PRIMUS GUARANTY LTD
Form 10-Q
August 13, 2010

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

FORM 10-Q

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2010

or

o **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: 001-32307

Primus Guaranty, Ltd.
(Exact name of registrant as specified in its charter)

Bermuda	**98-0402357**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Clarendon House
2 Church Street
Hamilton HM 11, Bermuda
(Address of principal executive offices, including zip code)
441-296-0519
(Registrant s telephone number, including area code)

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

As of August 10, 2010, the number of shares outstanding of the issuer s common shares, $0.08 par value, was 38,086,002.

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Part I. Financial Information
Item 1. Financial Statements

Primus Guaranty, Ltd.
Condensed Consolidated Statements of Financial Condition (Unaudited)
(in thousands except share amounts)

	June 30, 2010	December 31, 2009
Assets		
Cash and cash equivalents	$ 139,863	$ 299,514
Investments (includes $368,314 and $274,275 at fair value)	368,484	274,444
Restricted cash and investments	129,734	127,116
CLO cash and cash equivalents	117,357	
CLO loans and securities, at fair value	2,422,961	
CLO other assets	56,095	
Accrued interest and premiums	6,815	6,163
Unrealized gain on credit swaps, at fair value	126	2,207
Goodwill and other intangible assets, net	7,712	8,017
Other assets	13,488	15,286
Total assets	$ 3,262,635	$ 732,747
Liabilities and Equity (deficit)		
Liabilities		
Accounts payable and accrued expenses	$ 4,596	$ 7,855
Unrealized loss on credit swaps, at fair value	757,537	691,905
Payable for credit events	4,632	28,596
CLO notes, at fair value	2,266,583	
CLO other liabilities	87,968	
Long-term debt	226,305	244,051
Other liabilities	34,467	9,787
Total liabilities	3,382,088	982,194
Commitments and contingencies		
Equity (deficit)		
Common shares, $0.08 par value, 62,500,000 shares authorized, 38,580,653 and 38,267,546 shares issued and outstanding at June 30, 2010 and December 31, 2009	3,086	3,061
Additional paid-in capital	280,851	280,685
Accumulated other comprehensive income	3,818	2,148
Retained earnings (deficit)	(729,428)	(628,443)
Appropriated retained earnings from CLO consolidation	229,118	
Total shareholders equity (deficit) of Primus Guaranty, Ltd.	(212,555)	(342,549)
Preferred securities of subsidiary	93,102	93,102

Total equity (deficit)	(119,453)	(249,447)
Total liabilities and equity (deficit)	$ 3,262,635	$ 732,747

See accompanying notes.

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Primus Guaranty, Ltd.
Condensed Consolidated Statements of Operations (Unaudited)
(in thousands except per share amounts)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Revenues				
Net credit swap revenue (loss)	$ (189,708)	$ 571,883	$ (102,178)	$ 682,764
Net CLO loss	(124,842)		(47,249)	
CLO interest income	19,510		42,932	
Asset management and advisory fees	263	387	554	806
Interest income	3,541	1,125	6,241	3,498
Gain on retirement of long-term debt	2,676	33,189	7,433	38,948
Impairment loss on investments		(152)		(761)
Other income (loss)	(223)	2,550	(154)	2,474
Total revenues (losses)	(288,783)	608,982	(92,421)	727,729
Expenses				
CLO interest expense	8,258		14,095	
CLO other expenses	2,302		3,292	
Compensation and employee benefits	5,766	4,566	11,191	9,281
Professional and legal fees	2,308	1,957	3,947	3,378
Interest expense	1,737	2,310	3,606	5,068
Other	4,590	2,146	8,126	4,105
Total expenses	24,961	10,979	44,257	21,832
Income (loss) before provision for income taxes	(313,744)	598,003	(136,678)	705,897
Provision (benefit) for income taxes	(140)	5	3	147
Net income (loss)	(313,604)	597,998	(136,681)	705,750
Distributions on preferred securities of subsidiary	724	1,070	1,712	2,014
Less: Net loss attributable to non-parent interests in CLOs	(125,934)		(36,521)	
Net income (loss) available to common shares	$ (188,394)	$ 596,928	$ (101,872)	$ 703,736
Income (loss) per common share:				
Basic	$ (4.84)	$ 14.76	$ (2.63)	$ 17.31
Diluted	$ (4.84)	$ 14.46	$ (2.63)	$ 17.12
Average common shares outstanding:				
Basic	38,903	40,430	38,795	40,646
Diluted	38,903	41,268	38,795	41,096

See accompanying notes.

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Primus Guaranty, Ltd.
Condensed Consolidated Statements of Cash Flows (Unaudited)
(in thousands)

	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Cash flows from operating activities		
Net income (loss) available to common shares	$ (101,872)	$ 703,736
Net loss attributable to non-parent interests in CLOs	(36,521)	
Distributions on preferred securities of subsidiary	1,712	2,014
Net income (loss)	(136,681)	705,750
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Non-cash items included in net income (loss):		
Net unrealized losses on CLO loans and securities	6,366	
Net unrealized losses on CLO notes	92,558	
Net realized gains by the CLOs	(42,580)	
Net unrealized (gains) losses on credit swaps	67,712	(675,514)
Gain on retirement of long-term debt	(7,433)	(38,948)
Impairment loss on available-for-sale investments		761
Other	2,336	2,612
Increase (decrease) in cash resulting from changes in:		
CLO cash and cash equivalents	(25,219)	
CLO other assets	(16,261)	
CLO other liabilities	46,444	
Restricted cash	(1,992)	
Accrued interest and premiums	(652)	3,263
Other assets	(446)	(632)
Trading account assets	(53,346)	3,677
Accounts payable and accrued expenses	(3,260)	287
Payable for credit events	(23,964)	(1,146)
Other liabilities	24,680	(318)
Net cash used in operating activities	(71,738)	(208)
Cash flows from investing activities		
Proceeds from sale of CLO loans and securities	525,125	
Purchases of CLO loans and securities	(514,785)	
Fixed asset purchases	(23)	(56)
Payments received from CLO investments		94
Purchases of available-for-sale investments	(122,569)	(20,566)
Maturities and sales of available-for-sale investments	77,021	367,796
Net cash provided by (used in) investing activities	(35,231)	347,268

Cash flows from financing activities		
Repayment of CLO notes by the CLOs	(35,127)	
Retirement of long-term debt	(12,500)	(18,435)
Purchase, retirement and issuance of common shares	(3,269)	(1,876)
Purchase of preferred securities from subsidiary		(908)
Net preferred distributions of subsidiary	(1,712)	(2,014)
Net cash used in financing activities	(52,608)	(23,233)
Net effect of exchange rate changes on cash	(74)	117
Net increase (decrease) in cash	(159,651)	323,944
Cash and cash equivalents at beginning of period	299,514	280,912
Cash and cash equivalents at end of period	$ 139,863	$ 604,856
Supplemental disclosures		
Cash paid for interest	$ 3,679	$ 5,387
Cash paid for taxes	$ 41	$ 11

See accompanying notes.

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Primus Guaranty, Ltd.
Condensed Consolidated Statements of Equity (Deficit) (Unaudited)
(in thousands)

	Six Months Ended June 30, 2010	Year Ended December 31, 2009
Common shares		
Balance at beginning of period	$ 3,061	$ 3,263
Common shares purchased and retired	(48)	(275)
Shares issued under employee compensation plans	73	73
Balance at end of period	3,086	3,061
Additional paid-in capital		
Balance at beginning of period	280,685	281,596
Common shares purchased and retired	(3,294)	(10,150)
Shares vested under employee compensation plans	3,460	4,728
Preferred shares purchased by subsidiary		4,511
Balance at end of period	280,851	280,685
Accumulated other comprehensive income (loss)		
Balance at beginning of period	2,148	908
Adoption of ASC Topic 810, *Consolidation*	(1,061)	
Foreign currency translation adjustments	(74)	232
Change in unrealized holding gains on available-for-sale securities	2,805	1,008
Balance at end of period	3,818	2,148
Retained earnings (deficit)		
Balance at beginning of period	(628,443)	(2,088,723)
Adoption of ASC Topic 810, *Consolidation*	887	
Net income (loss)	(136,681)	1,463,697
Net loss attributable to non-parent interests in CLOs	36,521	
Distributions on preferred securities of subsidiary	(1,712)	(3,417)
Balance at end of period	(729,428)	(628,443)
Appropriated retained earnings from CLO consolidation		
Adoption of ASC Topic 810, *Consolidation*	265,639	
Net loss attributable to non-parent interests in CLOs	(36,521)	
Balance at end of period	229,118	

Total shareholders equity (deficit) of Primus Guaranty, Ltd.		(212,555)		(342,549)
Preferred securities of subsidiary				
Balance at beginning of period		93,102		98,521
Net purchase of preferred shares				(5,419)
Balance at end of period		93,102		93,102
Total equity (deficit) at end of period	$	(119,453)	$	(249,447)

See accompanying notes.

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Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

1. Organization

Primus Guaranty, Ltd., together with its consolidated wholly owned subsidiaries and, as the context requires, with the collateralized loan obligations (CLOs) under management as required by ASC Topic 810, *Consolidation* (as discussed below) (Primus Guaranty or the Company), is a Bermuda holding company that conducts business currently through its two principal operating subsidiaries, Primus Asset Management, Inc. together with its wholly owned subsidiary CypressTree Investment Management, LLC (collectively Primus Asset Management) and Primus Financial Products, LLC (together with its consolidated wholly owned subsidiaries, Primus Financial).

Effective January 1, 2010, the Company adopted ASC Topic 810, *Consolidation*, which required it to consolidate the assets, liabilities, revenues and expenses of the CLOs under its management.

Primus Asset Management manages CLOs, collateralized swap obligations (CSOs), investment fund vehicles and separately managed accounts on behalf of third parties. Additionally Primus Asset Management, Inc. acts as manager of the credit swap and cash investment portfolios of its affiliate, Primus Financial. Primus Asset Management receives fees for its investment management services. Primus Asset Management, Inc. also has entered into a Services Agreement with its affiliates, whereby it provides management, consulting and information technology services, among others, to its affiliates.

Primus Financial Products, LLC, as a credit derivative product company (CDPC), was established to sell credit protection in the form of credit swaps primarily to global financial institutions and major credit swap dealers. During 2009, the Company announced its intention to amortize Primus Financial Products, LLC s credit swap portfolio. Under the amortization model, Primus Financial s existing credit swap contracts will expire at maturity (unless terminated early) and it is not expected that additional credit swaps will be added to its portfolio, unless associated with a risk mitigation transaction.

2. Summary of Significant Accounting Policies

Accounting Standards Codification

In June 2009, the Financial Accounting Standards Board (FASB) issued the Accounting Standards Codification (ASC or Codification) which becomes the source of authoritative U.S generally accepted accounting principles (GAAP) recognized by the FASB. Rules and interpretive releases of the U.S. Securities and Exchange Commission (SEC) under authority of the U.S. federal securities law are also sources of authoritative GAAP for SEC registrants. This guidance, which is incorporated in ASC Topic 105, *Generally Accepted Accounting Principles*, was adopted by the Company on July 1, 2009. As of the effective date, the Codification supersedes all pre-existing non-SEC accounting and reporting standards. Under the Codification, the FASB issues new standards in the form of Accounting Standards Updates (ASUs).

Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Primus Guaranty, Ltd. have been prepared in accordance with GAAP for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation pursuant to these requirements have been included. The results of operations for any interim period are not necessarily indicative of the results for a full year.

Commencing with the first quarter of 2010, the Company s segment reporting has been modified. The Company s operations are reorganized into two segments for financial reporting purposes: (i) credit protection, asset management and corporate, and (ii) the CLOs on a standalone basis. The condensed consolidated financial statements are presented in U.S. dollar equivalents. During the periods presented, the Company s credit swap activities were conducted in U.S. dollars and euros.

Certain prior year amounts have been reclassified to conform to current year presentation. There was no effect on net income (loss) available to common shares as a result of these reclassifications.

Impact of Adoption of ASC Topic 810, Consolidation

Effective January 1, 2010, the Company adopted ASC Topic 810, *Consolidation*, which modified the previous analysis required to determine whether an enterprise s variable interest(s) give it a controlling financial interest in entities that are variable interest entities (VIEs). This analysis identifies the primary beneficiary of a VIE as the enterprise that has both the power to direct the activities and an obligation to absorb losses or the right to receive benefits that could be potentially significant to a VIE. The Company is required to consolidate the VIE if it is determined to be the primary beneficiary.

The Company s current involvement with VIEs is primarily through activities of Primus Asset Management, which acts as collateral manager for eight CLOs. The Company performed an analysis to determine if it is the primary beneficiary under the accounting standard. The analysis indicated that Primus Asset Management has the power to direct the activities of each CLO. In addition, the variability of both management fees and the Company s investment in the junior subordinated notes or preferred shares issued by certain CLOs indicated an obligation to absorb losses or a right to receive benefits that are potentially significant to each CLO. The analysis concluded that Primus Asset Management is the primary beneficiary of the CLOs under management and therefore, the CLOs under management are required to be consolidated into the Company s financial statements.

Upon adoption of this accounting change on January 1, 2010, the Company consolidated all eight of the CLOs Primus Asset Management manages. The consolidation of these CLOs resulted in an increase for the Company in total assets of $2.5 billion, an increase in total liabilities of $2.3 billion and an increase to total shareholders equity of $266 million on January 1, 2010. The $266 million increase in shareholders equity is not available to the common shareholders of Primus Guaranty. See note 5 of these notes to condensed consolidated financial statements for further discussion.

Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

Although these CLOs are consolidated, the assets of the CLOs are not available to Primus Guaranty for its general operations or in satisfaction of its debt obligations. Primus Guaranty does not have any rights to or ownership of these assets. The assets of the CLOs are restricted solely to satisfy the liabilities of the CLOs. Similarly, Primus Guaranty does not have any obligation to settle the liabilities of the CLOs. In addition, Primus Guaranty investments in the CLOs and management fees receivable will be eliminated in consolidation. Primus Guaranty has no contractual obligation to fund or provide other financial support to any CLO.

Appropriated Retained Earnings from CLO Consolidations

As a result of the adoption of ASC Topic 810, *Consolidation*, the Company established an appropriated retained earnings from CLO consolidations account in the shareholders equity section on the condensed consolidated statements of financial condition. Upon consolidation of the CLOs under management, the Company elected fair value option treatment under ASC Topic 825-10-25 to measure the CLO loans (including unfunded loan commitments) and securities and the CLO notes. The Company has determined that measurement of the CLO notes issued by CLOs at fair value better correlates with the value of the CLO loans and securities held by CLOs, which are held to provide the cash flows for the note obligations. Upon initial consolidation of the CLOs on January 1, 2010, the difference between the fair value amounts of the CLO assets and CLO liabilities was recorded in appropriated retained earnings from CLO consolidations as a cumulative effect adjustment. Subsequent to January 1, 2010, the net income or loss attributable to non-parent interests in the CLOs for each period will also be reflected in this account.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest, including CLOs, for which Primus Guaranty is deemed to be the primary beneficiary. All significant intercompany balances have been eliminated.

Other Recent Accounting Pronouncements

In January 2010, the FASB issued ASU No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820) Improving Disclosures about Fair Value Measurements*. ASU No. 2010-06 provides amended disclosure requirements related to fair value measurements, including transfers in and out of Levels 1 and 2 and activity in Level 3 under the fair value hierarchy. ASU No. 2010-06 is effective for financial statements issued for reporting periods beginning after December 15, 2009 for certain disclosures and for reporting periods beginning after December 15, 2010 for certain additional disclosures regarding activity in Level 3 fair value measurements. Since these amended principles require only additional disclosures concerning fair value measurements, adoption of ASU No. 2010-06 will not affect the Company s financial condition, results of operations or cash flows.

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Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

3. Investments

The following tables summarize the composition of the Company s investments at June 30, 2010 and December 31, 2009 (in thousands):

	June 30, 2010			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Available-for-sale:				
Corporate debt securities	$ 309,781	$ 4,409	$ (419)	$ 313,771
ABS bonds	1,265		(68)	1,197
Total available-for-sale	311,046	4,409	(487)	314,968
Trading:				
Corporate loans and debt securities	53,535	233	(422)	53,346
Total trading	53,535	233	(422)	53,346
Held-to-maturity:				
Certificate of deposit	170			170
Total held-to-maturity	170			170
Total investments	$ 364,751	$ 4,642	$ (909)	$ 368,484

	December 31, 2009			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Available-for-sale:				
Corporate debt securities	$ 271,809	$ 1,784	$ (662)	$ 272,931
Investments in CLOs under management	203	1,062		1,265
ABS bonds	84		(5)	79
Total available-for-sale	272,096	2,846	(667)	274,275
Held-to-maturity:				
Certificate of deposit	169			169
Total held-to-maturity	169			169
Total investments	$ 272,265	$ 2,846	$ (667)	$ 274,444

The Company s investments in the subordinated notes of the CLOs with a fair value of $8.7 million as of June 30, 2010 have been eliminated in consolidation.

The Company s trading account assets of $53.3 million relate to the two funds launched by the Company during the first quarter of 2010. All securities transactions of the two funds are cleared by banking and securities firms, pursuant to customer agreements. Additional liquidity is available for the Primus Absolute Return Credit Master Fund, Ltd. (the Fund) from the brokers using investments in securities and derivatives as collateral. Included in Other liabilities is a margin balance of $15.0 million as of June 30, 2010. The Fund is charged interest at fluctuating rates based on the prevailing broker call rate. The Fund s trading securities are held by the broker and are pledged to the broker on terms which permit the broker to sell or repledge to others, subject to certain limitations. See note 7 of these notes to condensed consolidated financial statements for further discussion.

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Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

As of June 30, 2010, approximately $308.7 million, or approximately 98%, of the corporate debt securities will mature before November 2014. The ABS bonds are estimated to mature between 2011 and 2025, although the actual maturity may differ.

As of June 30, 2010, the Company has a restricted investment within restricted cash and investments, which is comprised of a corporate note issued by a counterparty. At June 30, 2010, the carrying value of this held to maturity restricted investment was $37.1 million.

The tables below summarize the fair value of available-for-sale investments that have been in a continuous unrealized loss position for less than 12 months and for 12 months or more at June 30, 2010 and December 31, 2009 (in thousands). See note 6 of notes to these condensed consolidated financial statements for the fair value of the financial instruments held by the CLOs under management.

	June 30, 2010					
	Securities with Unrealized Losses					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Corporate debt securities	$ 90,048	$ (356)	$ 941	$ (63)	$ 90,989	$ (419)
ABS bonds	1,197	(68)			1,197	(68)
Total	$ 91,245	$ (424)	$ 941	$ (63)	$ 92,186	$ (487)

	December 31, 2009					
	Securities with Unrealized Losses					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Corporate debt securities	$ 121,983	$ (405)	$ 2,248	$ (257)	$ 124,231	$ (662)
ABS bonds	79	(5)			79	(5)
Total	$ 122,062	$ (410)	$ 2,248	$ (257)	$ 124,310	$ (667)

The Company makes an assessment to determine whether unrealized losses reflect declines in value of securities that are other-than-temporarily impaired. The Company considers many factors, including the length of time and significance of the decline in fair value of the investment; the intent to sell the investment or if it is more likely than not it will be required to sell the investment before recovery in fair value; recent events specific to the issuer or industry; credit ratings and asset quality of collateral structure; and any significant changes in estimated cash flows of the investment. If the Company, based on its evaluation, determines that the credit related impairment is other-than-temporary, the carrying value of the security is written down to fair value and the unrealized loss is recognized through a charge to earnings in the condensed consolidated statements of operations.

During the three and six months ended June 30, 2010, it was determined that there were no credit related impairment losses on investments.

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Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

4. Credit Swaps

Net Credit Swap Revenue (Loss)

Net credit swap revenue (loss) as presented in the condensed consolidated statements of operations comprises changes in the fair value of credit swaps, realized gains or losses on the termination of credit swaps sold, before their stated maturity, realized losses on credit events and premium income or expense. The realization of gains or losses on the termination of credit swaps or credit events generally will result in a reduction in unrealized gains or losses and accrued premium at the point in time realization occurs.

Credit swaps sold by Primus Financial on a single corporate or sovereign issuer, specified as a Reference Entity are referred to as single name credit swaps. Primus Financial also has sold credit swaps referencing portfolios containing obligations of multiple Reference Entities, which are referred to as tranches. Additionally, Primus Financial has sold credit swaps on asset-backed securities, which are referred to as CDS on ABS. These asset-backed securities reference residential mortgage-backed securities.

The table below presents the components of net credit swap revenue (loss) for the three and six months ended June 30, 2010 and 2009 (in thousands).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Net premiums earned	$ 15,234	$ 22,234	$ 31,670	$ 44,703
Net realized losses on credit swaps	(10,094)	(2,975)	(66,136)	(37,453)
Net unrealized gains (losses) on credit swaps	(194,848)	552,624	(67,712)	675,514
Total net credit swap revenue (loss)	$ (189,708)	$ 571,883	$ (102,178)	$ 682,764

Credit Events and Terminations of Credit Swaps

The table below presents the components of gross realized losses recorded by Primus Financial, related to risk mitigation transactions and credit events for the three and six months ended June 30, 2010 and 2009, respectively, as discussed further below (in thousands).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Realized losses on single name credit swaps	$ (10,011)	$	$ (29,234)	$ (9,850)
Realized losses on tranches	(83)		(35,083)	
Realized losses on CDS on ABS		(3,000)	(1,819)	(27,628)
Total realized losses	$ (10,094)	$ (3,000)	$ (66,136)	$ (37,478)

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Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

Single Name Credit Swaps

During the three months ended June 30, 2010, Primus Financial terminated additional credit swaps sold referencing Ambac Financial Group, Inc. with a total notional amount of $15.0 million and paid the counterparties termination fees of approximately $8.5 million. In addition, Primus Financial terminated credit swaps sold referencing MBIA Inc. with a notional amount of $10.0 million and paid the counterparty approximately $1.5 million.

During the six months ended June 30, 2010, Primus Financial terminated credit swaps sold referencing Ambac Financial Group, Inc. with a total notional amount of $85.0 million and paid the counterparties termination fees of approximately $27.7 million.

During the six months ended June 30, 2009, a credit event on one Reference Entity, Idearc Inc., occurred in Primus Financial s credit swap portfolio with a total notional amount of $10.0 million. As a result, Primus Financial recorded a realized loss of approximately $9.9 million, net of recovery values, related to such credit event in the condensed consolidated results of operations.

Tranches

On February 11, 2010, Primus Financial completed a portfolio repositioning transaction with a bank counterparty. In connection with the transaction, Primus Financial terminated three tranche transactions of $300.0 million total notional principal and paid the counterparty a termination fee of $35.0 million and as a result recognized a realized loss for the six months ended June 30, 2010.

CDS on ABS

During the three months ended June 30, 2010 and 2009, Primus Financial recorded realized losses of zero and $3.0 million, respectively, net of bond recovery values, which had been subject to credit events on its CDS on ABS portfolio.

During the six months ended June 30, 2010 and 2009, Primus Financial recorded realized losses of $1.8 million and $27.6 million, respectively, net of bond recovery values, which had been subject to credit events on its CDS on ABS portfolio.

Counterparty Default Lehman Brothers Special Financing Inc.

Primus Financial had entered into credit swap transactions with Lehman Brothers Special Financing Inc. (LBSF), pursuant to an ISDA Master Agreement. At the time of these transactions, LBSF was an indirect subsidiary of Lehman Brothers Holdings Inc. (LBH), and LBH was the credit support provider under these transactions. During and subsequent to the end of the third quarter of 2008, LBSF suffered a number of events of default under the ISDA Master Agreement, including bankruptcy, failure to pay premiums when due and bankruptcy of its credit support provider. Primus Financial has not designated any early termination date under the ISDA Master Agreement, and accordingly, intends to continue the credit swap agreements. Under relevant accounting standards, Primus Financial continues to carry outstanding credit swaps at their fair value. LBSF has been obligated to pay approximately $14.4 million in premiums on its credit swap transactions since the third quarter of 2008, but has failed to do so. As a consequence, Primus Financial did not recognize premium income of approximately $1.5 million and $1.8 million on the credit swaps with LBSF during the three months ended June 30, 2010 and 2009, respectively. Primus Financial did not recognize premium income of approximately $3.1 million and $3.6 million on the credit swaps with LBSF during the six months ended June 30, 2010 and 2009, respectively. The cumulative amount of $14.4 million due, but unpaid, was netted against the unrealized losses on the credit swaps with LBSF outstanding at June 30, 2010.

Primus Guaranty, Ltd.
Notes to Condensed Consolidated Financial Statements (Unaudited)

Credit Swap Portfolio Information

The tables below summarize, by S&P credit rating of Reference Entities and of counterparties, the notional amounts and unrealized gain or (loss) for fair values of credit swap transactions outstanding as of June 30, 2010 and December 31, 2009 (in thousands) (excluding a CDS index transaction with fair value of $114 thousand). If a Reference Entity is not rated by S&P, an equivalent credit rating is obtained from another Nationally Recognized Statistical Rating Organization, if available. Transactions with LBSF are included in the following tables and are noted as with a non rated counterparty.

	June 30, 2010		December 31, 2009	
Rating Category	**Notional Amount**	**Fair Value**	**Notional Amount**	**Fair Value**
By Single Name Reference Entity/Tranche				
Credit Swaps Sold-Single Name:				
AAA	$ 221,714	$ (4,736)	$ 347,963	$ (5,765)
AA	1,229,138	(15,588)	1,449,137	(7,442)
A	4,193,127	(30,695)	5,656,180	(11,217)
BBB	3,855,361	(23,212)	4,730,878	(8,438)
BB	355,275	(8,629)	598,908	(16,584)
B	76,119	(4,759)	189,284	(2,726)
CCC	70,000	(2,863)	85,000	(8,864)
CC	20,000	(11,841)	213,087	(106,143)
D	38,500	(21,040)	41,000	(21,868)
Non rated	243,780	(62,166)	56,482	(628)
Total	$ 10,303,014	$ (185,529)	$ 13,367,919	$ (189,675)
Credit Swaps Sold-Tranche:				
AAA	$ 2,650,000	$ (324,440)	$ 1,575,000	$ (120,112)
AA	200,000	(22,926)	1,275,000	(122,406)
A	300,000	(57,042)		
BBB	450,000	(86,996)	750,000	(103,601)
BB	150,000	(30,577)	100,000	(12,997)
B			100,000	(17,373)
CCC			200,000	(45,393)
C			100,000	(53,802)
Non rated	50,000	(28,997)		
Total	$ 3,800,000	$ (550,978)	$ 4,100,000	$ (475,684)
CDS on ABS:				
BBB	$ 736	$ (445)	$ 3,682	$ (2,880)
B			5,000	(4,357)
CCC	18,000	(14,321)	13,000	(10,534)
CC	10,000	(9,009)	10,000	(8,989)

Total	$ 28,736	$ (23,775)	$ 31,682	$ (26,760)

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Primus Guaranty, Ltd.
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	June 30, 2010		December 31, 2009	
Rating Category	**Notional Amount**	**Fair Value**	**Notional Amount**	**Fair Value**
By Single Name Reference Entity/Tranche				
Credit Swaps Purchased-Single Name:				
A	$ (4,120)	$ 212	$ (4,120)	$ 25
CC	(4,040)	2,545	(4,040)	2,396
Total	$ (8,160)	$ 2,757	$ (8,160)	$ 2,421
By Counterparty Buyer / (Seller)				
Credit Swaps Sold-Single Name:				
AA	$ 2,650,697	$ (22,570)	$ 3,263,322	$ (25,340)
A	5,929,464	(119,615)	8,888,189	(136,293)
BBB	20,000	11		
B	557,068	(9,787)		
Non rated	1,145,785	(33,568)	1,216,408	(28,042)
Total	$ 10,303,014	$ (185,529)	$ 13,367,919	$ (189,675)
Credit Swaps Sold-Tranche:				
AA	$ 1,850,000	$ (279,884)	$ 1,850,000	$ (199,745)
A	1,500,000	(184,098)	1,800,000	(210,057)
BBB	450,000	(86,996)	450,000	(65,882)
Total	$ 3,800,000	$ (550,978)	$ 4,100,000	$ (475,684)
CDS on ABS:				
A	$ 10,000	$ (7,972)	$ 26,682	$ (22,380)
B	13,736	(11,363)		
Non rated	5,000	(4,440)	5,000	(4,380)
Total	$ 28,736	$ (23,775)	$ 31,682	$ (26,760)
Credit Swaps Purchased-Single Name:				
A	$ (8,160)	$ 2,757	$ (8,160)	$ 2,421
Total	$ (8,160)	$ 2,757	$ (8,160)	$ 2,421

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Primus Guaranty, Ltd.
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The table below shows the geographical distribution of the credit swap portfolio by domicile of the Reference Entity and domicile of the counterparty (including transactions with LBSF), as of June 30, 2010 and December 31, 2009 (in thousands).

	June 30, 2010		December 31, 2009	
Country of Domicile	**Notional Amount**	**Fair Value**	**Notional Amount**	**Fair Value**
Credit Swaps Sold-Single Name				
By Reference Entity:				
North America	$ 5,390,547	$ (122,833)	$ 6,836,087	$ (161,513)
Europe	4,405,467	(57,615)	5,869,832	(24,249)
Asia-Pacific	437,000	(4,737)	522,000	(3,714)
Others	70,000	(344)	140,000	(199)
Total	$ 10,303,014	$ (185,529)	$ 13,367,919	$ (189,675)
By Counterparty:				
North America	$ 4,965,070	$ (74,799)	$ 6,359,144	$ (76,784)
Europe	5,235,944	(110,554)	6,891,775	(111,894)
Asia-Pacific	102,000	(176)	117,000	(997)
Total	$ 10,303,014	$ (185,529)	$ 13,367,919	$ (189,675)
Credit Swaps Sold -Tranche				
By Counterparty:				
North America	$ 600,000	$ (57,914)	$ 600,000	$ (47,099)
Europe	3,200,000	(493,064)	3,500,000	(428,585)
Total	$ 3,800,000	$ (550,978)	$ 4,100,000	$ (475,684)
CDS on ABS				
By Reference Entity:				
North America	$ 28,736	$ (23,775)	$ 31,682	$ (26,760)
Total	$ 28,736	$ (23,775)	$ 31,682	$ (26,760)
By Counterparty:				
North America	$ 18,736	$ (15,803)	$ 21,682	$ (18,830)
Europe	10,000	(7,972)	10,000	(7,930)
Total	$ 28,736	$ (23,775)	$ 31,682	$ (26,760)

Credit Swaps Purchased-Single Name								
By Reference Entity:								
North America	$	(8,160)	$	2,757	$	(8,160)	$	2,421
Total	$	(8,160)	$	2,757	$	(8,160)	$	2,421
By Counterparty:								
Europe	$	(8,160)	$	2,757	$	(8,160)	$	2,421