsible for all filing and other similar fees payable in connection with any filings or submissions under the HSR Act and any comparable foreign Laws.

**9.2 Notices.** All notices, requests, demands and other communications made under or by reasons of this Agreement shall be in writing and shall be given by facsimile, hand delivery, certified or registered mail, return receipt requested, or next day courier to the affected Party at the address set forth below. Such notices shall be deemed given (a) at the time personally delivered, if delivered by hand with receipt acknowledged; (b) at the time received, if sent by facsimile with confirmation of receipt or by certified or registered mail; and (c) the first day after timely delivery to the courier, if sent by next day courier specifying next day delivery:

- (i) if to Purchaser or, following Closing, the Company:
-



Radian Group Inc.  
1601 Market Street  
Philadelphia, PA 19103  
Attn: Edward J. Hoffman, General Counsel and Corporate Secretary  
Fax: (215) 405-9160

with a copy (which shall not constitute notice) to:

Wachtell, Lipton, Rosen & Katz  
51 West 52nd Street  
New York, NY 10019  
Attn: Nicholas G. Demmo  
Fax: (212) 403-2000

- (ii) if to any Unitholder, to the Unitholder Representative at the address provided below; and
- (iii) if, prior to the Closing, to the Company or, after the Closing, to the Unitholder Representative:

Cobra Green LLC  
c/o Greenfield Partners, LLC  
Two Post Road West  
Westport, CT 06880  
Attn.: Barry P. Marcus  
Fax: (203) 222-4930

with a copy (which shall not constitute notice) to:

Goodwin Procter LLP  
53 State Street  
Boston, MA 02109  
Attn: John R. LeClaire, Esq. and Matthew F. Walsh, Esq.  
Fax: (617) 523-1231

9.3 **Interpretation.** When a reference is made in this Agreement to “Sections,” or “Exhibits,” such reference shall be to a section of, or an exhibit of, this Agreement unless otherwise indicated. When a reference is made in this Agreement to “Schedule,” such reference shall be to a section of the Disclosure Schedules unless otherwise indicated. The table of contents and headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. Whenever the words “include,” “includes” or “including” are used in this Agreement, they shall be deemed to be followed by the words “without limitation.” The terms defined in the singular have a comparable meaning when used in the plural, and vice versa, and references herein to any gender includes each other gender. The term “director” and “manager” shall be used interchangeably and shall mean a member of an entity’s board of directors, board of managers or similar body. The Company and the Unitholders may, at their option, include in the Disclosure Schedule items that are not material in order to avoid any misunderstanding, and such inclusion, or any references to dollar amounts, shall not be deemed to be an acknowledgement or representation that such items are material, to establish any standard of materiality or to define further the meaning of such terms for purposes of this Agreement. Information disclosed in the Disclosure Schedule shall constitute a disclosure for, and only for, the corresponding Section or subsection of this Agreement and for any other Section or subsection of this Agreement to the extent that it is reasonably apparent on the face of such disclosure that such disclosure is relevant to such other Section or subsection.

9.4 **Counterparts.** This Agreement may be executed in two (2) or more counterparts (including by facsimile or other electronic transmission), all of which shall be considered one and the same agreement and shall become effective when counterparts have been signed by each of the Parties and delivered to the other Parties.

9.5 **Entire Agreement; Construction.** This Agreement (including the Disclosure Schedules, schedules, annexes and exhibits hereto and the other agreements and instruments referred to herein) constitute the entire agreement and supersede all prior agreements and understandings, both written and oral, among the Parties with respect to the subject matter hereof and thereof. The Parties have participated jointly in the negotiation and drafting of this Agreement. In the event an ambiguity or question of intent or interpretation arises, this Agreement shall be construed as if drafted jointly by the Parties and no presumption or burden of proof shall arise favoring or disfavoring any Party by virtue of the authorship of any of the provisions of this Agreement.

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9.6 **Amendment.** This Agreement may not be amended except by an instrument in writing signed by Purchaser and the Unitholder Representative.

9.7 **Waiver.** Purchaser may, with respect to the Company and the Unitholders, and the Unitholder Representative may, with respect to Purchaser, (a) extend the time for the performance of any of its obligations or other acts; (b) waive any inaccuracies in its representations and warranties contained herein or in any document delivered pursuant hereto; or (c) waive compliance with any of its agreements or conditions contained herein. Any such extension or waiver shall be valid if set forth in an instrument in writing signed by the Party against whom the waiver is to be effective. No failure or delay by any Party in exercising any right, power or privilege under this Agreement shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise thereof or the exercise of any other right, power or privilege.

9.8 **Governing Law; Waiver of Jury Trial.** Pursuant to Section 5-1401 of the General Obligations Law of the State of New York, the Parties hereby agree that all issues and questions concerning the construction, validity, enforcement and interpretation of this Agreement and the Schedules and Exhibits hereto shall be governed by, and construed in accordance with, the laws of the State of New York without giving effect to any choice of law or principles of conflict of law, rules or provisions (whether of the State of New York or any other jurisdiction) that would cause the application of the laws of any jurisdiction other than the State of New York. In furtherance of the foregoing, the internal law of the State of New York shall control the interpretation and construction of this Agreement (and all schedules and exhibits hereto), even though under that jurisdiction's choice of law or conflict of law analysis, the substantive law of some other jurisdiction would ordinarily apply. In reference to Section 5-1401 of the General Obligations Law of the State of New York, the Parties hereby agree that this Agreement involves more than \$250,000. All legal proceedings arising out of or relating to this Agreement shall be heard and determined exclusively in any New York federal court sitting in the Borough of Manhattan of the City of New York; *provided, however*, that if such federal court does not have jurisdiction over such legal proceeding, such legal proceeding shall be heard and determined exclusively in any New York state court sitting in the Borough of Manhattan of the City of New York. Consistent with the preceding sentence, the Parties hereto hereby (a) submit to the exclusive jurisdiction of any federal or state court sitting in the Borough of Manhattan of the City of New York for the purpose of any legal proceeding arising out of or relating to this Agreement brought by any party hereto; (b) agree that service of process will be validly effected by sending notice in accordance with Section 9.2; and (c) irrevocably waive, and agree not to assert by way of motion, defense, or otherwise, in any such legal proceeding, any claim that it is not subject personally to the jurisdiction of the above-named courts, that the legal proceeding is brought in an inconvenient forum, that the venue of the legal proceeding is improper, or that this Agreement or the transactions contemplated by this Agreement may not be enforced in or by any of the above-named courts. EACH PARTY HERETO HEREBY WAIVES, TO THE FULLEST EXTENT PERMITTED BY APPLICABLE LAW, ANY RIGHT IT MAY HAVE TO A TRIAL BY JURY IN RESPECT OF ANY SUIT, ACTION OR PROCEEDING DIRECTLY OR INDIRECTLY ARISING OUT OF, UNDER OR IN CONNECTION WITH THIS AGREEMENT.

9.9 **Unitholder Representative.**

(a) Each Unitholder hereby grants the Unitholder Representative full power and authority (but not the obligation) to take all actions under this Agreement and the Escrow Agreement that are to be taken by the Unitholder Representative. Each Unitholder hereby authorizes the Unitholder Representative to take any and all actions on behalf of the Unitholders which the Unitholder Representative believes are necessary or appropriate under this Agreement and the Escrow Agreement, including, without limitation, executing the Escrow Agreement as the Unitholder Representative, giving and receiving any notice or instruction permitted or required under this Agreement or the Escrow Agreement by the Unitholder Representative, interpreting all of the terms and provisions of this Agreement and the Escrow Agreement, authorizing payments to be made with respect hereto or thereto, obtaining reimbursement from the Unitholders for all out-of-pocket fees and expenses and other obligations of or incurred by the Unitholder Representative in connection with this Agreement and the Escrow Agreement, defending all Indemnification Claims against the Escrow Fund pursuant to Article VIII and all disputes pursuant to Section 1.5 or Section 1.6 hereof, consenting to, compromising or settling all Indemnification Claims or disputes pursuant to Section 1.5 or Section 1.6, conducting negotiations with Purchaser and its agents regarding such claims or disputes, dealing with Purchaser and the Escrow Agent under this Agreement and the Escrow Agreement, taking any all other actions specified in or contemplated by this Agreement and the Escrow Agreement to be taken by the Unitholders, and engaging counsel, accountants or other representatives in connection with the foregoing matters. Without limiting the generality of the foregoing, each Unitholder hereby grants the Unitholder Representative full power and authority to interpret all the terms and provisions of this Agreement and the Escrow Agreement and to consent to any amendment hereof or thereof in its capacity as the Unitholder Representative, in each case on behalf of the Unitholders.

(b) Each Unitholder hereby grants the Unitholder Representative the authority (but not the obligation), in each case on behalf of the Unitholders, to:

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(i) Receive all notices or documents given or to be given to Unitholder Representative pursuant hereto or to the Escrow Agreement or in connection herewith or therewith and to receive and accept services of legal process in connection with any suit or proceeding arising under this Agreement or the Escrow Agreement;

(ii) Engage counsel, and such accountants and other advisors and incur such other expenses in connection with this Agreement or the Escrow Agreement and the transactions contemplated hereby or thereby as the Unitholder Representative may in its sole discretion deem appropriate; and

(iii) At and after the Closing, take such action as the Unitholder Representative may in its sole discretion deem appropriate in respect of: (A) waiving any inaccuracies in the representations or warranties of Purchaser, or any breach of a covenant or agreement by Purchaser, in each case contained in this Agreement or in any document delivered by Purchaser pursuant hereto; (B) taking such other action as the Unitholder Representative is authorized to take under this Agreement or the Escrow Agreement; (C) receiving all documents or certificates and making all determinations, in its capacity as the Unitholder Representative, required under this Agreement or the Escrow Agreement; and (D) carrying out any of the transactions contemplated by this Agreement and the Escrow Agreement, including, without limitation, the defense and/or settlement of any claims for which indemnification or payment is sought pursuant to Section 1.5 or Article VIII and any waiver of any obligation of Purchaser.

(c) Notwithstanding any provision herein to the contrary, each Unitholder hereby agrees that the Unitholder Representative shall have no duties to the Unitholders or have any liability to the Unitholders with respect to any action taken, decision made or instruction given by the Unitholder Representative in connection with the Escrow Agreement or this Agreement.

(d) Each Unitholder agrees to indemnify the Unitholder Representative for and shall hold the Unitholder Representative harmless against any loss, liability, fee or expense (including legal, accounting and other advisors' fees and expenses, if applicable) incurred by the Unitholder Representative or any of its Affiliates and any of their respective partners, directors, officers, employees, agents, stockholders, consultants, attorneys, accountants, advisors, brokers, representatives or controlling persons, in each case relating to the Unitholder Representative's conduct as the Unitholder Representative, other than losses, liabilities or expenses resulting from the Unitholder Representative's gross negligence or willful misconduct in connection with its performance under this Agreement and the Escrow Agreement. This indemnification shall survive the termination of this Agreement. The costs of such indemnification (including the costs and expenses of enforcing this right of indemnification) shall be individual obligations of the Unitholders in proportion to their respective Pro Rata Shares of such costs. Each Unitholder hereby agrees that the Unitholder Representative may, in all questions arising under this Agreement, rely on the advice of counsel and for anything done, omitted or suffered in good faith by the Unitholder Representative in accordance with such advice, the Unitholder Representative shall not be liable to the Unitholders or the Escrow Agent or any other Person. Each Unitholder hereby agrees that in no event shall the Unitholder Representative be liable hereunder or in connection herewith for (i) any indirect, punitive, special or consequential damages or (ii) any other amounts that may become due and payable by any Unitholder hereunder.

(e) Each Unitholder agrees that in the performance of its duties hereunder, the Unitholder Representative shall be entitled to (i) rely upon any document or instrument reasonably believed to be genuine, accurate as to content and signed by any Unitholder or any Party hereunder and (ii) assume that any Person purporting to give any notice in accordance with the provisions hereof has been duly authorized to do so.

(f) Each Unitholder hereby authorizes the Unitholder Representative, in its sole discretion, to comply with final, nonappealable orders or decisions issued or process entered by any court of competent jurisdiction or arbitrator with respect to the Escrow Fund. If any portion of the Escrow Fund is disbursed to the Unitholder Representative and is at any time attached, garnished or levied upon under any court order, or in case the payment, assignment, transfer, conveyance or delivery of any such property shall be stayed or enjoined by any court order, or in case any order, judgment or decree shall be made or entered by any court affecting such property or any part thereof, then and in any such event, each Unitholder hereby authorizes the Unitholder Representative, in its sole discretion, but in good faith, to rely upon and comply with any such order, writ, judgment or decree which it is advised by legal counsel selected by it is binding upon it without the need for appeal or other action; and if the Unitholder Representative complies with any such order, writ, judgment or decree, each Unitholder hereby agrees that it shall not be liable to any Unitholder or to any other Person by reason of such compliance even though such order, writ, judgment or decree may be subsequently reversed, modified, annulled set aside or vacated.

(g) Each Unitholder hereby irrevocably constitutes and appoints the Unitholder Representative as such Unitholder's true and lawful attorney-in-fact and agent and authorizes him to act for such Unitholder and in such Unitholder's name, place and stead, in any and all capacities to do and perform every act and thing required or permitted to be done in connection with this Agreement and the Escrow Agreement, as fully to all intents and purposes as such Unitholder might or

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could do in person, including taking any and all action on behalf of such Unitholder from time to time as contemplated hereunder and thereunder. Any delivery by the Unitholder Representative of any waiver, amendment, agreement, opinion, certificate or other document executed by the Unitholder Representative will bind each Unitholder by such documents or action as fully as if such Unitholder had executed and delivered such documents. This appointment and power of attorney shall be deemed an agency coupled with an interest and all authority conferred hereby shall be irrevocable and shall not be subject to termination by operation of law, whether by the death or incapacity of any Unitholder or the occurrence of any other event or events. Such appointment shall be binding upon the heirs, executors, administrators, estates, personal representatives, officers, directors, security holders, successors and assigns of each such Unitholder. All decisions of the Unitholder Representative shall be final and binding on all of the Unitholder, and no such Unitholders shall have the right to object, dissent, protest or otherwise contest the same. Purchaser shall be entitled to rely upon, without independent investigation, any act, notice, instruction or communication from the Unitholder Representative and any document executed by the Unitholder Representative on behalf of any Unitholders and shall be fully protected in connection with any action or inaction taken or omitted to be taken in reliance thereon, absent willful misconduct.

9.10 **Severability.** Any term or provision of this Agreement which is invalid or unenforceable in any jurisdiction shall, as to that jurisdiction, be ineffective to the extent of such invalidity or unenforceability without rendering invalid or unenforceable the remaining terms and provisions of this Agreement or affecting the validity or enforceability of any of the terms or provisions of this Agreement in any other jurisdiction. If any provision of this Agreement is so broad as to be unenforceable, the provision shall be interpreted to be only so broad as is enforceable.

9.11 **Assignment.** Neither this Agreement nor any of the rights, interests or obligations hereunder shall be assigned by any of the Parties hereto (whether by operation of law or otherwise) without the prior written consent of Purchaser and the Unitholder Representative; *provided, however*, that Purchaser may assign any of its rights (but not its obligations) under this Agreement to a direct or indirect wholly owned subsidiary of Purchaser. Subject to the preceding sentence, this Agreement will be binding upon, inure to the benefit of and be enforceable by the Parties and their respective, heirs, successors and permitted assigns.

9.12 **No Third Party Beneficiaries.** Except as otherwise specifically set forth herein (including, without limitation, Sections 1.3(b), 1.5(e)(ii), 6.10(c) and Article VIII), this Agreement is for the sole benefit of the Parties hereto and their permitted assigns, and nothing herein expressed or implied shall give or be construed to give any Person, other than the Parties hereto and such permitted assigns, any legal or equitable rights hereunder. All references herein to the enforceability of agreements with third parties, the existence or non-existence of third party rights, the absence of breaches or defaults by third parties, or similar matters or statements, are intended only to allocate rights and risks among the Parties hereto and are not intended to be admissions against interests, give rise to any inference or proof of accuracy, be admissible against any Party hereto by any third party, or give rise to any claim or benefit to any third party.

9.13 **Enforcement of Agreement.** The Parties hereto agree that irreparable damage would occur if any of the provisions of this Agreement was not performed in accordance with its specific terms or was otherwise breached. It is accordingly agreed that the parties will be entitled to an injunction or injunctions to prevent breaches of this Agreement and to enforce specifically the terms and provisions hereof without bond or other security being required, this being in addition to any other remedy to which they are entitled hereunder, at law or in equity. Subject to the other terms of this Agreement and except as expressly provided in this Agreement, no right or remedy under this Agreement shall limit the exercise or applicability of any other right or remedy under this Agreement.

9.14 **Waiver of Conflicts; Privilege.**

(a) Each of the Parties acknowledges and agrees that Goodwin Procter LLP (“**Goodwin**”) has acted as counsel to the Company and its Subsidiaries, the Unitholder Representative and each of the Unitholders in connection with the negotiation of this Agreement and consummation of the transactions contemplated hereby.

(b) Purchaser hereby consents and agrees to, and from and after the Closing agrees to cause the Company and its Subsidiaries to consent and agree to, Goodwin representing the Unitholder Representative and/or any of the Unitholders (collectively, the “**Unitholder Parties**”) after the Closing in any dispute in which the interests of the Unitholder Parties may be directly adverse to Purchaser and its Subsidiaries (including the Company and its Subsidiaries) that either is existing on the date hereof or arises in the future and relates to this Agreement and the transactions contemplated hereby, even though Goodwin may have represented the Company or its Subsidiaries in a matter substantially related to any such dispute, or may be handling ongoing matters for the Company or its Subsidiaries. Purchaser further consents and agrees to, and from and after the Closing agrees to cause the Company and its Subsidiaries to consent and agree to, the communication by Goodwin to the Unitholder Parties in connection with any such representation of any fact known to Goodwin arising by reason of Goodwin’s prior representation of the Company and its Subsidiaries.

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(c) In connection with the foregoing, Purchaser hereby irrevocably waives and agrees not to assert, and from and after the Closing agrees to cause the Company and its Subsidiaries to irrevocably waive and not to assert, any conflict of interest arising from or in connection with (i) Goodwin's prior representation of the Company and its Subsidiaries and (ii) Goodwin's representation of the Unitholder Representative and the Unitholders prior to and after the Closing.

(d) Purchaser further agrees, on behalf of itself and, after the Closing, on behalf of the Company and its Subsidiaries, that as to all communications in any form or format whatsoever between or among Goodwin, on the one hand, and the Company, its Subsidiaries, the Unitholder Representative and/or any Unitholder, or any of their respective directors, officers employees or other representatives, on the other hand, that relate in any way to the negotiation, documentation and consummation of the transactions contemplated by this Agreement or any dispute arising under this Agreement (collectively, the "**Privileged Communications**"), the attorney-client privilege and the expectation of client confidence relating thereto belong solely to the Unitholder Representative and the Unitholders and shall be controlled by the Unitholder Representative on behalf of the Unitholders and shall not pass to or be claimed by Purchaser, the Company or any of its Subsidiaries.

(e) Notwithstanding the foregoing, in the event that a dispute arises between Purchaser, the Company or its Subsidiaries, on the one hand, and a third party other than the Unitholder Representative or a Unitholder, on the other hand (any such dispute, a "**Third Party Claim**"), Purchaser, the Company or its Subsidiaries may assert the attorney-client privilege to prevent the disclosure of the Privileged Communications to such third party or waive such privilege if desired in connection with resolving such Third Party Claim. In the event that Purchaser, the Company or its Subsidiaries is legally required or requested by Order or otherwise (any such request or Order, a "**Legal Request**") to access or obtain a copy of all or a portion of the Privileged Communications, Purchaser shall be entitled to access or obtain a copy of and disclose the Privileged Communications to the extent necessary to comply with any such Legal Request. In the event of any Legal Request, Purchaser shall promptly notify the Unitholder Representative in writing (prior to the disclosure by Purchaser of any Privileged Communications to the extent practicable) so that the Unitholder Representative can seek a protective order and Purchaser agrees to use all commercially reasonable efforts (at the sole cost and expense of the Unitholder Representative) to assist therewith.

(f) To the extent that files or other materials maintained by Goodwin constitute property of its clients, only the Unitholder Representative and the Unitholders shall hold such property rights and Goodwin shall have no duty to reveal or disclose any such files or other materials or any Privileged Communications to Purchaser, the Company or its Subsidiaries by reason of any attorney-client relationship between Goodwin, on the one hand, and the Company or its Subsidiaries, on the other hand, except that the foregoing limitations shall not apply in connection with any Third Party Claim or Legal Request.

(g) Purchaser agrees that it will not, and that it will cause the Company and its Subsidiaries not to, (i) access or use the Privileged Communications, including by way of review of any electronic data, communications or other information, or by seeking to have the Unitholder Representative or any Unitholder waive the attorney-client or other privilege, or by otherwise asserting that Purchaser, the Company or any of its Subsidiaries has the right to waive the attorney-client or other privilege or (ii) seek to obtain the Privileged Communications from Goodwin; *provided* that (A) the foregoing limitations shall not apply in connection with any Third Party Claim or Legal Request, (B) in no event shall Purchaser, the Company or its Subsidiaries have any liability to the Unitholder Representative or any Unitholder in respect of any inadvertent access to such communications, nor shall Purchaser, the Company or its Subsidiaries have any duty to notify the Unitholder Representative or any Unitholder of any such inadvertent access, (C) none of Purchaser, the Company or its Subsidiaries shall have any duty to segregate any such communications from the other books and records, databases or other data storage media of any kind whatsoever of Purchaser, the Company or its Subsidiaries and (D) in the event that segregation and/or retrieval of such communications becomes necessary or desirable, then the Unitholders shall bear the costs of such segregation and/or retrieval (including reasonable fees and expenses of counsel related thereto).

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IN WITNESS WHEREOF, the Parties have caused this Agreement to be executed and delivered as of the date first above written.

**PURCHASER:**

RADIAN GROUP INC.

By: /s/ S.A. Ibrahim  
Name: S.A. Ibrahim  
Title: Chief Executive Officer

**COMPANY:**

CLAYTON HOLDINGS LLC

By: /s/ Paul T. Bossidy  
Name: Paul T. Bossidy  
Title: Chief Executive Officer

**UNITHOLDERS:**

COBRA GREEN LLC

By: /s/ Barry P. Marcus  
Name: Barry P. Marcus  
Title: Senior Vice President

/s/ Paul T. Bossidy  
Paul T. Bossidy

**UNITHOLDER REPRESENTATIVE:**

COBRA GREEN LLC

By: /s/ Barry P. Marcus  
Name: Barry P. Marcus  
Title: Senior Vice President

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**Schedule I**

<u>Unitholder</u>	<u>Class A Units</u>	<u>Class B Units</u>	<u>Pro Rata Share</u>
Cobra Green LLC	131,739.67	0	99.95513%
Paul T. Bossidy	59.14	100	0.04487%
<b>Total</b>	<b>131,798.81</b>	<b>100</b>	<b>100%</b>

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## Schedule II

### **Definitions**

In addition to any other definitions contained in this Agreement, the following words, terms and phrases shall have the following meanings when used in this Agreement.

“**Affiliate**” means, with respect to any Person, any other Person that, directly or indirectly through one (1) or more intermediaries, controls, or is controlled by, or is under common control with, such Person, and the term “control” (including the terms “controlled by” and “under common control with”) means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of such Person, whether through ownership of voting securities, by contract or otherwise. When referring to Cobra Green, “**controlled Affiliates**” of Cobra Green shall be deemed to include any Affiliate of Cobra Green controlled by Greenfield Acquisition Partners V, L.P.; *provided* that, solely with respect to Sections 6.13(a)(iii)-(iv), when referring to Cobra Green, “**controlled Affiliates**” of Cobra Green also shall be deemed to include any Affiliate of Cobra Green controlled by Greenfield Acquisition Partners VI, L.P. or Greenfield Acquisition Partners VII, L.P.

“**Aggregate Incentive Pool**” has the meaning set forth in the LLC Agreement.

“**Agreement**” is defined in the Preamble of this Agreement.

“**Alternative Transaction**” is defined in Section 6.9 of this Agreement.

“**Balance Sheet**” is defined in Section 3.4(a) of this Agreement.

“**Basket Amount**” is defined in Section 8.4(a) of this Agreement.

“**Benefit Plan**” means any compensatory or employee benefit plan, program, policy or other arrangement providing benefits to any current or former employee, officer, director or independent contractor of the Company or any of its Subsidiaries or to which the Company or any of its Subsidiaries contributes or is obligated to contribute, whether or not written, including without limitation any employee welfare benefit plan within the meaning of Section 3(1) of ERISA, any employee pension benefit plan within the meaning of Section 3(2) of ERISA (whether or not such plan is subject to ERISA) and any bonus, incentive, deferred compensation, tax gross-up, stock purchase, stock option, severance, employment, change of control or fringe benefit plan, program or policy.

“**Board**” means the Board of Managers of the Company.

“**Bossidy**” is defined in the Recitals of this Agreement.

“**Business Day**” means any day of the year on which national banking institutions in New York are opened to the public for conducting business and are not required or authorized to close.

“**Cap**” is defined in Section 8.4(a) of this Agreement.

“**Clayton Credit Agreement**” means the Credit Agreement, dated September 30, 2013, among the Company, as Borrower, the other loan parties thereto, the lenders party thereto and JPMorgan Chase Bank, N.A., as Administrative Agent.

“**Closing**” is defined in Section 2.1 of this Agreement.

“**Closing Balance Sheet**” is defined in Section 1.5(a) of this Agreement.

“**Closing Cash Payment**” is defined in Section 1.2 of this Agreement.

“**Closing Date**” is defined in Section 2.1 of this Agreement

“**Closing Date Net Working Capital Amount**” means the amount by which (i) Current Assets exceeds (ii) Current Liabilities, in each case, determined as of the close of business on the day immediately preceding the Closing Date and in accordance with GAAP as applied in the Financial Statements.

“**Code**” means the Internal Revenue Code of 1986, as amended.

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“**Company**” is defined in the Preamble of this Agreement.

“**Company Employees**” is defined in Section 6.11 of this Agreement.

“**Company Representatives**” is defined in Section 6.9 of this Agreement.

“**Consent**” means any approval, consent, ratification, permission, waiver or authorization from any Person other than any Governmental Entity.

“**Contract**” means any agreement, contract, obligation, promise, commitment or undertaking that is or purports to be legally binding.

“**Controlled Group Liability**” means any and all liabilities (i) under Title IV of ERISA, (ii) under Section 302 of ERISA, (iii) under Sections 412 and 4971 of the Code, (iv) as a result of a failure to comply with the continuation coverage requirements of Section 601 et seq. of ERISA and Section 4980B of the Code, and (v) under corresponding or similar provisions of foreign laws or regulations.

“**Current Assets**” means the aggregate amount of all (i) accounts receivable, net, plus (ii) unbilled receivables, plus (iii) prepaid expenses, plus (iv) other current assets of the Company and its Subsidiaries reflected on the Closing Balance Sheet; *provided* that for purposes of calculating the Estimated Closing Date Net Working Capital Amount and the Closing Date Net Working Capital Amount, Current Assets shall not include any restricted cash or any assets related to income Taxes.

“**Current Liabilities**” means the aggregate amount of all (i) accounts payable, plus (ii) accrued expenses, plus (iii) deferred revenue of the Company and its Subsidiaries reflected on the Closing Balance Sheet; *provided* that for the purposes of calculating the Estimated Closing Date Net Working Capital Amount and the Closing Date Net Working Capital Amount, Current Liabilities shall not include (i) any Indebtedness or Selling Expenses, (ii) any other liabilities paid on or prior to the Closing Date by or on behalf of the Company, (iii) any other liabilities of the Company or its Subsidiaries resulting from or attributable to any action taken on the Closing Date by or on behalf of Purchaser or any of its Affiliates, including any Financing sourced by Purchaser or any of its Affiliates, (iv) any liabilities that are the obligation of Purchaser or any of its Affiliates pursuant to the terms of this Agreement, (v) any income Tax liabilities, whether current or deferred, (vi) any deferred non-income Tax liabilities or (vii) any servicer escrow liability.

“**Disclosure Schedule**” is defined in Article III of this Agreement.

“**Dispute Period**” is defined in Section 8.5(a) of this Agreement.

“**Divested Business**” means any company, business, product line, business unit or business operation that was owned, operated or conducted by the Company or any Subsidiary (or any predecessor thereto) or any former subsidiary thereof, at any time prior to the Closing Date and that is not owned, operated or conducted by the Company or any Subsidiary as of the Closing Date, in each case, whether as a result of a sale, transfer, conveyance, or other disposition.

“**DOJ**” means the Antitrust Division of the U.S. Department of Justice.

“**D’Urso Employment Agreement**” means that certain Amended and Restated Employment Agreement, dated as of November 1, 2013, by and between the Company and Joseph D’Urso, as the same may be amended and/or amended and restated from time to time.

“**Enterprise Value**” is defined in Section 1.2 of this Agreement.

“**ERISA**” means the Employee Retirement Income Security Act of 1974, as amended.

“**ERISA Affiliate**” means any entity that would be considered a single employer with the Company under Section 4001(b) of ERISA or part of the same “controlled group” as the Company for purposes of Section 302(d)(3) of ERISA.

“**Escrow Account**” is defined in Section 1.3(a) of this Agreement.

“**Escrow Agent**” is defined in Section 1.3(a) of this Agreement.

“**Escrow Agreement**” is defined in Section 1.3(a) of this Agreement.

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“**Escrow Amount**” is defined in Section 1.3(a) of this Agreement.

“**Escrow Fund**” has the meaning assigned to such term in the Escrow Agreement.

“**Escrow Termination Date**” is defined in Section 1.3(a) of this Agreement.

“**Estimated Closing Date Net Working Capital Amount**” is defined in Section 1.4 of this Agreement.

“**Estimated Preliminary Statement**” is defined in Section 1.4 of this Agreement.

“**Estimated Purchase Price Adjustment**” is defined in Section 1.4 of this Agreement.

“**Excluded Taxes**” means any liability, whether or not accrued, assessed or currently due and payable, without duplication, for (a) any Taxes of, imposed on or relating to the Company or any Subsidiary for any Pre-Closing Tax Period, (b) any Taxes with respect to any Divested Business, (c) any Taxes of any Unitholder (including any of their direct or indirect owners), (d) any Taxes resulting from or arising in connection with any breach of or inaccuracy in any representation or warranty contained in Section 3.13 (disregarding for this purpose all references to “Knowledge,” “material,” “Material Adverse Effect” and similar qualifications as to materiality set forth therein and any exception set forth in Schedule 3.13), (e) any Taxes attributable to or resulting from any breach of or any failure by the Unitholders, the Company or any Subsidiary to perform any covenant or obligation set out in this Agreement and (f) any Taxes of any other Person for which the Company or any Subsidiary is liable under Treasury Regulations Section 1.1502-6 (or any similar provision of state, local or foreign law) by reason of having been included in any consolidated, affiliated, combined or unitary group at any time before the Closing Date, as transferee or successor, by contract or otherwise.

“**Final Determination**” is defined in Section 8.5(c) of this Agreement.

“**Final Statement**” is defined in Section 1.5(c) of this Agreement.

“**Financial Statements**” is defined in Section 3.4 of this Agreement.

“**Financing**” means any debt, equity or hybrid financing, whether private or public, undertaken by Purchaser or its Affiliates prior to, simultaneously with or immediately following the Closing in connection with the transactions contemplated by this Agreement.

“**FTC**” means the U.S. Federal Trade Commission.

“**GAAP**” means generally accepted accounting principles in the United States in effect as of the applicable date, consistently applied.

“**General Enforceability Exceptions**” is defined in Section 3.1(b) of this Agreement.

“**Goodwin**” is defined in Section 9.14 of this Agreement.

“**Governing Documents**” means with respect to any particular entity, (i) if a corporation, the articles or certificate of incorporation and the bylaws (or similar organizational documents for any entity organized or existing in any non-U.S. jurisdiction), (ii) if a limited partnership, the limited partnership agreement and the articles or certificate of limited partnership (or similar organizational documents for any entity organized or existing in any non-U.S. jurisdiction), (iii) if a limited liability company, the articles of organization or certificate of formation and the limited liability company agreement or operating agreement (or similar organizational documents for any entity organized or existing in any non-U.S. jurisdiction), (iv) if any other type of entity (including any non-U.S. entity), the formation or organizational documents and the governing documents, (v) all equityholders’ agreements, voting agreements, voting trust agreements, joint venture agreements, or registration rights agreements, and (vi) any amendment or supplement to any of the foregoing.

“**Governmental Entity**” means any federal, state, local or foreign government or political subdivision thereof, or any agency or instrumentality of such government or political subdivision, or any self-regulated organization or other non-governmental regulatory authority or quasi-governmental authority (to the extent that the rules, regulations or orders of such organization or authority have the force of Law), or any arbitrator, court or tribunal of competent jurisdiction. For the avoidance of doubt, “Governmental Entities” shall include the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation.

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“**HSR Act**” means the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

“**Incentive Payment**” has the meaning set forth in the Management Incentive Plan.

“**Indebtedness**” means, without duplication, (i) a contract or agreement under which the Company or any of its Subsidiaries has borrowed any money from, or issued or is subject to any loan agreement, credit agreement, promissory note, bond, debenture, line of credit or other evidence of indebtedness to, any Person, (ii) a contract or agreement under which any of the Company or its Subsidiaries has directly or indirectly guaranteed indebtedness for borrowed money of any other Person (other than endorsements for the purpose of collection in the Ordinary Course of Business), (iii) any other loan agreement, credit agreement, promissory note, bond, debenture, or other evidence of indebtedness for borrowed money issued to any Person by the Company or any of its Subsidiaries, (iv) any payment or increased cost under the Management Incentive Plan or the D’Urso Employment Agreement that is triggered by the consummation of the Transaction, and (v) all leases capitalized in accordance with GAAP and all obligations under sale-and-lease back transactions, agreements to repurchase securities sold and other similar financing transactions; *provided, however*, that in no event shall Indebtedness include, or be deemed to include, (a) any obligations, indebtedness or liabilities of the Company or any of its Subsidiaries resulting from any action taken on the Closing Date by or on behalf of Purchaser or any of its Affiliates, including any Financing sourced by Purchaser or any of its Affiliates (except that Indebtedness under the Clayton Credit Agreement shall only be excluded from the definition of Indebtedness to the extent Purchaser increases the outstanding amount of such Indebtedness in connection with, or any time after, the Closing), (b) any obligations, indebtedness or liabilities that are the obligation of Purchaser or any of its Affiliates pursuant to the terms of this Agreement, and (c) any liabilities of the Company or any of its Subsidiaries that are included in the Final Statement as a Current Liability and used in determining the Closing Date Net Working Capital Amount.

“**Indemnification Claim**” is defined in [Section 8.5\(a\)](#) of this Agreement.

“**Indemnified Party**” is defined in [Section 8.5\(a\)](#) of this Agreement.

“**Indemnifying Party**” is defined in [Section 8.5\(a\)](#) of this Agreement.

“**Information Practices**” is defined in [Section 3.18](#) of this Agreement.

“**Insurance Policies**” is defined in [Section 3.10](#) of this Agreement.

“**Intellectual Property**” means all intellectual property rights arising from or in respect of the following: (i) all patents and applications therefor, including continuations, divisionals, continuations-in-part, or reissues of patent applications, and patents issuing thereon; (ii) all trademarks, service marks, trade names, service names, brand names, trade dress rights, logos, internet domain names and corporate names, together with the goodwill associated with any of the foregoing, and all applications, registrations and renewals thereof; and (iii) copyrights and registrations and applications therefor, works of authorship and mask work rights.

“**Knowledge of the Company**” means the actual knowledge of Paul T. Bossidy, Robert Harris, Peter Kushel, Joseph D’Urso, Evan Guttman (solely with respect to human resources and compensation matters), Jennifer Harrison (solely with respect to Clayton Fixed Income Services surveillance business matters), Tom Donatacci (solely with respect to sales and marketing matters), Scott Mowry (solely with respect to loan review and due diligence), Lorenz Schwarz (solely with respect to Green River Capital - REO, short sale and component services matters), Michael Bolton (solely with respect to Clayton Euro Risk matters) and Teresa Gallagher (solely with respect to Clayton Euro Risk matters).

“**Law**” means any and all statutes, laws, ordinances, rules, regulations, Orders, Permits, case law and other rules of law enacted, promulgated or issued by any Governmental Entity.

“**Leased Real Property**” means all real property leased by the Company and/or its Subsidiaries.

“**Legal Proceeding**” means any action, claim (including any cross-claim or counter-claim), suit, litigation, arbitration, proceeding (including any civil, criminal, administrative, investigative or appellate proceeding), hearing, inquiry, audit, examination or investigation commenced, brought, conducted or heard by or before, or otherwise involving, any court or other Governmental Entity or any arbitrator or arbitration panel.

“**Legal Request**” is defined in [Section 9.14\(e\)](#) of this Agreement.

“**Letter Agreement**” is defined in the Recitals of this Agreement.

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“**Lien**” means any mortgage, pledge, security interest, encumbrance, lien (statutory or other), conditional sale agreement, hypothecation, right of others, lease, sublease, license, occupancy agreement, adverse claim or interest, easement, covenant, encroachment, burden, title defect, title retention agreement, voting trust agreement, interest, equity, option, right of first refusal, charge or other restrictions or limitations of any nature.

“**LLC Agreement**” means that certain Third Amended and Restated Limited Liability Company Agreement of the Company, as the same may be amended and/or amended and restated from time to time.

“**Loss**” is defined in Section 8.2(a) of this Agreement.

“**Management Incentive Plan**” means the Company’s Management Incentive Plan, adopted on January 3, 2013, as the same may be amended and/or amended and restated from time to time.

“**Material Adverse Effect**” means, with respect to the Company and its Subsidiaries, the occurrence or existence of an event, condition, fact, change, effect, or development that, individually or in the aggregate, (a) prevents or materially impairs, or would be reasonably likely to prevent or materially impair, the ability of the Company and the Unitholders to timely consummate the transactions contemplated hereby or to perform its agreements or covenants hereunder, or (b) has an effect that is material and adverse on the business, operations, financial condition or results of operations of the Company and its Subsidiaries, on a consolidated basis; *provided, however*, that “**Material Adverse Effect**” shall not include any event, occurrence, fact, condition or change to the extent arising out of or attributable to: (i) any changes, conditions or effects after the date hereof in the economies as a whole or securities or financial markets in general anywhere in the world in which the Company and/or its Subsidiaries currently conducts business; (ii) changes, conditions or effects after the date hereof that affect generally the industries in which the Company operates; (iii) any change, effect or circumstance resulting from an action required by this Agreement or taken at the express written request of Purchaser; (iv) the effect of any changes after the date hereof in applicable Laws or accounting rules, including GAAP; (v) any change, effect or circumstance resulting from the announcement of this Agreement; or (vi) conditions caused by acts of terrorism or war (whether or not declared) or any natural or man-made disaster or other acts of God; except, with respect to clauses (i), (ii), (iv) and (vi) above, to the extent that the effects of such change, condition or effect disproportionately adversely affect the Company and its Subsidiaries, taken as a whole, as compared to other companies in the industries in which the Company and its Subsidiaries operate.

“**Material Contract**” is defined in Section 3.7 of this Agreement.

“**MSLS Holdings**” means MSLS Holdings LLC, a Delaware limited liability company.

“**Neutral Arbitrator**” is defined in Section 1.5(c) of this Agreement.

“**Non-Disclosure and Confidentiality Agreement**” is defined in Section 6.3 of this Agreement.

“**Objection Notice**” is defined in Section 1.5(b) of this Agreement.

“**Order**” is defined in Section 2.3(c) of this Agreement.

“**Ordinary Course of Business**” means the ordinary and usual course of normal day-to-day operations of the Company and its Subsidiaries, consistent with past practice.

“**Participant**” has the meaning set forth in the Management Incentive Plan.

“**Parties**” is defined in the Preamble of this Agreement.

“**Payoff Amount**” is defined in Section 2.3(c) of this Agreement.

“**Payoff Letter**” is defined in Section 2.3(c) of this Agreement.

“**Permitted Liens**” means (i) liens for Taxes not yet due and payable or being contested in good faith by appropriate procedures and for which adequate reserves have been established; (ii) mechanics, carriers’, workmen’s, repairmen’s or other like liens arising or incurred in the Ordinary Course of Business, which secure payment of obligations not past due or which are being contested in good faith by appropriate procedures and for which adequate reserves have been established; (iii) easements, rights of way, zoning ordinances and other similar encumbrances affecting the Real Property Leases which do not and would not reasonably be expected to impair in any material respect the operations of the underlying Leased Real Property or the business of the Company

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or its Subsidiaries; (iv) liens arising under original purchase price conditional sales contracts and equipment leases with third parties entered into in the Ordinary Course of Business and disclosed on [Schedule 3.6\(b\)\(ii\)](#); or (v) other imperfections of title or Liens, if any, that individually or in the aggregate, do not and would not reasonably be expected to materially impair or affect the ownership, use or value of the underlying asset to the Company and its Subsidiaries.

“**Permits**” means all permits, certificates, registrations, accreditations, exemptions, licenses, franchises, approvals, authorizations, and consents that have been issued or granted by any Governmental Entity.

“**Person**” means any individual, corporation, partnership, limited liability company, firm, joint venture, association, joint-stock company, trust, unincorporated organization, Governmental Entity or other entity.

“**Personal Property Leases**” means all leases of tangible personal property to which the Company or any of its Subsidiaries is a party.

“**Pre-Closing Period**” is defined in [Section 6.1](#) of this Agreement.

“**Pre-Closing Tax Contest**” is defined in [Section 6.5\(c\)](#) of this Agreement.

“**Pre-Closing Tax Period**” means any taxable period (or portion thereof) ending on or before the Closing Date.

“**Pre-Closing Tax Returns**” is defined in [Section 6.5\(b\)](#) of this Agreement.

“**Preliminary Statement**” is defined in [Section 1.5\(a\)](#) of this Agreement.

“**Pro Rata Share**” means, with respect to a Unitholder, the percentage shown opposite such Unitholder’s name on [Schedule I](#).

“**Purchase Price**” is defined in [Section 1.2](#) of this Agreement.

“**Purchaser**” is defined in the Preamble of this Agreement.

“**Purchaser Indemnified Parties**” is defined in [Section 8.2\(a\)](#) of this Agreement.

“**Purchaser Terminating Breach**” is defined in [Section 2.3\(e\)](#) of this Agreement.

“**Real Property Leases**” is defined in [Section 3.6\(a\)](#) of this Agreement.

“**Resolution Period**” is defined in [Section 1.5\(b\)](#) of this Agreement.

“**Restricted Employee**” is defined in [Section 6.13\(a\)\(iii\)](#) of this Agreement.

“**Restricted Services**” is defined in [Section 6.13\(a\)\(i\)](#) of this Agreement.

“**Review Period**” is defined in [Section 1.5\(b\)](#) of this Agreement.

“**Securities Act**” is defined in [Section 5.4](#) of this Agreement.

“**Selling Expenses**” means the unpaid obligations of the Company and its Subsidiaries for all legal and other expenses incurred in connection with the Transaction (including any fees and expenses of (i) Goodwin, (ii) Raymond James & Associates, Inc. and (iii) other advisors of the Company) and any other extraordinary expenses incurred by the Company and its Subsidiaries at or prior, or in respect of actions taken at or prior, to the Closing in connection with preparing for, negotiating, documenting or consummating the transactions contemplated hereby; *provided* that (1) Purchaser shall pay for all fees associated with the filing of any notification under the HSR Act and any comparable foreign Laws, as provided in [Section 9.1](#), and (2) in no event shall Selling Expenses include, or be deemed to include, any fee, liability, cost or expense (a) incurred by or on behalf of Purchaser or any of its Affiliates that is otherwise payable to Purchaser or any of its Affiliates, (b) that the Company or any of its Subsidiaries incurs as a result of any action taken on the Closing Date by or on behalf of Purchaser or any of its Affiliates, including any Financing sourced by Purchaser or any of its Affiliates, (c) that is otherwise allocated to, or the obligation of, Purchaser or any of its Affiliates pursuant to the terms of this Agreement, or (d) that is included in the Final Statement as a Current Liability in determining the Closing Date Net Working Capital Amount.

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“**Significant Customer**” is defined in Section 3.17 of this Agreement.

“**Significant Supplier**” is defined in Section 3.17 of this Agreement.

“**Solvent**” is defined in Section 5.5 of this Agreement.

“**Special Bonus**” has the meaning set forth in the D’Urso Employment Agreement.

“**Straddle Returns**” is defined in Section 6.5(b) of this Agreement.

“**Subsidiaries**” means (i) the entities set forth on Schedule 3.3(b) and (ii) all other Persons in which the Company, directly or indirectly, (i) owns at least a majority of the equity interests or other interests having by their terms ordinary voting power to elect a majority of the board of directors or others performing similar functions or (ii) has the power to appoint a general partner, manager or managing member; *provided, however*, that (a) neither MSLS Holdings nor any of its direct or indirect subsidiaries shall be deemed to be Subsidiaries for any purpose hereunder and (b) Quantum Servicing Corporation shall be considered a Subsidiary for purposes of Article III for all periods up to and including January 1, 2014.

“**Target Net Working Capital Amount**” is defined in Section 1.4 of this Agreement.

“**Tax**” means any tax (including any income tax, gross receipts, license, payroll, employment, excise, severance, stamp, occupation, premium, windfall profits, capital stock, franchise, profits, capital gains tax, value-added tax, sales tax, property tax, withholding tax, social security (or similar) or unemployment, and any related charge or amount (including any fine, penalty, interest, or addition to tax)), imposed, assessed, or collected by or under the authority of any Taxing Authority.

“**Tax Authority**” and “**Taxing Authority**” mean any U.S. or non-U.S. federal, national, state, provincial, county, or municipal or other local government, any subdivision, agency, commission, or authority thereof, or any quasi-governmental body exercising any taxing authority or any other authority exercising Tax regulatory authority.

“**Tax Return**” or “**Tax Returns**” means any return, declaration, report, claim for refund, information return or statement or other document relating to Taxes that is filed or required to be filed with any Taxing Authority, including any schedule or attachment thereto, and including any amendments thereof.

“**Termination Date**” is defined in Section 2.3(a) of this Agreement.

“**Third Party Claim**” is defined in Section 9.14(e) of this Agreement.

“**Transaction**” is defined in the Recitals of this Agreement.

“**Transaction Documents**” mean this Agreement and the Escrow Agreement.

“**Transfer Taxes**” is defined in Section 6.5(a) of this Agreement.

“**Unitholder Indemnified Parties**” is defined in Section 8.3(a) of this Agreement.

“**Unitholder Representative**” is defined in the Preamble of this Agreement.

“**Unitholders**” is defined in the Preamble of this Agreement.

“**Unitholder Terminating Breach**” is defined in Section 2.3(d) of this Agreement.

**Radian Group Inc.**  
**Ratio of Earnings to Fixed Charges**

<u>(In thousands)</u>	Three Months Ended	Fiscal Years Ended December 31,				
	March 31, 2014	2013	2012	2011	2010	2009
Net earnings (loss)	\$ 202,759	\$ (196,985)	\$ (451,468)	\$ 302,150	\$ (1,805,867)	\$ (147,879)
Federal and state income tax (benefit) provision	(241)	(10,070)	7,271	66,362	226,189	(94,401)
Earnings (loss) before income taxes	202,518	(207,055)	(444,197)	368,512	(1,579,678)	(242,280)
Equity in net loss (income) of affiliates	13	(1)	13	(65)	(14,668)	(33,226)
Distributed income from equity investees	—	—	92	—	29,498	11,040
Net earnings (loss)	202,531	(207,056)	(444,092)	368,447	(1,564,848)	(264,466)
Fixed charges:						
Interest	19,927	74,618	51,832	61,394	41,777	46,010
One-Third of all rentals	419	1,432	1,873	1,678	1,621	2,496
Fixed charges	20,346	76,050	53,705	63,072	43,398	48,506
Net earnings (loss) available for fixed charges <sup>(1)</sup>	\$ 222,877	\$ (131,006)	\$ (390,387)	\$ 431,519	\$ (1,521,450)	\$ (215,960)
Ratio of net earnings (loss) to fixed charges	11.0x	(2)	(2)	6.8x	(2)	(2)

(1) We do not have any preferred stock for any of the periods presented.

(2) For the fiscal years ended 2013, 2012, 2010 and 2009, earnings were not adequate to cover fixed charges in the amount \$(131,006), \$(390,387), \$(1,521,450) and \$(215,960), respectively. Interest on tax accruals that are non-third party indebtedness are excluded from the calculations.

## CERTIFICATIONS

I, Sanford A. Ibrahim, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Radian Group Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2014

/s/ SANFORD A. IBRAHIM

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Sanford A. Ibrahim  
Chief Executive Officer



I, C. Robert Quint, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Radian Group Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2014

/s/ C. ROBERT QUINT

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C. Robert Quint  
Chief Financial Officer

**Section 1350 Certifications**

I, Sanford A. Ibrahim, Chief Executive Officer of Radian Group Inc., and I, C. Robert Quint, Chief Financial Officer of Radian Group Inc., certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Quarterly Report on Form 10-Q for the quarter ended March 31, 2014 (the "Periodic Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

(2) The information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of Radian Group Inc.

Date: May 6, 2014

/s/ S. A. IBRAHIM

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Sanford A. Ibrahim  
Chief Executive Officer

/s/ C. ROBERT QUINT

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C. Robert Quint  
Chief Financial Officer

