

American Capital Agency Corp
Form 10-Q/A
July 12, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

- x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2010

OR

- .. TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission file number 001-34057

AMERICAN CAPITAL AGENCY CORP.

(Exact name of registrant as specified in its charter)

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Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

26-1701984
(I.R.S. Employer
Identification No.)

2 Bethesda Metro Center, 14th Floor

Bethesda, Maryland 20814

(Address of principal executive offices)

(301) 968-9300

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports 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 earlier 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 definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

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

Accelerated filer

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

The number of shares of the issuer's common stock, \$0.01 par value, outstanding as of April 30, 2010, was 26,760,295.

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AMERICAN CAPITAL AGENCY CORP.

EXPLANATORY NOTE

On May 3, 2010, we filed our Quarterly Report on Form 10-Q for the quarter ended March 31, 2010 (the "Original Filing"), with the Securities and Exchange Commission (the "SEC"). The Original Filing is being amended to include certifications of the Company's CEO and CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, filed as exhibits hereto, inadvertently omitted from the Original Filing.

This Amendment does not change any information presented in the Original Filing other than adding the certifications noted in the preceding paragraph, and has not been updated to reflect events occurring subsequent to the date of the Original Filing. This Amendment speaks as of the date of the Original Filing, except for certain certifications, which speak as of their respective dates and the filing date of this Amendment. This Amendment should be read in conjunction with our filings made with the SEC subsequent to the filing of the Original Filing, including any amendments to those filings.

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Table of Contents**ITEM 1. Financial Statements****AMERICAN CAPITAL AGENCY CORP.****CONSOLIDATED BALANCE SHEETS****(in thousands, except per share data)**

	March 31, 2010 (Unaudited)	December 31, 2009
Assets:		
Agency securities, at fair value (including pledged assets of \$4,855,633 and \$4,136,596, respectively)	\$ 5,240,254	\$ 4,300,115
Cash and cash equivalents	105,264	202,803
Restricted cash	26,630	19,628
Interest receivable	26,168	22,872
Derivative assets, at fair value	8,736	11,960
Receivable for agency securities sold	273,832	47,076
Principal payments receivable	88,474	20,473
Other assets	631	757
Total assets	\$ 5,769,989	\$ 4,625,684
Liabilities:		
Repurchase agreements	\$ 4,651,115	\$ 3,841,834
Payable for agency securities purchased	436,100	180,345
Accrued interest payable	2,265	2,007
Derivative liabilities, at fair value	28,689	17,798
Dividend payable	37,465	34,050
Due to Manager	843	1,662
Accounts payable and other accrued liabilities	393	1,166
Total liabilities	5,156,870	4,078,862
Stockholders equity:		
Preferred stock, \$0.01 par value; 10,000 shares authorized, 0 shares issued and outstanding, respectively		
Common stock, \$0.01 par value; 150,000 shares authorized, 26,760 and 24,322 shares issued and outstanding, respectively	268	243
Additional paid-in capital	569,595	507,465
Retained earnings	35,625	19,940
Accumulated other comprehensive income	7,631	19,174
Total stockholders equity	613,119	546,822
Total liabilities and stockholders equity	\$ 5,769,989	\$ 4,625,684

See accompanying notes to consolidated financial statements.

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AMERICAN CAPITAL AGENCY CORP.
CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME
(unaudited)
(in thousands, except per share data)

	For the three months ended March 31,	
	2010	2009
Interest income:		
Interest income	\$ 38,797	\$ 22,351
Interest expense	15,510	8,129
Net interest income	23,287	14,222
Other income, net:		
Gain on sale of agency securities, net	27,408	4,818
Gain (loss) on derivative instruments, net	5,920	(358)
Total other income, net	33,328	4,460
Expenses:		
Management fees	1,784	903
General and administrative expenses	1,681	1,468
Total expenses	3,465	2,371
Net income	\$ 53,150	\$ 16,311
Net income per common share basic and diluted	\$ 2.13	\$ 1.09
Weighted average number of common shares outstanding basic and diluted	25,002	15,005
Dividends declared per common share	\$ 1.40	\$ 0.85
Comprehensive income:		
Net income	\$ 53,150	\$ 16,311
Other comprehensive (loss) income:		
Unrealized gain on available-for-sale securities, net	1,933	29,284
Unrealized loss on derivative instruments, net	(13,476)	(2,038)
Other comprehensive (loss) income	(11,543)	27,246
Comprehensive income	\$ 41,607	\$ 43,557

See accompanying notes to consolidated financial statements.

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AMERICAN CAPITAL AGENCY CORP.

CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

(in thousands)

	Preferred Stock		Common Stock			Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount	Shares	Amount	Additional Paid-in Capital			
Balance, December 31, 2009		\$	24,322	\$ 243	\$ 507,465	\$ 19,940	\$ 19,174	\$ 546,822
Net income						53,150		53,150
Other comprehensive income (loss):								
Unrealized gain on available- for-sale securities, net							1,933	1,933
Unrealized loss on derivative instruments, net							(13,476)	(13,476)
Issuance of common stock			2,434	24	62,114			62,138
Issuance of restricted common stock			4	1				1
Stock-based compensation					16			16
Common dividends declared						(37,465)		(37,465)
Balance, March 31, 2010 (Unaudited)		\$	26,760	\$ 268	\$ 569,595	\$ 35,625	\$ 7,631	\$ 613,119

See accompanying notes to consolidated financial statements.

Table of Contents**AMERICAN CAPITAL AGENCY CORP.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(unaudited)****(in thousands)**

	For the three months ended March 31,	
	2010	2009
Operating activities:		
Net income	\$ 53,150	\$ 16,311
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of agency securities premiums and discounts, net	12,259	3,449
Amortization of interest rate swap termination fees	3,676	329
Ineffectiveness of derivative instruments	192	(586)
Stock-based compensation	17	7
Gain on sale of agency securities, net	(27,408)	(4,818)
Gain on derivative instruments, net	(6,112)	
Decrease (increase) in interest receivable	1,732	(2,062)
Decrease in other assets	126	130
Increase (decrease) in accrued interest payable	258	(2,236)
Decrease in due to Manager	(819)	(49)
(Decrease) increase in accounts payable and other accrued liabilities	(773)	105
Net cash provided by operating activities	36,298	10,580
Investing activities:		
Purchases of agency securities	(3,056,410)	(1,631,281)
Proceeds from sale of agency securities	1,916,207	1,019,862
Net proceeds from derivative instruments not designated as qualifying hedges	794	
Principal collections on agency securities	175,205	126,492
Net cash used in investing activities	(964,204)	(484,927)
Financing activities:		
Cash dividends paid	(34,050)	(18,006)
Increase in restricted cash	(7,002)	(6,476)
Payments made on interest rate swap terminations		(6,617)
Proceeds from repurchase arrangements, net	809,281	503,208
Net proceeds from common stock issuances	62,138	
Net cash provided by financing activities	830,367	472,109
Net change in cash and cash equivalents	(97,539)	(2,238)
Cash and cash equivalents at beginning of period	202,803	56,012
Cash and cash equivalents at end of period	\$ 105,264	\$ 53,774

See accompanying notes to consolidated financial statements.

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AMERICAN CAPITAL AGENCY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1. Unaudited Interim Consolidated Financial Statements

The interim consolidated financial statements of American Capital Agency Corp. (together with its consolidated subsidiary, is referred throughout this report as the Company , we , us and our) are prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Article 10 of Regulation S-X. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

Our unaudited consolidated financial statements include the accounts of our wholly-owned subsidiary, American Capital Agency TRS, LLC. Significant intercompany accounts and transactions have been eliminated. In the opinion of management, all adjustments, consisting solely of normal recurring accruals, necessary for the fair presentation of financial statements for the interim period have been included. The current period's results of operations are not necessarily indicative of results that ultimately may be achieved for the year. There has been no activity in American Capital Agency TRS, LLC during the three months ended March 31, 2010 and 2009.

Note 2. Organization

We were organized in Delaware on January 7, 2008, and commenced operations on May 20, 2008 following the completion of our initial public offering (IPO). Our common stock is traded on The NASDAQ Global Select Market under the symbol AGNC .

We have elected to be taxed as a real estate investment trust (REIT) under the Internal Revenue Code of 1986, as amended (the Code). As such, we are required to distribute annually 90% of our taxable net income. As long as we qualify as a REIT, we will generally not be subject to U.S. federal or state corporate taxes on our taxable net income to the extent that we distribute all of our annual taxable net income to our stockholders. We are managed by American Capital Agency Management, LLC (our Manager), a subsidiary of a wholly-owned portfolio company of American Capital, Ltd. (American Capital).

We earn income primarily from investing in residential mortgage pass-through securities and collateralized mortgage obligations (CMOs) on a leveraged basis. These investments consist of securities for which the principal and interest payments are guaranteed by U.S. Government-sponsored entities such as the Federal National Mortgage Association, or Fannie Mae, and the Federal Home Loan Mortgage Corporation, or Freddie Mac, or by a U.S. Government agency such as the Government National Mortgage Association, or Ginnie Mae. We refer to these types of securities as agency securities and the specific agency securities in which we invest as our investment portfolio.

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Our principal goal is to generate net income for distribution to our stockholders through regular quarterly dividends from our net interest income, which is the spread between the interest income earned on our interest earning assets and the interest costs of our borrowings and hedging activities, and realized gains on our investments. We fund our investments primarily through short-term borrowings structured as repurchase agreements.

Note 3. Summary of Significant Accounting Policies

Investments in Agency Securities

Accounting Standards Codification (ASC) Topic 320, *Investments Debt and Equity Securities* (ASC 320), requires that at the time of purchase, we designate a security as held-to-maturity, available-for-sale or trading depending on our ability and intent to hold such security to maturity. Securities classified as trading and

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

available-for-sale are reported at fair value, while securities classified as held-to-maturity are reported at amortized cost. We may, from time to time, sell any of our agency securities as part of our overall management of our investment portfolio. Accordingly, we typically designate our agency securities as available-for-sale. All securities classified as available-for-sale are reported at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income (loss) (OCI), a component of stockholders' equity. We determine the cost of the security and the amount to reclassify out of accumulated OCI into earnings based on the specific identification method.

Interest-only strips represent our right to receive a specified proportion of the contractual interest flows of specific agency and CMO securities. Interest-only strips are measured at fair value through earnings in gain (loss) on derivative instruments, net in our consolidated statements of operations and comprehensive income. Our investments in interest-only strips are included in agency securities, at fair value on the accompanying consolidated balance sheet.

We evaluate securities for other-than-temporary impairment (OTTI) on at least a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. Based on the criteria in ASC 320, the determination of whether a security is other-than-temporarily impaired involves judgments and assumptions based on subjective and objective factors. When an agency security is impaired, an OTTI is considered to have occurred if (i) we intend to sell the agency security or (ii) it is more likely than not that we will be required to sell the agency security before recovery of its amortized cost basis. If we intend to sell the security or if it is more likely than not that we will be required to sell the agency security before recovery of its amortized cost basis, the entire amount of the impairment loss is recognized in earnings as an unrealized loss and the cost basis of the security is adjusted.

We did not recognize any OTTI charges on any of our agency securities for the three months ended March 31, 2010 and 2009.

Derivative Instruments

We maintain an interest rate risk management strategy under which we use derivative financial instruments to manage the adverse impact of interest rate changes on the value of our investment portfolio as well as our cash flows. In particular we attempt to mitigate the risk of the cost of our short-term variable rate liabilities increasing at a faster rate than the earnings of our long-term assets during a period of rising interest rates. The principal derivative instruments that we use are interest rate swaps, options to enter into interest rate swap agreements (interest rate swaptions), to-be-announced agency securities (TBAs), options and futures. We account for derivatives in accordance with ASC Topic 815, *Derivatives and Hedging* (ASC 815). ASC 815 requires an entity to recognize all derivatives as either assets or liabilities in the balance sheet and to measure those instruments at fair value.

The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives that are intended to hedge exposure to variability in expected future cash flows are considered cash flow hedges. For derivatives designated in qualifying cash flow hedging relationships, the effective portion of the fair value adjustments are initially recorded in OCI

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(a component of stockholders' equity) and reclassified to income at the time that the hedged transactions affect earnings. The ineffective portion of the fair value adjustments is recognized in gain (loss) on derivative instruments, net immediately. When the underlying hedged transaction ceases to exist, all changes in the fair value of the instrument are included in gain (loss) on derivative instruments, net for each period until the derivative instrument matures or is settled. Any amounts that have been previously recorded in accumulated OCI may need to be reclassified to net income. For derivatives not designated in hedging relationships under ASC 815, the fair value adjustments are

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

recorded in gain (loss) on derivative instruments, net. Derivatives in a gain position are reported as derivative assets at fair value, and derivatives in a loss position are reported as derivative liabilities at fair value in our consolidated balance sheet. Any gain (loss) on derivative instruments is included in the operating section in our consolidated statement of cash flows.

We use interest rate swaps to hedge the variable cash flows associated with short-term borrowings made under our repurchase agreement facilities. We generally enter into such derivatives with the intention of qualifying for hedge accounting.

We may purchase interest rate swaptions to help mitigate the potential impact of large increases or decreases in interest rates on the performance of our investment portfolio (referred to as convexity risk). The interest rate swaptions provide us the option to enter into an interest rate swap agreement for a predetermined notional amount, stated term and pay and receive interest rates in the future. The premium paid for interest rate swaptions is reported as an asset in our consolidated balance sheets. The premium is valued at an amount equal to the fair value of the swaption that would have the effect of closing the position. The difference between the premium and the fair value of the swaption is reported in gain (loss) on derivative instruments, net in our consolidated statement of operations and comprehensive income. When a swaption expires unexercised, a realized loss is reported in our consolidated statement of operations and comprehensive income equal to the premium paid. When we exercise a swaption, a realized gain or loss is reported in our consolidated statement of operations and comprehensive income equal to the difference between the fair value of the underlying interest rate swap and the premium paid.

A TBA security is a futures contract for the purchase or sale of agency securities at a predetermined price, face amount, issuer, coupon and stated maturity on an agreed-upon future date. The specific agency securities delivered into the contract upon the settlement date, published each month by the Securities Industry and Financial Markets Association, are not known at the time of the transaction. TBA securities are exempt from ASC 815 if there is no other way to purchase or sell that security, delivery of that security and settlement will occur within the shortest period possible for that type of security and it is probable at inception and throughout the term of the individual contract that physical delivery of the security will occur. For the TBA security contracts that we have entered into, we have not asserted that physical settlement is probable and therefore, we did not designate such forward commitments as hedging instruments. Accordingly, all realized and unrealized gains and losses are recognized in our consolidated statement of operations in the line item gain (loss) on derivative instruments, net.

We may purchase put and call options on TBA securities to hedge against short-term changes in interest rates. Under a purchased put option, we have the right to sell the counterparty a specified TBA security at a predetermined price on the option exercise date in exchange for a premium at execution. Under a purchased call option, we have the right to purchase from the counterparty a specified TBA security at a predetermined price on the option exercise date in exchange for a premium at execution. The premium paid for a put or call option is reported as an asset in our consolidated balance sheets. The premium is valued at an amount equal to the fair value of the option that would have the effect of closing the position. The difference between the premium and the fair value of the option is reported in gain (loss) on derivative instruments, net in our consolidated statement of operations and comprehensive income. When a purchased put or call option expires unexercised, a realized loss is reported in our consolidated statement of operations equal to the premium paid. When a purchased put or call option is exercised, a realized gain or loss is reported in our consolidated statement of operations equal to the difference between the premium paid and the fair value of the exercised put or call option. In addition, a derivative asset is recorded in our consolidated balance sheet for the TBA security resulting from the put or call option exercise.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

We may also write put and call options on TBA securities to hedge against short-term changes in interest rates. Under a written put option, the counterparty has the right to sell us a specified TBA security at a predetermined price on the option exercise date in exchange for a premium at execution. Under a written call option, the counterparty has the right to purchase from us a specified TBA security at a predetermined price on the option exercise date in exchange for a premium at execution. The premium received from writing a put or call option is reported as a liability in our consolidated balance sheets. The premium is valued at an amount equal to the fair value of the option that would have the effect of closing the position. The difference between the premium and the fair value of the option is reported in gain (loss) on derivative instruments, net in our consolidated statement of operations and comprehensive income. When a written put or call option expires unexercised, a realized gain is reported in our consolidated statement of operations equal to the premium received. When we terminate a written put or call option, a realized gain or loss is reported in our consolidated statement of operations equal to the difference between the termination payment and the premium received. When a written put or call option is exercised, a realized gain or loss is reported in our consolidated statement of operations equal to the difference between the premium received and the fair value of the exercised put or call option. In addition, a derivative asset or liability is recorded in our consolidated balance sheet for the TBA security resulting from the put or call option exercise.

We may enter into a forward commitment to purchase or sell specified agency securities as a hedge against short-term changes in interest rates. Contracts for the purchase or sale of specified agency securities are accounted for as derivatives if the delivery of the specified agency security and settlement extends beyond the shortest period possible for that type of security. We may designate the forward commitment as a qualifying cash flow hedge if at the time of the purchase or sale of the security, and throughout the term of the individual contract, it is probable that physical delivery of the security will occur. Realized and unrealized gains and losses associated with forward commitments not designated as hedging instruments are recognized in our consolidated statement of operations in the line item gain (loss) on derivative instruments, net.

We estimate the fair value of interest rate swaps and interest rate swaptions based on the estimated net present value of the future cash flows using a forward interest rate yield curve in effect as of the measurement period, adjusted for non-performance risk based on our credit risk and our counterparty's credit risk. We consider the impact of any collateral requirements, credit enhancements or netting arrangements on credit risk. TBA securities and forward settling contracts to purchase or sell securities are valued using third-party pricing services. These third-party pricing services use pricing models that incorporate such factors as coupons, prepayment speeds, spread to the Treasury and swap curves, convexity, duration, periodic and life caps and credit enhancement.

The use of derivatives creates exposure to credit risk relating to potential losses that could be recognized in the event that the counterparties to these instruments fail to perform their obligations under the contracts. We minimize this risk by limiting our counterparties to major financial institutions with acceptable credit ratings and monitoring positions with individual counterparties.

Variable Interest Entities

In June 2009, the FASB issued SFAS No. 167, *Amendments to FASB Interpretation No. 46(R)* (SFAS No. 167). In December 2009, the FASB issued Accounting Standards Update (ASU) 2009-17, *Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*, which codified SFAS No. 167 in FASB ASC Topic 810, *Consolidation* (ASC 810). ASC 810, as amended by ASU 2009-17, revises the

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evaluation of whether entities represent variable interest entities (VIEs) and requires a qualitative assessment in determining the primary beneficiary of a VIE. Further, ASC 2009-17 requires ongoing assessments of control over such entities as well as additional disclosures for entities that have variable interests in VIEs. The amendments significantly affect the overall consolidation analysis under ASC 810 and changes the way entities

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

account for securitizations and special purpose entities as a result of the elimination of the qualifying special purpose entity (QSPE) scope exemption from ASC 810. The requirements of ASC 810 as they relate to ASU 2009-17 were effective for us as of January 1, 2010.

Prior to our adoption of ASC 810, as amended by ASU 2009-17, the CMO trusts we invested in were exempt from consolidation. Upon our adoption of ASC 810, as amended by ASU 2009-17, we evaluated such CMO trusts and determined that they are VIEs and our investments are variable interests. We consolidate a CMO trust if we are its primary beneficiary, that is, if we have a variable interest (or combination of variable interests) that provides us with a controlling financial interest in the CMO trust. An entity is deemed to have a controlling financial interest if the entity has the power to direct the activities of a VIE that most significantly impacts the VIE's economic performance and the obligation to absorb losses of or right to receive benefits from the VIE that could potentially be significant to the VIE. In determining if we have a controlling financial interest, we evaluate whether we share the power to control the selection of financial assets transferred to the CMO trust with an unrelated party. While we believe there is shared power in the selection of the assets (i.e. both us and the unrelated party must consent to the transfer of such assets to the CMO trust), if our economic interest in the CMO trust is disproportionate to the shared power, we would be deemed to be the primary beneficiary.

As of and during the three months ended March 31, 2010, we were the primary beneficiary of certain CMO trusts in which we hold a variable interest. However, the impact of consolidating such CMO trusts was immaterial to our financial states as of and for the period then ended. Our investments in CMO trusts are included in agency securities on the accompanying consolidated balance sheets.

Recent Accounting Pronouncements

In June 2009, the FASB issued SFAS No. 166, *Accounting for Transfers of Financial Assets - an amendment of FASB Statement No. 140* (SFAS No. 166). In December 2009, the FASB issued Accounting Standards Update (ASU) 2009-16, *Accounting for Transfers of Financial Assets* which codified SFAS No. 166 in FASB ASC Topic 860, *Transfers and Servicing* (ASC 860). SFAS No. 166 amends the derecognition guidance in SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, eliminates the concept of a qualifying special-purpose entity (QSPE) and requires more information about transfers of financial assets, including securitization transactions as well as a company's continuing exposure to the risks related to transferred financial assets. AGNC adopted the requirements of ASC 860, as they relate to SFAS No. 166, on January 1, 2010. The requirements will be effective for financial asset transfers occurring after January 1, 2010 and for substantive changes to transfers of financial assets that occurred prior to January 1, 2010.

In January 2010, the FASB issued ASU No 2010-06, *Improving Disclosures about Fair Value Measurements* (ASU 2010-06), which amended FASB ASC Topic 820, *Fair Value Measurements and Disclosures* (ASC 820), to require a number of additional disclosures regarding fair value measurements, including the amount of transfers between Levels 1 and 2 of the fair value hierarchy, the reasons for transfers in or out of Level 3 of the fair value hierarchy and activity for recurring Level 3 measures. ASU 2010-06 also clarifies certain existing disclosure requirements related to the level at which fair value disclosures should be disaggregated and the requirement to provide disclosures about the valuation techniques and inputs used in determining the fair value of assets or liabilities classified as Levels 2 or 3. The ASU is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures related to the activity in Level 3 fair value measurements

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which are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. Early adoption is permitted. We adopted the requirements of ASU 2010-06 in the first quarter of 2010 and the adoption did not have a material effect on our consolidated financial statements.

In February 2010, the FASB issued ASU No. 2010-09, *Amendments to Certain Recognition and Disclosure Requirements* (ASU 2010-09), which amends FASB ASC Topic 855, *Subsequent Events* (ASC 855). ASU

Table of Contents**AMERICAN CAPITAL AGENCY CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(unaudited)**

No. 2010-09 removes the requirement for an SEC filer (as defined in ASU 2010-09) to disclose the date, in both issued and revised financial statements, through which it has evaluated subsequent events. This change alleviates potential conflicts with current SEC guidance. ASU No. 2010-09 is effective upon issuance for all entities other than conduit bond obligors. We adopted the requirements of ASU No. 2010-09 on the effective date. We do not have any material subsequent events that impact our consolidated financial statements.

Reclassifications

Certain prior period amounts in the notes to the consolidated financial statements have been reclassified to conform to the current period presentation.

Note 4. Agency Securities

The following tables summarize our investments in agency securities as of March 31, 2010 and December 31, 2009 (dollars in thousands):

	As of March 31, 2010			
	Fannie Mae	Freddie Mac	Ginnie Mae	Total
Available-for-sale securities:				
Agency securities, par	\$ 3,035,735	\$ 1,913,115	\$ 7,827	\$ 4,956,677
Unamortized discount	(91)			(91)
Unamortized premium	115,239	92,500	324	208,063
Amortized cost	3,150,883	2,005,615	8,151	5,164,649
Gross unrealized gains	27,857	14,298	219	42,374
Gross unrealized losses	(3,494)	(929)		(4,423)
Available-for-sale securities, at fair value	3,175,246	2,018,984	8,370	5,202,600
Agency securities remeasured at fair value through earnings:				
Interest-only strips, amortized cost	3,072	32,495		35,567
Gross unrealized gains		2,698		2,698
Gross unrealized losses	(601)	(10)		(611)
Agency securities measured at fair value through earnings, at fair value	2,471	35,183		37,654

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Total agency securities, at fair value	\$ 3,177,717	\$ 2,054,167	\$ 8,370	\$ 5,240,254
Weighted average coupon	5.09%	5.74%	6.00%	5.34%
Weighted average yield as of March 31, 2010(1)	3.74%	3.55%	5.12%	3.68%
Weighted average yield for the three months ended March 31, 2010(1)	3.92%	3.50%	3.27%	3.78%

(1) Incorporates future prepayment assumptions and forward rates.

	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Fair Value
Fixed-Rate	\$ 1,823,809	\$ 13,832	\$ (2,717)	\$ 1,834,924
Adjustable-Rate	2,694,280	17,641	(1,364)	2,710,557
CMO	646,560	10,901	(342)	657,119
Interest-only strips	35,567	2,698	(611)	37,654
	\$ 5,200,216	\$ 45,072	\$ (5,034)	\$ 5,240,254

Table of Contents**AMERICAN CAPITAL AGENCY CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(unaudited)**

	As of December 31, 2009			
	Fannie Mae	Freddie Mac	Ginnie Mae	Total
Available-for-sale securities:				
Agency securities, par	\$ 2,853,278	\$ 1,248,698	\$ 12,456	\$ 4,114,432
Unamortized discount	(92)			(92)
Unamortized premium	99,709	49,662	386	149,757
Amortized cost	2,952,895	1,298,360	12,842	4,264,097
Gross unrealized gains	36,750	8,965	340	46,055
Gross unrealized losses	(6,335)	(3,702)		(10,037)
Agency securities, at fair value	\$ 2,983,310	\$ 1,303,623	\$ 13,182	\$ 4,300,115
Weighted average coupon	5.26%	5.31%	6.00%	5.28%
Weighted average yield as of December 31, 2009(1)	4.20%	3.50%	5.33%	3.99%
Weighted average yield for the year ended December 31, 2009(1)	4.78%	4.27%	4.88%	4.64%
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Fair Value
Fixed-Rate	\$ 1,863,261	\$ 28,210	\$ (4,067)	\$ 1,887,404
Adjustable-Rate	1,699,513	9,447	(3,473)	1,705,487
CMO	701,323	8,398	(2,497)	707,224
	\$ 4,264,097	\$ 46,055	\$ (10,037)	\$ 4,300,115

(1) Incorporates future prepayment assumptions and forward rates.

For the three months ended March 31, 2010, we recognized an unrealized gain of \$2.1 million in gain (loss) on derivative instruments, net in our consolidated statements of operations and comprehensive income for the change in value of investments in interest-only strips, which represent our right to receive a specified proportion of the contractual interest flows of specific agency and CMO securities. We did not have any investments in interest-only strips during the three months ended March 31, 2009.

Actual maturities of agency securities are generally shorter than the stated contractual maturities. Actual maturities are affected by the contractual lives of the underlying mortgages, periodic principal payments and principal prepayments. The following table summarizes our agency securities as of March 31, 2010 and December 31, 2009, according to their estimated weighted average life classifications (dollars in thousands):

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Weighted Average Life	As of March 31, 2010			As of December 31, 2009		
	Fair Value	Amortized Cost	Weighted Average Coupon	Fair Value	Amortized Cost	Weighted Average Coupon
Less than one year	\$ 4,620	\$ 4,954	16.29%	\$ 432	\$ 428	1.95%
Greater than one year and less than three years	803,228	797,555	5.46%	281,721	281,143	5.87%
Greater than three years and less than five years	2,050,046	2,035,995	5.30%	1,340,665	1,337,777	5.14%
Greater than or equal to five years	2,382,360	2,361,712	5.31%	2,677,297	2,644,749	5.25%
Total	\$ 5,240,254	\$ 5,200,216	5.34%	\$ 4,300,115	\$ 4,264,097	5.28%

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AMERICAN CAPITAL AGENCY CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The weighted average lives of the agency securities as of March 31, 2010 and December 31, 2009 in the table above incorporates anticipated future prepayment assumptions. As of March 31, 2010, our expected constant prepayment rate (CPR) over the remaining life of our aggregate investment portfolio is 18%. Our estimates differ materially for different types of securities and thus individual holdings have a wide range of projected CPRs. We estimate long-term prepayment assumptions for different securities using third-party services, market data and internal estimates. These third-party services estimate prepayment speeds using models that incorporate the forward yield curve, current mortgage rates, mortgage rates of the outstanding loans, loan age, volatility and other factors. As market conditions are changing rapidly, we use our judgment in making adjustments to our models for different securities. Various market participants could use materially different assumptions.

The following table presents the gross unrealized loss and fair values of our available-for-sale agency securities by length of time that such securities have been in a continuous unrealized loss position as of March 31, 2010 and December 31, 2009 (dollars in thousands):