

AMBAC FINANCIAL GROUP, INC.

CHARTER OF THE AUDIT AND RISK ASSESSMENT COMMITTEE OF THE BOARD OF DIRECTORS

(As of July 19, 2005)

Mission

The mission of the Ambac Financial Group, Inc. Audit and Risk Assessment Committee (the "**Committee**") is to monitor the corporate control and risk environment of Ambac Financial Group, Inc. (the "**Company**"). The purpose of the Committee shall include, among other things, to assist the Board of Directors in fulfilling its oversight responsibilities by reviewing: 1) the integrity of the Company's financial statements and other financial information that is provided to stockholders; 2) the performance of the Company's internal audit function and the Company's independent auditors; 3) the independent auditors' qualifications and independence; 4) the Company's compliance with relevant legal, regulatory and accounting requirements; and 5) the performance and effectiveness of the Company's management of its portfolio credit and market risks. It is the objective of the Committee to maintain free and open means of communications among the Board of Directors, the independent auditors, the internal auditors and the financial and senior management of the Company.

Membership and Meeting Requirements

The Committee will meet as often as it determines but not less frequently than quarterly. In addition, the Committee shall, periodically, meet separately with the General Counsel, the Director of Internal Audit, the executive officer in charge of the Portfolio and Market Risk Management Group and the independent auditors in order to fulfill its duties and make regular reports to the Board.

The Committee will be comprised of at least four independent directors, who, in the judgment of the Board of Directors, are financially literate or who become financially literate within a reasonable period of time. Each member of the Committee will satisfy all independence and other membership requirements of the New York Stock Exchange and the Sarbanes-Oxley Act of 2002 (the "**Act**"), related rules of the United States Securities and Exchange Commission (the

"SEC") and the Company's categorical standards of independence set out in the Company's Corporate Governance Guidelines. At least one member of the Committee will be an "audit committee financial expert", as defined under the rules of the SEC, or, if no member of the Committee is an "audit committee financial expert", then such fact will be disclosed in the Company's filings with the SEC. At least one member of the Committee will also have, in the judgment of the Board of Directors, accounting or related financial management expertise in accordance with the New York Stock Exchange listing standards (*provided that the Board may presume that an individual who qualifies as an "audit committee financial expert" satisfies this requirement as well*).

Members of the Committee shall not serve on more than two other public company audit committees.

As directed or required by the Committee, the Company's Head of the Portfolio and Market Risk Management Group, Chief Financial Officer, the General Counsel, representatives from the Company's independent auditors, the Director of Internal Audit, Chief Executive Officer, President or other members of management of the Company will attend Committee meetings.

Duties and Responsibilities

The Company's management is responsible for the preparation, presentation and integrity of the Company's financial statements and the independent auditors are responsible for auditing the financial statements and reviewing the unaudited financial statements. The Committee is responsible for overseeing the conduct of these activities by the Company's management and the independent auditors and not to plan or conduct audits or to determine that the Company's financial statements are complete and accurate and are in accordance with accounting principles generally accepted in the United States of America (GAAP). In carrying out its oversight responsibilities, the Committee is not providing any expert or special assurance as to the Company's financial statements or any professional certification as to the independent auditor's work. The following responsibilities are within the authority of the Committee, and shall not be delegated or allocated to a different committee of the Board:

- 1) Report regularly to the Board to discuss issues regarding the quality or integrity of the Company's financial statements, the Company's compliance with legal and regulatory requirements, the performance and independence of the Company's independent auditors, and the performance of the internal audit function.

- 2) Prepare a report, for inclusion in the Company's proxy statement or, if applicable, Annual Report on Form 10-K, as required by the rules of the SEC, disclosing that the Committee:
 - a) reviewed and discussed the audited financial statements with management;
 - b) discussed with the independent auditors the matters required by Statement on Auditing Standards No. 61 (*which requires the independent auditors to communicate to the Committee matters related to the conduct of the audit*);
 - c) received the written disclosures and the letter from the auditors regarding the auditors' independence, including all non-audit services and fees and discussed the auditors' independence as required by Independent Standards Board Standard No. 1 with the auditors (*which requires the independent auditors to disclose any relationship that could impact the auditors' objectivity and independence*);

and that, based on the review and discussions referred to in paragraphs (a) through (c), recommended to the Board of Directors that the financial statements be included in the Company's Annual Report on Form 10-K.

- 3) Review with management and the independent auditors the Company's annual financial statements prior to the filing of its Form 10-K and its quarterly financial statements prior to the filing of its Form 10-Q, including the Company's disclosures under "Management's Discussion and Analysis of Financial Condition and Results of Operations". Also, the Committee shall discuss the results of the independent auditors' annual audits and quarterly reviews and any other matters required to be communicated

to the Committee by the independent auditors under the standards of the Public Company Accounting Oversight Board (PCAOB).

- 4) Review annually with management and the Company's independent auditors:
 - a) all critical accounting practices and policies to be used; and
 - b) all alternative treatments of financial information within GAAP that have been discussed by the independent auditors and management, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the auditors.

- 5) Review with management and the Company's independent auditors:
 - a) major issues regarding accounting principles and financial statements presentations, including any significant changes in the Company's selection or application of accounting principles;
 - b) any analyses prepared by management and/or the independent auditors setting forth significant financial reporting issues and judgments made in connection with the preparation of the financial statements, including analyses of the ramifications and effects of alternative GAAP methods on the Company's financial statements;
 - c) the effect of regulatory and accounting initiatives, as well as off-balance sheet structures, on the Company's financial statements; and
 - d) the effect, if any, of new or pending accounting pronouncements.

- 6) Review management's report on its assessment of the effectiveness of internal control over financial reporting as of the end of each fiscal year and the independent auditors' report on (1) management's assessment and (2) the effectiveness of internal control over financial reporting.

- 7) Discuss with management, the internal auditors and the independent auditors management's process for assessing effectiveness of internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act.

- 8) Review on a regular basis with both the Company's independent auditors and internal auditors any problems or difficulties encountered by the auditors in the course of any audit work, including management's response with respect thereto, any restrictions on the scope of the auditors' activities or on access to requested information, and any significant disagreements with management. In connection with the above, the Committee should review with the independent auditors:
 - a) any accounting adjustments that were noted or proposed by the independent auditors but were rejected by management (*as immaterial or otherwise*);
 - b) any communications between the audit team and the independent auditor's national office regarding auditing or accounting issues; and
 - c) all other material written communications between the independent auditors and management, including any "management" or "internal control" letter issued, or proposed to be issued, by the independent auditors that is in addition to their report on the effectiveness of internal control over financial reporting.

- 9) Discuss the type and presentation of information to be included in the Company's earnings press releases (*paying particular attention to any use of "pro forma" or "adjusted" information not in compliance with GAAP*), as well as review any financial information and earnings guidance provided by the Company to analysts and rating agencies, provided that the Committee need not discuss in advance, in each instance, such disclosures.

- 10) Resolve all disagreements between management and independent auditors regarding financial reporting or audit, review or attest services.

- 11) Select the Company's independent auditors, approve the fees and terms of the independent auditors' engagement, review the overall scope of the annual audit plan of the independent auditors, including planning and staffing, review and evaluate the performance and independence of the independent auditors, including the lead audit partner and other audit partners serving the account, monitor the auditors' compliance

with SEC partner rotation requirements, and make decisions regarding the replacement or termination of the independent auditors. When evaluating the independent auditors, the Committee should consider the opinions of management and the Company's internal auditors, and should consider the desirability of regularly rotating the Company's independent auditors.

- 12) Pre-approve all permitted audit-related and non-audit services performed by the independent auditors. The Committee may adopt policies and procedures that provide for the automatic pre-approval of permitted audit-related and non-audit services to be provided by the independent auditors and/or the delegation of pre-approval authority to the Chairman of the Audit Committee.
- 13) At least annually, obtain and review a report from the Company's independent auditors describing:
 - a) the independent auditors' internal quality-control procedures;
 - b) any material issues raised by the most recent internal quality-control review, or peer review, or PCAOB review, of the independent auditors, or by any inquiry or investigation by any governmental or professional authority, within the preceding five years, regarding any independent audits carried out by the independent auditors, and any steps taken to deal with any such issues;
 - c) all relationships between the independent auditors and the Company *(including a description of each category of services provided by the independent auditors to the Company and a list of the fees billed for each such category)*; and
 - d) compliance with professional and regulatory requirements regarding the conduct of their audit, including that the audit was conducted in a manner consistent with Section 10A of the Exchange Act and no action under Section 10A(b) of the Securities and Exchange Act of 1934 has been initiated.

- 14) Set clear hiring policies for employees and former employees of the independent auditors.
- 15) Evaluate whether management is setting the appropriate control environment through an annual review of the Company's entity-level controls, including but not limited to their enforcement of a positive business ethics environment, the establishment of fraud monitoring and fraud prevention controls across all business and monitoring the enforcement of the Company's Code of Business Conduct.
- 16) Establish procedures for (a) the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters, and (b) the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.
- 17) Review the Company's disclosure controls and procedures policy and other steps the Company has taken to ensure that all financial and non-financial information required to be disclosed is collected, summarized, evaluated and reported within the time periods specified in the SEC's rules and forms, including receiving a quarterly report regarding any Form 8-Ks filed during the prior quarter.
- 18) Review annually with the Company's internal auditors and independent auditors the Company's guidelines and policies relating to risk assessment and risk management, including the identification of potential fraud risk, fraud protection and fraud detection methods.
- 19) Review annually with management guidelines and policies of the Company's risk management and underwriting areas, including the Company's insured book of business, derivatives business and investment portfolios and discuss other steps management has taken to monitor and control the Company's major financial risk exposures.

- 20) Review quarterly with the Head of the Portfolio and Market Risk Management Group, the Company's current adversely classified credit book, with particular focus on problem credits.

- 21) Review with the chief executive officer and chief financial officer, as appropriate, and independent auditors, periodically, the following:
 - a) all significant deficiencies and material weaknesses in the design or operation of internal controls which could adversely affect the Company's ability to record, process, summarize, and report financial data, including any material weaknesses in internal controls identified by the Company's independent auditors;
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal controls;
 - c) any significant changes in internal controls or in other factors that could significantly affect internal controls, including any corrective actions with regard to significant deficiencies and material weaknesses; and
 - d) procedures undertaken in connection with the CEO and CFO certifications for Form 10-K and 10-Q's, including their evaluation of the Company's disclosure controls and procedures and internal controls.

- 22) Review the Company's internal audit function, including its independence, its responsibilities, budget and staffing, the scope of the audits, the findings of the internal auditors, and management's response and implementation of such recommendations.

- 23) Review with the Company's general counsel, and outside counsel, when appropriate, all legal and regulatory matters, if any, that may have a material impact on the Company's financial statements and the Company's compliance policies, and any material reports or inquiries received from regulators or government agencies

- 24) Conduct or authorize investigations and engage special legal, accounting or other consultants to help advise the Audit Committee with such investigations, into any matters within the Committee's scope of responsibilities.
- 25) Conduct, and review with the Board, an annual performance evaluation of the Committee.
- 26) Review and assess the adequacy of this audit and risk assessment committee charter on an annual basis and make any recommended changes.
- 27) As appropriate, obtain advice and assistance from outside legal, accounting and other advisors, consultants or experts, and ensure that the Company provides appropriate funding for the payment of the fees of such advisors.
- 28) Perform such additional activities, and consider such other matters, within the scope of its responsibilities, as the Committee or the Board deems necessary or appropriate.