

EXHIBIT 3

1 UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

2 *In re:* Case No. 10-15973-scc
3 AMBAC FINANCIAL GROUP, INC. New York, New York
4 *Debtor.* November 9, 2010
2:59 p.m.

5
6 TRANSCRIPT OF CHAP 11 HEARING RE
7 ADVERSARY PROCEEDING: 10-04210-SCC
8 AMBAC FINANCIAL GROUP, INC. VS. UNITED STATES OF AMERICA
9 **DOC #2 MOTION FOR TEMPORARY RESTRAINING ORDER**
10 **AND PRELIMINARY INJUNCTION**

11 DOC# 3 DEBTOR'S MOTION FOR INTERIM ORDER ESTABLISHING
12 PROCEDURES FOR CERTAIN TRANSFERS OF EQUITY INTERESTS IN AND
13 CLAIMS AGAINST THE DEBTOR AND SCHEDULING A FINAL HEARING

14 DOC# 4 DEBTOR'S MOTION FOR INTERIM ORDER
15 (I) AUTHORIZING DEBTOR TO CONTINUE USING EXISTING CASH
16 MANAGEMENT SYSTEM AND BANK ACCOUNTS AND HONOR RELATED
17 PREPETITION OBLIGATIONS, (II) EXTENDING DEBTORS TIME
18 TO COMPLY WITH SECTION 345(B) OF THE BANKRUPTCY CODE,
19 AND (III) SCHEDULING A FINAL HEARING

20 DOC# 5 DEBTOR'S MOTION FOR ORDER ESTABLISHING CERTAIN
21 NOTICE, CASE MANAGEMENT, AND ADMINISTRATIVE PROCEDURES

22 DOC# 7 DEBTOR'S MOTION FOR ORDER (I) EXTENDING TIME TO
23 FILE SCHEDULES AND STATEMENT OF FINANCIAL AFFAIRS, AND
24 (II) WAIVING REQUIREMENT TO FILE EQUITY LIST AND SERVE
25 NOTICE OF COMMENCEMENT ON EQUITY HOLDERS
BEFORE THE HONORABLE SHELLEY C. CHAPMAN
UNITED STATES BANKRUPTCY JUDGE

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1 THE COURT: Good afternoon. Please be seated. Mr.
2 Bienenstock, how are you?

3 MR. BIENENSTOCK: Fine. Thanks, Your Honor. And
4 thanks for hearing us this afternoon.

5 THE COURT: Certainly. All right. We're ready when
6 you are.

7 MR. BIENENSTOCK: Shall I start and would you prefer I
8 stand here or over there?

9 THE COURT: Why don't we have whoever's going to speak
10 come to the podium and I think we have a few folks on the phone.
11 So let me find out who is on the phone. Is anyone on the phone,
12 please?

13 (No response.)

14 THE COURT: All right. My understanding is that we're
15 on listen only, so I won't require parties on the phone to
16 identify themselves.

17 Okay, Mr. Bienenstock.

18 MR. BIENENSTOCK: Thank you, Your Honor and we very
19 much appreciate the Court giving us time on very short notice to
20 have these first day hearings in the Chapter 11 case of AMBAC
21 Financial Group, Inc. Our plan if it's okay with the Court is
22 for me to make some introductions and provide the Court a
23 snapshot of the company and the case and then with the help of
24 some of my colleagues here to get into the first day motions.

25 THE COURT: Okay.

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1 MR. BIENENSTOCK: So as not to hold any suspense, we
2 do think we're very fortunate in having a stipulation with the
3 Internal Revenue Service which would obviate a dispute in that
4 regard in connection with the papers we filed this morning.
5 Because it only happened recently, it will be oral. We will ask
6 the Court to so order it.

7 THE COURT: Okay.

8 MR. BIENENSTOCK: But I think we're in agreement and
9 the United States Attorney will definitely correct me if I get
10 anything wrong.

11 THE COURT: I'm sure he will. Okay.

12 MR. BIENENSTOCK: Okay. Your Honor, first with me at
13 counsel table is my partner, Peter Ivanick and my colleague,
14 Allison Weiss of Dewey & LeBoeuf.

15 THE COURT: Okay.

16 MR. BIENENSTOCK: He'll blush a bit, but my partner
17 Peter Ivanick and Ms. Weiss have a specialty that I certainly
18 don't have, and I don't know how many of them are in the country
19 that do. There's an interface between the bankruptcy law and
20 insurance insolvency law that is critical in this case. Few
21 people in the country understand it and can deal with it and at
22 least on our side, these people actually can.

23 And I don't want to get too far ahead of ourselves,
24 but just to give Your Honor a flavor of the types of issues that
25 come up; we're all accustomed to federal preemption. When it

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1 comes to insurance, there's something called reverse preemption.
2 And under the McCarran Ferguson Act at 15 U.S.C. 1012(b),
3 Congress has legislated that "No act of Congress shall be
4 construed to invalidate, impair or supersede any law enacted by
5 any state for the purpose of regulating the business of
6 insurance unless such act specifically relates to the business
7 of insurance."

8 That may or may not actually be litigated in this
9 case. We hope not but it basically changes the normal calculus
10 in the sense that the insurance company at issue here is a
11 subsidiary, goes by a state set of rules that have supremacy
12 over some of our rules such as our preference statutes. So a
13 preview of things perhaps to come or not but we do have people
14 who understand it, who can brief it well for the Court if it
15 ever comes up.

16 THE COURT: All right.

17 MR. BIENENSTOCK: Now who is Ambac? Ambac is a
18 company known conventionally as a monoline insurance company.
19 It is quite substantial. Its subsidiary, Ambac Assurance
20 Corporation, and in turn subsidiaries of what we call AAC, have
21 insured a notional amount of approximately 367 billion dollars
22 of different types of debt.

23 Of that 367 billion dollars of commitments to insured
24 debt, approximately 67 billion are in what AAC calls the
25 segregated account. The segregated account is an account under

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1 currently the supervision of the Wisconsin Insurance
2 Commissioner. And with us in court today is Frank DiCastrì of
3 Foley & Lardner, representing OCI.

4 While I'm on introductions, Your Honor, we also have
5 in court as attorneys, Tony Princi of Morrison Foerster who
6 represents the ad hoc committee of bondholders at AFG and his
7 colleague, Gary Lee. Just to finish the introductions from the
8 company we have David Wallis, the President and Chief Executive
9 Officer, the General Counsel, Kevin Doyle and Executive Vice
10 President, Michael Callen, Chairman of the Board and Wes
11 Kirchhoff, its Tax Director.

12 And to the extent, if any, that any of the first day
13 motions require any disputed facts which we don't anticipate, we
14 have the right people here.

15 THE COURT: Okay.

16 MR. BIENENSTOCK: Getting back to AAC, Your Honor, 67
17 billion of what it's guaranteed approximately is in what we call
18 the segregated account that's subject to a rehabilitation
19 proceeding in Wisconsin. For the next two weeks my partner,
20 Peter Ivanick, is going to be in Wisconsin, hopefully getting
21 approved a rehabilitation plan for that segregated account.

22 It's not too much of an exaggeration to say that the
23 hopes and prayers of Ambac Financial Group, Inc.'s creditors
24 ride with the future solvency and significant value of AAC.
25 Although we all are familiar with the crisis that occurred let's

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1 say notionally at Lehman's filing in September of 2008, the fact
2 is that most of the debt AAC guaranteed we do not believe will
3 default or there will be any exposure on but there's a time
4 where that will prove to be true or not true and there will be a
5 time hopefully when substantial benefits can be reaped by our
6 creditors from the value of AAC.

7 Because of the fact that the guarantees of other
8 peoples' debts, other entities' debts including municipalities'
9 debts, are based on a variety of different contracts. It won't
10 surprise the Court to know that a lot of those contracts go into
11 default if precipitous things happen to AAC. That is why we
12 needed to file the pleadings we filed this morning for
13 declaratory judgment in connection with whether AAC and the tax
14 group and AFG primarily owes any taxes to the IRS. As explained
15 in our papers, we received consensually approximately 700
16 million dollars of tax refunds the last three years and were
17 just recently advised that the IRS may or may not take action to
18 take it back.

19 Under the IRS rules and regulations and statutes,
20 there are various provisions entitling them to seize things in
21 enforcement before we have notice and before there's a trial on
22 the merits. If that happened, many of our, the contracts of AAC
23 would go into default. The consequence of default would be very
24 similar to the Lehman filing. Counterparties would be entitled
25 to sell their collateral. The flood of collateral on the market

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1 would depress its value. Therefore, the liabilities would go
2 way up and the asset value of the collateral we have would go
3 way down.

4 I think in the Lehman situation, forty to seventy
5 billion dollars of loss was occasioned simply because of the
6 bankruptcy default. That's why it's the difference here between
7 having value for our creditors, and perhaps very substantial
8 value, and in not allowing there to be a default vis-à-vis our
9 contracts by any precipitous action. And I want to emphasize,
10 we are in no sense at war with the IRS. We don't think they
11 feel they're at war with us.

12 THE COURT: Okay.

13 MR. BIENENSTOCK: We pay all of our taxes. We're not
14 aggressive in taking tax positions. If we owe taxes, we want to
15 pay them completely. What we have to guard against is the
16 possibility that a precipitous action would inadvertently create
17 tremendous loss that would have ripples probably far beyond
18 Ambac if other cases are a guide and might cause loss
19 unnecessarily and we are, as I hope today's stipulation
20 evidences, we think we're on track at least to try to resolve
21 this with the IRS. If not, what our stipulation provides with
22 the IRS is the IRS agrees as requested in our papers that it
23 will not take enforcement action against Ambac Financial Group,
24 Inc. or its subsidiaries or their assets, absent giving us five
25 business days notice first. That would enable us to come to

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1 court. And that agreement by consent will last until a date the
2 Court assigns for having and deciding the preliminary injunction
3 motion that we've made. We've agreed with the Department of
4 Justice that it will file its answering brief by Friday,
5 December 31. The debtor will file its reply brief by Tuesday,
6 January 18. There will then be a hearing if we haven't
7 otherwise --

8 THE COURT: On the PI.

9 MR. BIENENSTOCK: On the PI -- if we haven't otherwise
10 resolved things.

11 THE COURT: Okay.

12 MR. BIENENSTOCK: And the stipulation will go through
13 the hearing through the Court's decision.

14 THE COURT: Okay.

15 MR. BIENENSTOCK: And at that point whatever happens.
16 I think I got --

17 THE COURT: All right. But it's possible that in that
18 five day window it would be wonderful if everyone keeps talking
19 to each other.

20 MR. BIENENSTOCK: Right.

21 THE COURT: But the purpose of the stipulation is to
22 enable you to come in and seek an actual preliminary injunction.

23 MR. BIENENSTOCK: Right.

24 THE COURT: Correct?

25 MR. BIENENSTOCK: Yes, Your Honor.

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1 THE COURT: All right.

2 MR. BIENENSTOCK: Now if -- I think since I've put
3 that on the record, if I might defer to the US Attorney for a
4 moment, Mr. Cordaro, because if that's okay we would ask the
5 Court to so order the stipulation.

6 THE COURT: Okay.

7 MR. CORDARO: Thank you, Mr. Bienenstock. Joseph
8 Cordaro, Assistant United States Attorney, Southern District of
9 New York.

10 Yes, Your Honor, we have agreed to a stipulation and
11 the government just having received these papers in the recent
12 past, I just wanted to be sure that there's no misunderstanding.
13 As I understand our agreement, that the -- that we would give
14 five days notice before taking any enforcement action contrary
15 to the state court injunction which the government has seen yet
16 but we're willing to agree to that.

17 THE COURT: I think you're -- all right. Let's be
18 clear on this because I think you're relief was broader than
19 that.

20 MR. BIENENSTOCK: Well I said five business days. I
21 think that's okay with the IRS.

22 THE COURT: No, but --

23 MR. CORDARO: Yes.

24 THE COURT: But Mr. Cordaro just referred to the state
25 court injunction. My understanding of the relief that you'll

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1 want is any action; five days notice of any action with respect
2 to --

3 MR. BIENENSTOCK: Well, okay. Your Honor, the
4 reconciling factor is the state court injunction is very broad
5 and in our view. Any action would trip it. But Mr. Cordaro is
6 correct. What we agreed to is any action that violates the
7 state court injunction, whether or not it's in effect --

8 THE COURT: Okay.

9 MR. BIENENSTOCK: -- requires five business days'
10 notice to us in advance.

11 THE COURT: All right. But is that -- I guess my
12 question is is that broad enough to encompass -- the state court
13 injunction is broad enough by its terms to encompass any action
14 that the IRS would take against a non-debtor subsidiary with
15 respect to the tax refunds.

16 MR. BIENENSTOCK: Yes, Your Honor.

17 THE COURT: I just want to make sure it's fully
18 protected.

19 MR. BIENENSTOCK: Yes, Your Honor.

20 THE COURT: All right.

21 MR. CORDARO: Then that's fine with the government,
22 Your Honor.

23 THE COURT: All right?

24 MR. BIENENSTOCK: Yes, Your Honor.

25 THE COURT: All right. Then I will so order the

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1 record in that regard. Mr. Bienenstock, could you once again
2 read those dates?

3 MR. BIENENSTOCK: Yes. The government's answering
4 brief by December 31 which is a Friday. The debtors' reply
5 brief by January 18 which is a Tuesday. We think that Monday is
6 a holiday, so we made it the Tuesday.

7 THE COURT: It's Martin Luther King Day probably;
8 right? Right. Okay. Very well.

9 MR. CORDARO: Thank you, Your Honor.

10 THE COURT: Thank you. Thank you for your prompt
11 response, Mr. Cordaro.

12 MR. CORDARO: Thank you.

13 MR. BIENENSTOCK: Okay.

14 THE COURT: Okay.

15 MR. BIENENSTOCK: Your Honor, the other piece of good
16 news which my colleague Allison Weiss will embellish on a bit I
17 think, is that while we haven't filed a proposed Chapter 11 plan
18 with our petition, we have been in discussions with the
19 bondholders and their group for quite some time. We have a non-
20 binding understanding and we are very hopeful it will quickly
21 become a binding understanding and lead to the Chapter 11 plan.

22 So our goal here is to at all costs protect the
23 insurance company. Everyone, all our creditors are aligned and
24 we need to protect the insurance company. And the value of that
25 in the future will be down to the benefit of our creditors in

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1 what we think should be a successful reorganization.

2 THE COURT: Okay.

3 MR. BIENENSTOCK: And unless the Court has questions,
4 I would like to turn things over to Allison Weiss to go through
5 the first day motions.

6 THE COURT: All right. Very well.

7 MR. BIENENSTOCK: Or at least some of them.

8 THE COURT: That's great. Thank you, Mr. Bienenstock.

9 MR. BIENENSTOCK: Thank you.

10 MS. WEISS: Good afternoon, Your Honor. Allison
11 Weiss --

12 THE COURT: Good afternoon, Ms. Weiss.

13 MS. WEISS: -- from Dewey and LeBoeuf. Before
14 addressing the administrative and operational motions, we have
15 asked the Court to consider today, I would like to first provide
16 the Court with some additional background regarding the debtor
17 and the events leading up to the filing.

18 THE COURT: Okay.

19 MR. BIENENSTOCK: For a more detailed discussion, I
20 refer you to the affidavit of David Wallis, the debtor's
21 President and Chief Executive Officer in support of our first
22 day motions. Mr. Wallis is present in the courtroom today and
23 available to testify.

24 Because AAC's financial guarantee and financial
25 services businesses were devastated in the financial crisis