

STATE OF WISCONSIN CIRCUIT COURT DANE COUNTY

 In the Matter of the
 Rehabilitation of:
 SEGREGATED ACCOUNT OF AMBAC Case No. 10-CV-1576
 ASSURANCE CORPORATION

 HONORABLE WILLIAM D. JOHNSTON
 CIRCUIT COURT JUDGE, PRESIDING

 PLACE: Lafayette County Courthouse
 626 Main Street
 Darlington, WI 53530

 PROCEEDINGS: Confirmation Hearing

 DATE: November 18, 2010

A P P E A R A N C E S

MICHAEL B. VAN SICKLEN and **JEFFREY SIMMONS**,
 Attorneys at Law, FOLEY & LARDNER LLP, 150 East Gilman
 Street, Madison, Wisconsin, appeared on behalf of
 Petitioner Sean Dilweg, Commissioner of Insurance of
 the State of Wisconsin, and the Department of
 Insurance of the State of Wisconsin.

DANIEL W. STOLPER, Attorney at Law, STAFFORD
 ROSENBAUM LLP, Madison, Wisconsin, and **HENRY J.**
RICARDO, WILLIAM PRIMPS, RICHARD REINTHALER, PETER
IVANICK, Attorneys at Law, DEWEY & LE BOEUF LLP, New
 York, New York, appeared on behalf of Ambac Assurance
 Corporation.

DAVID M. GREENWALD, PATRICK TROSTLE, and **MICHAEL**
BRODY, Attorneys at Law, JENNER & BLOCK LLP, Chicago,
 Illinois, and **TIMOTHY MUTH**, Attorney at Law, Reinhart
 Boerner Van Deuren, Madison, Wisconsin, appeared on
 behalf of RMBS Policyholders.

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THOMAS J. WELSH, Attorney at Law, ORRICK,
 HERRINGTON & SUTCLIFFE LLP, Sacramento, California,
 and **GREGORY W. LYONS**, Attorney at Law, O'Neil Cannon
 Hollman DeJong & Laing, Milwaukee, Wisconsin appeared
 on behalf of Depfa Bank plc.

CRAIG S. BLOOMGARDEN, Attorney at Law, MANATT,
 PHELPS & PHILLIPS, Los Angeles, California, appeared
 on behalf of Federal Home Loan Mortgage Corporation.

ANDREW DEVORE, Attorney at Law, ROPES & GRAY,
 Boston, Massachusetts, and **ANNE M. BENSKY**, Attorney at
 Law, GARVEY McNEIL & ASSOCIATES, S.C., Madison,
 Wisconsin, appeared on behalf of One State Street.

STEVEN T. WHITMER and **KEVIN WISNIEWSKI**, Attorneys
 at Law, LOCKE LORD BISSELL & LIDDELL LLP, Chicago,
 Illinois, and **STEPHEN MORGAN**, Attorney at Law, Murphy
 Desmond, Madison, Wisconsin, appeared on behalf of
 Wells Fargo Bank as Trustee for the LVM Bondholders.

THOMAS PYPER, Attorney at Law, WHYTE HIRSCHBOECK &
 DUDEK, Madison, Wisconsin, appeared on behalf of
 Countrywide Home Loans, Inc.

PHILIP BENTLEY and **MATTHEW TEMKIN**, Attorneys at
 Law, KRAMER LEVIN NAFTALIS & FRANKEL LLP, New York,
 New York, and **NOREEN PARRETT**, Attorney at Law, PARRETT
 & O'CONNELL, appeared on behalf of the LVM
 Bondholders.

MICHAEL E. JOHNSON, Attorney at Law, ALSTON & BIRD
 LLP, New York, New York 10016, appeared telephonically
 on behalf of Wells Fargo and Bank of America as
 Trustee, Wilmington Trust Company, Wilmington Trust
 FSB.

PAUL LUCEY, Attorney at Law, MICHAEL BEST &
 FRIEDRICH, Milwaukee, Wisconsin, appeared on behalf of
 Deutsche Bank Trust and U.S. Bank Trust.

JAMES C. OWEN, Attorney at Law, MCCARTHY, LEONARD
 & KAEMMERER, Chesterfield, Missouri, appeared on
 behalf of ALL Student Loan Corporation and Lloyds TSB
 Bank plc.

THOMAS ROSS HOOPER, Attorney at Law, Seward &
 Kissel LLP, New York, New York, appeared
 telephonically on behalf of Bank of New York Mellon as
 Trustee.

PROCEEDINGS
 (The following proceedings reported
 by Reporter Albert.)
 (On the record at 8:59 a.m.)
 00:00:55 **5** THE COURT: Let's call the Circuit Court for
 00:00:58 **6** Dane County in session in the matter of 10 CV 1576.
 00:01:06 **7** It is In the Matter of the Rehabilitation of the
 00:01:09 **8** Segregated Account of Ambac Assurance Corporation.
 00:01:12 **9** Do you have the hand mic ready, Rich?
 00:01:16 **10** THE BAILIFF: Yes.
 00:01:20 **11** THE COURT: All right. Let's start this day's
 00:01:22 **12** proceedings with appearances.
 00:01:24 **13** MR. VAN SICKLEN: Good morning, your Honor.
 00:01:26 **14** Mike Van Sicklen on behalf of -- and with me today to
 00:01:31 **15** my left is my partner, Jeff Simmons, from the law firm
 00:01:36 **16** Foley & Lardner on behalf of the Rehabilitator and the
 00:01:39 **17** Office of the Commissioner of Insurance. Also present
 00:01:42 **18** on behalf of the OCI is the witness, Mr. Peterson.
 00:01:47 **19** MR. STOLPER: Good morning, your Honor. Dan W.
 00:01:50 **20** Stolper of Stafford Rosenbaum appearing on behalf of
 00:01:54 **21** Ambac Assurance Corporation. And with me is Attorney
 00:02:00 **22** Richard Reintaler, William Primps, Peter Ivanick, and
 00:02:02 **23** Henry Ricardo of Dewey & LeBoeuf. And from Ambac is
 00:02:09 **24** Cathleen Matanle, managing director, and David
 00:02:12 **25** Barranco, managing director.

00:02:13 **1** THE COURT: Thank you.

00:02:15 **2** MR. WHITMER: Good morning, your Honor. Steven

00:02:21 **3** Whitmer, Locke Lord Bissell & Liddell, here on behalf

00:02:21 **4** of Wells Fargo as Trustee for the LVM Bondholders.

00:02:26 **5** Also with me is my colleague, Kevin Wisniewski, also

00:02:29 **6** from Locke Lord. And our local counsel, Steve Morgan

00:02:33 **7** from Murphy Desmond

00:02:38 **8** MR. BENTLEY: Good morning, your Honor. Philip

00:02:43 **9** Bentley of Kramer Levin Naftalis & Frankel for the LVM

00:02:44 **10** Bondholders. As before, with me are my colleague,

00:02:47 **11** Matthew Temkin, and our co-counsel, Noreen Parrett of

00:02:50 **12** the Parrett & O'Connell firm.

00:02:52 **13** THE COURT: The Wisconsin Economic Council asks

00:02:56 **14** that I on their behalf thank you for your promotion of

00:02:59 **15** Wisconsin products.

00:03:06 **16** Continue.

00:03:07 **17** MR. OWEN: Jim Owen for Lloyds Bank and ALL

00:03:11 **18** Student Loan.

00:03:13 **19** MR. BLOOMGARDEN: Good morning, your Honor.

00:03:15 **20** Craig Bloomgarden of Manatt, Phelps & Phillips on

00:03:19 **21** behalf of Freddie Mac.

00:03:22 **22** MR. WELSH: Good morning, your Honor. Tom Welsh

00:03:24 **23** of Orrick Herrington & Sutcliffe, and also joined by

00:03:27 **24** my co-counsel, Gregory Lyons of the O'Neil Cannon firm

00:03:32 **25** for policyholder Depfa Bank plc.

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00:03:37 **1** MR. GREENWALD: Good morning, your Honor. David

00:03:39 **2** Greenwald from the firm Jenner & Block. And I'm

00:03:41 **3** joined here with my partners -- by my partners Patrick

00:03:44 **4** Trostle and Michael Brody, and counsel Timothy Muth

00:03:48 **5** from the Reinhart firm on behalf of Aurelius Capital

00:03:51 **6** Management LP, Fir Tree, Inc., King Street Capital LP,

00:03:56 **7** King Street Capital Master Fund, Limited, Monarch

00:03:59 **8** Alternative Capital LP, and Stonehill Capital

00:04:02 **9** Management.

00:04:03 **10** MR. DEVORE: Good morning, your Honor. Andrew

00:04:07 **11** Devore, Ropes & Gray. And with me is Anne Bensky of

00:04:11 **12** Garvey McNeil & Associates, representing One State

00:04:13 **13** Street, LLC.

00:04:14 **14** MR. JOHNSON: Good morning, your Honor. Michael

00:04:16 **15** Johnson from Alston & Bird. I'm here today on behalf

00:04:19 **16** of the Bank of America, Wells Fargo, and Wilmington

00:04:25 **17** Trust Trustees.

00:04:25 **18** MR. LUCEY: Good morning, your Honor. Paul

00:04:28 **19** Lucey of Michael Best & Friedrich here on behalf of

00:04:32 **20** Deutsch Bank National Trust Company, Deutsch Bank

00:04:34 **21** Trust Company of the Americas, and U.S. Bank National

00:04:38 **22** Association, all as Trustees under Securitization

00:04:41 **23** Trusts.

00:04:41 **24** MR. PYPER: Good morning, your Honor. Tom Pyper

00:04:45 **25** of Whyte Hirschboeck Dudek here on behalf of

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00:04:48 **1** Countrywide Home Loans Servicing LP and Countrywide

00:04:52 **2** Home Loans, Incorporated.

00:04:53 **3** THE COURT: All right. On the phone?

00:04:56 **4** MR. HOOPER (speaking via telephone): Good

00:04:58 **5** morning, your Honor. Thomas Ross Hooper of Seward &

00:04:58 **6** Kissel LLP on behalf of Bank of New York Mellon as

00:04:58 **7** Trustee and Venture Trustee For Collateral Agents,

00:05:09 **8** directly or through its affiliates, for the benefit of

00:05:10 **9** holders and secured parties, certain mortgage-backed

00:05:12 **10** and other asset-backed securities, collateralized loan

00:05:16 **11** obligation and collateralized debt obligation.

00:05:19 **12** THE COURT: All right. Could you repeat your

00:05:20 **13** name again? We had some noise in the courtroom.

00:05:22 **14** MR. HOOPER (speaking via telephone): Of course,

00:05:23 **15** your Honor. Thomas Ross Hooper of Seward & Kissel

00:05:29 **16** LLP.

00:05:29 **17** THE COURT: All right. Anyone else on the

00:05:31 **18** phone?

00:05:36 **19** MR. HOOPER (speaking via telephone): We have a

00:05:38 **20** number of parties. I'm not listing all my staff.

00:05:42 **21** THE COURT: All right. Then Mr. Peterson, for

00:05:44 **22** your appearance today we'll have you take the witness

00:05:46 **23** oath again, please. Raise your hand.

00:05:46 **24** ROGER A. PETERSON,

00:05:46 **25** called as a witness, having been first duly

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00:05:46 **1** sworn, was examined and testified as follows:

00:05:58 **2** THE COURT: All right be seated. And you may

00:06:03 **3** proceed with cross.

00:06:03 **4** **CROSS EXAMINATION**

00:06:05 **5** **BY MR. WHITMER:**

00:06:05 **6** **Q** Good morning, Mr. Peterson. My name's Steven Whitmer,

00:06:10 **7** and I represent Wells Fargo as Trustee for the LVM

00:06:15 **8** Bondholders.

00:06:15 **9** **A** **Good morning.**

00:06:16 **10** **Q** I'd like to start with the topic that you've been

00:06:20 **11** discussing over the last few days. And I think the

00:06:23 **12** words you used were that OCI went to great pains as it

00:06:27 **13** was trying to select the policies to allocate to the

00:06:31 **14** Segregated Account?

00:06:32 **15** **A** **Yes. I believe I used those words.**

00:06:33 **16** **Q** And I'd like to direct you to your testimony on

00:06:39 **17** November 16th. And if the transcript is in front of

00:06:42 **18** you, I'm going to ask that you turn to page 179.

00:06:45 **19** **A** **I have it, yes.**

00:06:59 **20** **Q** My question for you will pertain to the Q and the A

00:07:04 **21** that take up most of page 179. If you could look that

00:07:07 **22** over for a second, and I'd like to direct your

00:07:10 **23** attention to a specific part of that.

00:07:15 **24** (Pause)

00:08:01 **25** **A** **I've reviewed it.**

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00:08:02 **1 Q** Sir, I direct your attention to the middle of your
00:08:05 **2** answer where you start with the words "So we created
00:08:09 **3** subgroups." Do you see that?
00:08:10 **4 A Uh-huh (affirmative).**
00:08:11 **5 Q** It goes on to state, "You know, we kept -- generally
00:08:15 **6** we wanted to look at, rather than looking at the
00:08:19 **7** potential risk only from an economic perspective,
00:08:23 **8** where that could have been perceived as unfair, that
00:08:26 **9** we're just allocating the bad policies to," and then
00:08:30 **10** it goes on.
00:08:30 **11** Could you explain for us what precisely was that
00:08:35 **12** potential risk that you were referring to?
00:08:37 **13 A Risks of losses related to contractual triggers that**
00:08:48 **14 could have accelerated claims or created contractual**
00:08:54 **15 damages with regard to transfers to the Segregated**
00:09:00 **16 Account or being placed into receivership action.**
00:09:05 **17 Q** So what was it that you were concerned would be
00:09:07 **18** perceived as unfair?
00:09:09 **19 A There had been at the time, ah, terms like "good**
00:09:15 **20 bank," "bad bank" used. And we were -- um, those**
00:09:24 **21 terms have taken on kind of a meaning of their own in**
00:09:29 **22 the insurance industry.**
00:09:35 **23 In some situations, perhaps restructurings have**
00:09:44 **24 been done in a way that the perception was that all**
00:09:48 **25 losses were walled off for the benefit of the holding**

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00:09:56 **1 company or equity holders. We don't -- we don't**
00:10:01 **2 believe that's the case here, and that we wanted to**
00:10:03 **3 have an even, broad-based approach to our allocation**
00:10:08 **4 to the Segregated Account rather than something that**
00:10:13 **5 took on a character or could be perceived as taking on**
00:10:18 **6 a character like that "good bank," "bad bank."**
00:10:23 **7 Q** So in other words, was the concern about perception of
00:10:26 **8** unfairness of allocating just the bad policies to the
00:10:30 **9** Segregated Account?
00:10:32 **10 A Perception. We believe that we have conducted the**
00:10:38 **11 allocation in as fair a way as we could do that. But**
00:10:43 **12 obviously, perception is a factor in any kind of**
00:10:49 **13 public action on -- with regard to an insurance**
00:10:57 **14 company or other situations.**
00:10:58 **15 Q** I'd like to turn your attention to the LVM policy.
00:11:04 **16** You'd agree that you're fully familiar with this LVM
00:11:07 **17** policy situation?
00:11:08 **18 A For the most part, yes.**
00:11:09 **19 Q** Well, in fact, you've testified in this case that the
00:11:12 **20** LVM exposure represents one of the highest projected
00:11:16 **21** individual deal losses in the Segregated Account;
00:11:20 **22** correct?
00:11:21 **23 A Um, it has that exposure. I don't recall whether I**
00:11:27 **24 testified specifically to it or not. But yes, that's**
00:11:30 **25 my understanding that it does have -- it is one of the**

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00:11:35 **1 largest single exposures or the largest single**
00:11:39 **2 exposure.**
00:11:40 **3 Q** And to be more specific, and I can give you your
00:11:43 **4** affidavit. It's Exhibit 9 if you'd like to take a
00:11:47 **5** look at it.
00:11:50 **6** MR. STOLPER: Which exhibit?
00:11:52 **7** MR. WHITMER: 9.
00:12:09 **8 Q** I'd like to direct your attention to page 8, paragraph
00:12:12 **9** 13.
00:12:16 **10 A Yes.**
00:12:16 **11 Q** I'm gonna read the last sentence of that paragraph.
00:12:19 **12** You state: "The LVM exposure represents one of the
00:12:23 **13** highest projected individual deal losses in the
00:12:27 **14** Segregated Account."
00:12:28 **15** You'd agree with that?
00:12:29 **16 A Yeah, that's what it says. I believe that is the**
00:12:33 **17 case, yes.**
00:12:33 **18 Q** What is that projected loss in net present value
00:12:38 **19** terms?
00:12:38 **20 A Well, we feel like the individual projections of loss**
00:12:44 **21 are confidential information.**
00:12:47 **22 Q** Well --
00:12:51 **23 A And given that we are attempting to negotiate a**
00:12:54 **24 settlement with the Las Vegas Monorail Bondholders,**
00:13:01 **25 disclosing our or the company's estimate of probable**

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00:13:05 **1 loss would affect that negotiating.**
00:13:10 **2 Q** Well, sir, you say it's confidential. But let's take
00:13:13 **3** a look at paragraph 13 of your affidavit to this
00:13:22 **4** Court. The sentence right before the one I read --
00:13:24 **5 A Uh-huh (affirmative).**
00:13:25 **6 Q** -- states: "The present value of losses associated
00:13:28 **7** with the LVM exposure estimated as of December 31,
00:13:32 **8** 2009, using a 5.1 percent discount rate could exceed
00:13:38 **9** \$350 million in the absence of remediation."
00:13:41 **10** That was your estimate at that time; right?
00:13:43 **11 A Yeah. That continues to be the case. I thought you**
00:13:46 **12 were asking for a specific number or a more specific**
00:13:50 **13 number. And in response to that, I believe that more**
00:13:54 **14 specific number is -- I'm not at liberty to discuss**
00:13:58 **15 that.**
00:13:58 **16 Q** Well, would you agree that currently the net present
00:14:04 **17** value of the projected losses exceeds --
00:14:06 **18 A Yes, sir.**
00:14:07 **19 Q** -- half a billion dollars?
00:14:09 **20 A Again, I would stand on the written testimony in my**
00:14:15 **21 affidavit.**
00:14:15 **22 Q** Sir, are you also familiar with the expected schedule
00:14:22 **23** for claims payouts to be made under the LVM policy
00:14:26 **24** over the years?
00:14:27 **25 A In general.**

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00:14:29 **1 Q** And you'd know, for example, that claims are expected
00:14:32 **2** to be made in the year 2011?
00:14:36 **3 A** **I believe that's correct, yes.**
00:14:37 **4 Q** And then again in 2012 and 2015, 2020, each year going
00:14:44 **5** up through, for example, 2040?
00:14:47 **6 A** **Yes.**
00:14:48 **7 Q** And you're also aware that the majority of the LVM
00:14:54 **8** claims arise after the year 2030; right?
00:14:58 **9 A** **That's my understanding, yes.**
00:15:00 **10 Q** And from your review and your analysis of this largest
00:15:04 **11** projected exposure, you would know that the largest
00:15:08 **12** one-year payouts would be in the years 2032, 2034, and
00:15:16 **13** 2040. That sounds right to you?
00:15:18 **14 A** **Well, I didn't -- I don't know those dates**
00:15:21 **15** **specifically. I know that the majority of the**
00:15:25 **16** **potential claim is payable out in, you know, past**
00:15:30 **17** **2030, as you stated.**
00:15:33 **18** **The exact years, I'm not familiar with that.**
00:15:35 **19 Q** There's been discussion in this case about the
00:15:37 **20** difference between short-tail claimants and long-tail
00:15:40 **21** claimants. Under any view of those words, the LVM
00:15:45 **22** exposure is in the category of long-tail. You'd
00:15:49 **23** agree?
00:15:49 **24 A** **I think that's fair to say, yes.**
00:15:50 **25 Q** And you're also aware that the original obligor on the

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00:15:57 **1** bonds at issue that are covered by the LVM policy,
00:16:01 **2** that's what we refer to as the Las Vegas Monorail?
00:16:06 **3 A** **Yes.**
00:16:07 **4 Q** And I think as you explain in your affidavit, the Las
00:16:12 **5** Vegas Monorail is currently in a Nevada bankruptcy
00:16:16 **6** proceeding. You're aware of that?
00:16:17 **7 A** **I'm aware of that, yes.**
00:16:19 **8 Q** So what I'd like to do is discuss the Plan's
00:16:22 **9** assignment of rights provision in the context of the
00:16:26 **10** LVM Bondholders. And as you just explained for the
00:16:31 **11** Court, you're aware that the first claim would be made
00:16:34 **12** if the Plan were confirmed in the year 2011; right?
00:16:39 **13 A** **Yes.**
00:16:39 **14 Q** And let's -- I'm going to ask you, you don't know what
00:16:42 **15** the value of that claim would actually be in detail;
00:16:45 **16** right?
00:16:46 **17 A** **Amounts that may be due in 2011?**
00:16:48 **18 Q** Right.
00:16:49 **19 A** **No, I do not.**
00:16:50 **20 Q** Let's just assume then that it's \$36 million. That
00:16:53 **21** sounds reasonable?
00:16:54 **22 A** **Well, we can assume it's 36. I don't know if it's**
00:16:58 **23** **reasonable or not.**
00:16:58 **24 Q** Under the Plan, if the \$36 million claim is made in
00:17:05 **25** 2011, that claim would receive \$9 million in cash;

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00:17:12 **1** right?
00:17:13 **2 A** **That's correct math, yes.**
00:17:15 **3 Q** And \$27 million in surplus notes?
00:17:18 **4 A** **That's correct as well.**
00:17:19 **5 Q** And at the moment, the very moment that that claim is
00:17:23 **6** made, under the Plan, the terms as provided by OCI,
00:17:32 **7** all of -- every penny of the \$520 million claim
00:17:37 **8** against the Monorail would immediately at that point
00:17:40 **9** be assigned to AAC; correct?
00:17:46 **10 A** **I can't testify to that. I'm not familiar, ah, with**
00:17:53 **11** **that legal outcome.**
00:17:57 **12 Q** Well, I'm not talking about a legal outcome. I'm
00:18:02 **13** talking about what the Plan provides for. You're
00:18:04 **14** familiar with the provisions of the Plan; right?
00:18:06 **15 A** **Generally speaking, yes.**
00:18:07 **16 Q** You were the financial centerpiece to helping provide
00:18:14 **17** the backup information needed to establish this Plan;
00:18:16 **18** right?
00:18:20 **19 A** **I was involved in the preparation of a Plan, and in**
00:18:28 **20** **particular, financial aspects of the Plan, helping**
00:18:34 **21** **gauge what was fair and equitable to the policyholders**
00:18:42 **22** **and what might be reasonable and appropriate to**
00:18:47 **23** **disclose, things like that, kind of high-level**
00:18:53 **24** **judgments about how OCI's authority should be**
00:18:57 **25** **exercised.**

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00:18:58 **1 Q** I think the words you used were "what's fair and
00:19:02 **2** equitable to the policyholders." You'd agree that
00:19:05 **3** that's really the goal of what we're trying to
00:19:08 **4** accomplish before the Court this week is trying to
00:19:11 **5** figure out what is fair and equitable to the
00:19:13 **6** policyholders?
00:19:13 **7 A** **Well, I've testified that we had goals to provide**
00:19:20 **8** **durable coverage to protect policyholders from**
00:19:26 **9** **additional loss and to provide as much value to**
00:19:29 **10** **policyholders as we prudently could.**
00:19:32 **11 Q** Then let's go back to the scenario we were just
00:19:37 **12** discussing which concerns the assignment provision
00:19:39 **13** provided for in the Plan. I'm going to ask you to
00:19:42 **14** turn to Exhibit 26.
00:20:00 **15 A** **All right.**
00:20:00 **16 Q** And if you could turn to page 20 at section 4.04H.
00:20:10 **17** That section is titled "Assignment of Rights."
00:20:18 **18 A** **All right.**
00:20:22 **19 Q** And that section provides, "Without prejudice to the
00:20:29 **20** terms and provisions of the applicable policy and any
00:20:33 **21** related underlying instruments or contracts, and any
00:20:36 **22** assignment previously executed, whether pursuant to
00:20:40 **23** approved policy claim form or otherwise, upon receipt
00:20:44 **24** of a payment with respect to a permitted policy claim,
00:20:50 **25** each such holder shall be deemed to have assigned its

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00:20:55 **1** rights relating to payment under the underlying
00:20:59 **2** instruments or contracts to AAC." Do you see that?
00:21:03 **3 A Yes.**
00:21:03 **4 Q** And just for context, I'm going to ask that you turn
00:21:08 **5** back to page 5, and specifically to section 1.29,
00:21:12 **6** which defines the term "holder." And 1.29 states,
00:21:26 **7** "Any person holding a claim against the Segregated
00:21:30 **8** Account, including in the case of a policy claim the
00:21:34 **9** named beneficiary of the related policy." Do you see
00:21:38 **10** that?
00:21:38 **11 A I do.**
00:21:39 **12 Q** Let's go back to the scenario I was just discussing.
00:21:43 **13** Am I reading the Plan provisions correctly --
00:21:47 **14** going back to the scenario, the day before the claim
00:21:51 **15** is submitted for that \$36 million, of which \$9 million
00:21:57 **16** would be paid out in cash, there's a \$520 million
00:22:03 **17** claim against the Monorail, right, assuming the inputs
00:22:08 **18** that we talked about before were; correct?
00:22:10 **19 A I'm not testifying as to that aggregate value of the**
00:22:15 **20 claim. I don't have -- you know, that's confidential**
00:22:21 **21 information that I'm not going to be tricked into**
00:22:23 **22 testifying on.**
00:22:24 **23 Q** I don't want to trick you into anything. I just want
00:22:27 **24** -- let's call it X.
00:22:29 **25 A Okay.**

17

00:22:29 **1 Q** The point that I'm trying to get at here.
00:22:32 **2 A There's some larger number X, yes.**
00:22:34 **3 Q** So X. Let's go back and assume it's X.
00:22:36 **4** The day before that \$36 million claim is made
00:22:40 **5** under the Plan --
00:22:41 **6 A Uh-huh (affirmative).**
00:22:42 **7 Q** -- there is a claim for X dollars under the policy
00:22:48 **8** against the Monorail; right?
00:22:51 **9 A Well, it hasn't been submitted yet, so I don't know**
00:22:55 **10 that it's a claim. But there's a potential loss**
00:23:00 **11 against AAC that exists on that day before the claim**
00:23:05 **12 is filed.**
00:23:09 **13** THE COURT: Are you asking whether one claim
00:23:11 **14** triggers all claims in the category?
00:23:15 **15** MR. WHITMER: Yes.
00:23:15 **16** THE COURT: That's basically what he's saying.
00:23:17 **17** If a claim is made and it's permitted, does it then
00:23:25 **18** trigger the rest of the claims in the category?
00:23:28 **19** I guess your answer is no because it has to go
00:23:32 **20** through the application process and be accepted and be
00:23:35 **21** permitted.
00:23:37 **22 A Well, yes. The claim review process exists. As to**
00:23:44 **23 the legal procedures that exist there, I'm not**
00:23:52 **24 currently familiar with those.**
00:23:53 **25 Q** Let me state it a different way. Maybe we can clear

18

00:23:56 **1** this up.
00:23:56 **2** The day that the very first claim is made under
00:23:59 **3** this Plan with respect to the LVM policy, any future
00:24:05 **4** rights whatsoever that the LVM policyholders would
00:24:09 **5** have had against the Monorail in their entirety are
00:24:13 **6** assigned over to AAC. Isn't that the way the Plan is
00:24:16 **7** supposed to operate?
00:24:17 **8 A I think it's fair.**
00:24:19 **9** MR. VAN SICKLEN: I guess I object. It calls
00:24:21 **10** for legal conclusions. There's no foundation this
00:24:24 **11** witness knows the answer to that.
00:24:27 **12** THE COURT: Your response?
00:24:28 **13** MR. WHITMER: I guess I'm trying to figure out
00:24:30 **14** if this witness knows how the Plan operates with
00:24:34 **15** respect to the LVM policy.
00:24:35 **16** THE COURT: In that respect then I will sustain
00:24:38 **17** the objection because it is asking for a legal
00:24:41 **18** conclusion, and he's indicated that he does not know
00:24:45 **19** that.
00:24:48 **20** BY MR. WHITMER:
00:24:48 **21 Q** Sir, do you have an understanding about how this Plan
00:24:51 **22** operates in the context that we've been discussing
00:24:55 **23** before the Court?
00:24:57 **24** MR. VAN SICKLEN: Wait, wait. I guess vague as
00:25:00 **25** to what context we're talking about.

19

00:25:02 **1** MR. WHITMER: I think the witness -- go ahead.
00:25:04 **2** MR. VAN SICKLEN: The legal conclusion to be
00:25:06 **3** drawn from the assignment provision? Or just
00:25:09 **4** generally about the LVM policy?
00:25:12 **5** MR. WHITMER: I think, your Honor, the witness
00:25:14 **6** said "In general I do." And I would like to follow up
00:25:16 **7** with the witness and find out what that general
00:25:18 **8** understanding is.
00:25:19 **9** THE COURT: Well, I think he's given you that.
00:25:22 **10** Your question seems to be if one bondholder out of
00:25:25 **11** many makes a claim, does that trigger all of the other
00:25:29 **12** bondholders? And his answer, I think, is no.
00:25:34 **13** You still gotta go through the claims process.
00:25:37 **14** You have to have your claim permitted. But one group,
00:25:42 **15** I'm gathering one bondholder out of a group making a
00:25:46 **16** claim and getting the permitted claim doesn't trigger
00:25:49 **17** all the rest. That's where you seem to be going.
00:25:53 **18** MR. WHITMER: Let me see if I can take this one
00:25:56 **19** other direction that might clear this all up.
00:25:58 **20 Q** After an initial claim is made -- we've been
00:26:00 **21** discussing the 2011 claim for \$36 million -- is there
00:26:05 **22** any opportunity at all for the LVM policyholders to
00:26:10 **23** obtain a penny at any point in the future from the
00:26:14 **24** Monorail?
00:26:17 **25** MR. VAN SICKLEN: From the Monorail? Wait.

20

00:26:19 **1** Objection. From the Monorail or through the Plan?

00:26:22 **2 Q** From the Monorail through the bankruptcy proceedings.

00:26:24 **3** Is there any opportunity to obtain a penny? Or have

00:26:28 **4** all those claims been assigned to AAC?

00:26:31 **5** MR. VAN SICKLEN: Objection. Calls for legal

00:26:32 **6** conclusions.

00:26:32 **7** THE COURT: It does. And unless you can show

00:26:37 **8** that he's got some sort of familiarity with the state

00:26:37 **9** of the bankruptcy proceedings in Nevada on this to

00:26:41 **10** know what's going on there, I don't know how he'd know

00:26:44 **11** the application of the bankruptcy.

00:26:44 **12** BY MR. WHITMER:

00:26:46 **13 Q** And sir, I'm just trying to find out what your

00:26:50 **14** understanding is. And I'm not asking anything about

00:26:52 **15** what's pending in the bankruptcy proceedings. What I

00:26:56 **16** want to know is with respect to whatever claim exists

00:26:59 **17** in the bankruptcy proceeding, the day after that claim

00:27:02 **18** is submitted, who owns that claim as the Plan is

00:27:05 **19** constituted?

00:27:06 **20** MR. VAN SICKLEN: Same objection.

00:27:07 **21** THE COURT: Sustained.

00:27:09 **22 Q** Let's move on to how this Plan applies to claimants

00:27:15 **23** who are making claims after the year 2020. I'll refer

00:27:21 **24** to it as post-2020 claims.

00:27:25 **25** This Plan does not provide any specifics regarding

21

00:27:29 **1** how claims arising after June 1, 2020, will be

00:27:33 **2** handled; right?

00:27:35 **3 A** **Not currently.**

00:27:36 **4 Q** The way that that is going to be addressed, as we

00:27:41 **5** understand it, the Commissioner expects to handle

00:27:44 **6** those post-2020 claims through an amendment to the

00:27:49 **7** Plan; right?

00:27:49 **8 A** **That's correct.**

00:27:50 **9 Q** And that amendment is going to be prepared at some

00:27:53 **10** point in the future; right?

00:27:55 **11 A** **That's correct.**

00:27:55 **12 Q** And no one knows what those terms are today as we sit

00:28:00 **13** in this room?

00:28:02 **14 A** **I suppose that's correct. But I expect they would be**

00:28:08 **15** **substantially similar to what exists now.**

00:28:12 **16 Q** Am I correct that the amendment that we've been

00:28:15 **17** discussing will be developed, at least in part, based

00:28:20 **18** on how the claims-paying resources for Ambac develop

00:28:25 **19** in the coming months or years?

00:28:28 **20 A** **Yes. Our Plan also allows for amendment of a plan**

00:28:34 **21** **between now and 2020 to reflect those factors and to**

00:28:41 **22** **adjust or increase payments under the Plan.**

00:28:43 **23 Q** Now, sir, shifting directions a bit here, we've heard

00:28:48 **24** a lot in this room about your experience in financial

00:28:53 **25** analyses and examinations. That's your neck of the

22

00:28:58 **1** woods; right?

00:29:00 **2 A** **I know a little bit about financial analysis of**

00:29:03 **3** **insurance companies, yes.**

00:29:04 **4 Q** And you also would agree you have a good understanding

00:29:07 **5** of basic financial principles?

00:29:09 **6 A** **A reasonable understanding, I believe, yes.**

00:29:12 **7 Q** Well, for example, you'd agree that a promise of a

00:29:15 **8** company to pay a fixed amount ten years from now is

00:29:19 **9** worth less today than a promise of the same company to

00:29:22 **10** pay that amount tomorrow. Basic principle; right?

00:29:25 **11 A** **I do understand the time value of money, yes.**

00:29:28 **12 Q** And you agree with the statement; right?

00:29:30 **13 A** **Yes. In the current trade environment, perhaps**

00:29:35 **14** **there's not very much difference, but --**

00:29:37 **15 Q** Well, you know, in Ambac's portfolio, for example,

00:29:41 **16** there are bonds from corporate borrowers that would

00:29:43 **17** work just that way. They have to pay a risk premium

00:29:46 **18** to compensate for the risk that they default in each

00:29:49 **19** year; right?

00:29:51 **20 A** **Yes. There's -- a risk premium is part of how the**

00:29:56 **21** **interest rates become accepted in the market as well**

00:30:01 **22** **as overall interest rate expectations and a number of**

00:30:07 **23** **other factors as to how a bond might be marketed.**

00:30:11 **24 Q** And that would be true even if there's no inflation.

00:30:14 **25** There's always a premium above, I don't know, say,

23

00:30:16 **1** treasuries for each year that principal is owed into

00:30:20 **2** the future?

00:30:20 **3 A** **That is the accepted view of financial scholars, yes.**

00:30:28 **4 Q** And the reason for that accepted view of financial

00:30:31 **5** scholars is because, simply put, risk compounds into

00:30:37 **6** the future; right?

00:30:40 **7 A** **Ah, yes.**

00:30:43 **8 Q** And the fact that risk compounds into the future, that

00:30:48 **9** was one of the factors that you, heading up the

00:30:52 **10** financial aspects of OCI's Plan, had to take into

00:30:56 **11** account; right?

00:30:57 **12 A** **Well, uncertainty as to the future, as you said, may**

00:31:07 **13** **be greater in more out periods as opposed to more in**

00:31:14 **14** **the near term.**

00:31:15 **15 Q** And you were here when Commissioner Dilweg testified

00:31:18 **16** about that point a few days ago; right?

00:31:20 **17 A** **Well, I think I understand the general testimony that**

00:31:25 **18** **you're referring to, yes.**

00:31:26 **19 Q** And putting his testimony aside, let's talk about

00:31:31 **20** yours. You agree there are a lot of uncertainties

00:31:34 **21** that are presented by the issues before the Court

00:31:36 **22** today; right?

00:31:37 **23** MR. VAN SICKLEN: Your Honor, I think we're

00:31:38 **24** certainly in the re-plowed category.

00:31:41 **25** THE COURT: I would agree. Sustain the

24

00:31:42 **1** objection.

00:31:43 **2 Q** Sir, yesterday you explained to the Court that OCI had

00:31:47 **3** made efforts to treat policyholders as fair as

00:31:50 **4** possible given the circumstances. That was your

00:31:54 **5** testimony; right?

00:31:55 **6 A Yes.**

00:31:56 **7 Q** And the circumstances that we have here today present

00:32:01 **8** a lot of uncertainties. That's a point you would

00:32:04 **9** agree with?

00:32:05 **10 A Yes. And in fact, our Plan is developed to be a**

00:32:12 **11 flexible, scaleable plan that deals with those**

00:32:16 **12 uncertainties.**

00:32:17 **13 Q** One thing that's not flexible about the Plan, let me

00:32:22 **14** propose to you, is that if this Plan is confirmed,

00:32:28 **15** there's no flexibility about whether that 25-cent

00:32:32 **16** piece will be changed, for example, to 15 cents in

00:32:36 **17** January of 2011. That's not something contemplated

00:32:39 **18** right now by OCI; is it?

00:32:41 **19 A Not contemplated.**

00:32:43 **20 Q** Would you agree, based on the finance principles we

00:32:48 **21** talked about and your experience, in order to ensure

00:32:52 **22** equitable treatment of policyholders, there should be

00:32:56 **23** an equal probability that each policyholder will be

00:33:00 **24** paid out equally on its claims; correct?

00:33:05 **25 A Equal probability that each policyholder would be paid**

25

00:33:14 **1 an equal amount?**

00:33:15 **2 Q** To the extent that that's possible.

00:33:17 **3 A I'm not sure I understand what that means.**

00:33:19 **4 Q** To the extent it's possible to ensure in this

00:33:22 **5** proceeding that there's equal probability that each

00:33:26 **6** policyholder will at the end of the day, whether it's

00:33:29 **7** 2050, 2060, 2070, whatever the end of the day is, that

00:33:33 **8** each policyholder will have been paid out equally on

00:33:37 **9** its claims.

00:33:37 **10 A Again, when you say there's an equal probability, I**

00:33:42 **11 don't know what that means because that probability is**

00:33:44 **12 equal to what? Across what range? With what**

00:33:47 **13 assumptions?**

00:33:48 **14** MR. VAN SICKLEN: I don't understand what "equal

00:33:50 **15** probability" means in that context. I understand what

00:33:53 **16** "equal payments" means.

00:33:55 **17 Q** Well, if we were all sitting here in 2070, we could

00:34:00 **18** all talk about whether the policyholders were paid

00:34:03 **19** equally under the Plan. That's something we can't do

00:34:06 **20** because it's not 2070.

00:34:07 **21 A I'll mark my calendar for that.**

00:34:09 **22 Q** So instead, what we're left to do is to try to figure

00:34:12 **23** out to the best ability possible that there's equal

00:34:16 **24** probability that when we sit in this room in 2070 that

00:34:20 **25** all the policyholders would have been paid out

26

00:34:23 **1** equally.

00:34:23 **2 A Again, equal probability I don't believe makes a**

00:34:26 **3 particular amount of sense in your question. But I**

00:34:29 **4 will attempt to respond that OCI understands that**

00:34:35 **5 there needs to be a mechanism or we needed to guard**

00:34:44 **6 against the possibility that we couldn't sustain 25**

00:34:47 **7 percent cash payments. And we have evaluated that**

00:34:54 **8 using stress conditions for the Segregated Account**

00:35:00 **9 business as well as on the General Account business.**

00:35:05 **10 We've taken conservative assumptions as to the value**

00:35:09 **11 of the assets of the company. And we believe without**

00:35:15 **12 certainty, of course, because certainty, as you've**

00:35:17 **13 pointed out, is not possible, but we believe that we**

00:35:22 **14 have established the 25 percent in a conservative and**

00:35:27 **15 quite prudent manner.**

00:35:29 **16 Q** And we'll turn to that in a second. But before we get

00:35:32 **17** there, I'd like to just briefly address the four

00:35:35 **18** scenarios that you've presented to this Court.

00:35:37 **19** You've talked about the analysis that was done to

00:35:41 **20** prepare the four scenarios. I don't want to repeat

00:35:45 **21** that. But what I don't think I've heard answered is

00:35:49 **22** has OCI or AAC undertaken any attempt to analyze the

00:35:53 **23** probability that Scenario 1, for example, we've got a

00:36:01 **24** 15 percent probability of being Scenario 1, 20 percent

00:36:06 **25** probability Scenario 2, 17 percent probability

27

00:36:11 **1** Scenario 3 -- I'm just making up numbers here. Has

00:36:15 **2** there be any analysis undertaken along that line?

00:36:18 **3 A Other than the fact that some underlying data to the**

00:36:21 **4 model, such as a moodyeconomics.com information, is --**

00:36:27 **5 has judgmental probabilities associated with those**

00:36:34 **6 outcomes as presented by the Moody's people, no.**

00:36:43 **7 The other factors haven't been weighed to try to**

00:36:47 **8 assign specific probabilities. It's impossible to do**

00:36:52 **9 that. You'd have to have statistical distributions of**

00:36:55 **10 the possible outcomes for each of those variables in**

00:37:00 **11 the equation. That kind of thing doesn't exist. It**

00:37:07 **12 exists in the judgment of an entity like Moody's that**

00:37:13 **13 puts together certain data sets and publishes that we**

00:37:17 **14 relied on. But as to other factors, you don't -- you**

00:37:24 **15 don't have the statistical database to go say that,**

00:37:29 **16 you know, the work through the calculations say that**

00:37:32 **17 the outcome has a 14 percent probability. That just**

00:37:36 **18 doesn't exist.**

00:37:38 **19 Q** So we'll get to Moody's in a second. But before we

00:37:42 **20** get there, would you agree with me that the best way

00:37:46 **21** to determine which of the four scenarios is ultimately

00:37:52 **22** most probable, you would have to look at, like you

00:37:55 **23** did, the underlying risks that provide insight as to

00:38:02 **24** those four scenarios; right?

00:38:04 **25 A We have some insight as to possible outcomes. But,**

28

00:38:13 **1** again, those are judgments that are subject to

00:38:18 **2** substantial variability.

00:38:20 **3 Q** And put it this way. In order to know the probability

00:38:26 **4** of the four scenarios, you would really need to know

00:38:29 **5** the probabilities with respect to the loss

00:38:32 **6** development, as you've been testifying about, and

00:38:35 **7** also, for example, the R and W remediation efforts.

00:38:38 **8** Those are important factors when trying to consider

00:38:40 **9** the probabilities?

00:38:41 **10 A** We identify those as the two most important factors.

00:38:47 **11** But, of course, the loss development involves quite a

00:38:54 **12** number of underlying factors that will affect mortgage

00:38:58 **13** default or the severity of mortgage default.

00:39:03 **14** Likewise, the recoveries on the reps and

00:39:06 **15** warranties litigation also involves many legal factors

00:39:11 **16** and collectability issues and the like.

00:39:14 **17 Q** These two factors that we're talking about, loss

00:39:17 **18** development and R and W remediations, as OCI looked at

00:39:21 **19** those two concepts, one of the main things that it was

00:39:26 **20** doing was trying to balance the risks both to

00:39:29 **21** short-term claimants as compared to long-term

00:39:32 **22** claimants; correct?

00:39:34 **23 A** The action that we took to put the Segregated Account

00:39:39 **24** into rehabilitation was premised on that need to

00:39:46 **25** restrain short-term payments in order to protect the

29

00:39:51 **1** broad base of policyholders, long-tail as well as

00:39:55 **2** short-tail.

00:39:55 **3 Q** Well, let's turn to the Disclosure Statement because I

00:39:59 **4** think it's addressed quite directly. It's Exhibit 27

00:40:03 **5** at page 69.

00:40:17 **6 A** Page 69 you said?

00:40:19 **7 Q** Correct. And sir, my question to you, we were talking

00:40:31 **8** about whether one of the things OCI was looking at was

00:40:35 **9** attempting to balance risks between short- and

00:40:38 **10** long-term policyholders. And you were describing that

00:40:40 **11** there are two primary risks that OCI evaluated. The

00:40:45 **12** first one was loss development; right?

00:40:50 **13 A** Well, the use of the word "primary" may be somewhat

00:40:56 **14** misleading. But they were significant ones that we

00:41:00 **15** that we utilized. That's fine, yes.

00:41:03 **16 Q** Sir, you say it's misleading, but --

00:41:06 **17 A** Well, I mean, yes, there's four scenarios that include

00:41:09 **18** those two factors at severe-case or stress-case and

00:41:16 **19** base-case recoveries zero and recoveries that the

00:41:22 **20** companies estimate.

00:41:22 **21 Q** But to be clear, the only two factors that were

00:41:26 **22** changed for these four scenarios, these are the two

00:41:31 **23** factors?

00:41:31 **24 A** That's correct.

00:41:31 **25 Q** Loss development and R and W remediation recoveries?

30

00:41:35 **1 A** That's correct, yes.

00:41:35 **2 Q** So for me to say it's a primary factor, that's really

00:41:39 **3** not misleading; is it?

00:41:41 **4 A** No. All right. They were primary, fine.

00:41:43 **5 Q** Let's take a look at loss development, the first of

00:41:47 **6** your two factors the top of page 69.

00:41:49 **7 A** Uh-huh (affirmative).

00:41:49 **8 Q** I'm going to read the last sentence of paragraph A,

00:41:54 **9** and what I'd like for you to tell us is whether it's

00:41:56 **10** true and accurate to your knowledge. Okay?

00:41:59 **11** "If loss development were to continue to exceed

00:42:04 **12** expectations and the cash percentage were set too

00:42:08 **13** high, the resulting diminution of claims-paying

00:42:13 **14** resources could lead to inequitable treatment for

00:42:17 **15** holders of long-dated policy claims, as claims-paying

00:42:20 **16** resources may be exhausted in the payment of

00:42:23 **17** short-dated policy claims before long-dated policy

00:42:27 **18** claims matured."

00:42:29 **19 A** That's what it says.

00:42:30 **20 Q** I know it says that. Is it true and accurate, to your

00:42:33 **21** knowledge?

00:42:33 **22 A** Yes, it is. And in fact, I think that documents our

00:42:36 **23** awareness of the risk and the fact that we considered

00:42:41 **24** that risk in devising the Plan that we have in front

00:42:46 **25** of the Court.

31

00:42:46 **1 Q** Right. Isn't the point you're making here that

00:42:50 **2** increasing the cash percentage increases the risk that

00:42:55 **3** adverse loss development will negatively impact

00:42:58 **4** long-tail policyholders?

00:43:01 **5 A** That's correct.

00:43:02 **6 Q** As opposed to short-tail?

00:43:04 **7 A** That's correct, yes.

00:43:04 **8 Q** Now, yesterday you discussed some probability analyses

00:43:13 **9** that were conducted on loss development; right?

00:43:16 **10 A** Yes. We had some testimony about probabilities.

00:43:21 **11 Q** One of the things you explained for the Court was that

00:43:27 **12** to test the loss development in the Segregated

00:43:33 **13** Account, you looked to Moody's Analytics; right?

00:43:37 **14 A** Well that was a baseline kind of a data feed into

00:43:45 **15** reserving models, yes.

00:43:47 **16 Q** When you say a baseline data feed, another way of

00:43:53 **17** saying that is that the Moody's Analytics that you

00:43:57 **18** used is sort of the foundation upon which your model

00:44:00 **19** was built; right?

00:44:02 **20 A** That's reasonable, yes.

00:44:04 **21 Q** You said yesterday that OCI used S3 to do the

00:44:14 **22** analysis; right?

00:44:16 **23 A** In the stress case, yes.

00:44:17 **24 Q** And when you say "stress case," you're saying that's,

00:44:21 **25** in colloquial terms, worst-case scenario is the same

32

00:44:26 **1** thing as stress-case?

00:44:27 **2 A No. I wouldn't say that.**

00:44:29 **3 Q** Stress case is, as you're looking at your four

00:44:32 **4** different models or your four different analyses,

00:44:36 **5** stress case is one of the terms that's been used in

00:44:38 **6** the Disclosure Statement with respect to those four

00:44:41 **7** models; right?

00:44:42 **8 A Yes.**

00:44:43 **9 Q** I've looked through the Disclosure Statement

00:44:48 **10** carefully. I may have missed it, but, you know, is

00:44:51 **11** there anything about S3 stated anywhere in the

00:44:56 **12** Disclosure Statement, do you know?

00:44:57 **13 A I don't recall whether there is or not. It's a --**

00:45:07 **14 Q** S3, that actually stands for, in Moody's parlance,

00:45:11 **15** Scenario 3; right?

00:45:14 **16 A Yes. I believe that's correct.**

00:45:15 **17 Q** Okay. And could you tell the Court how many scenarios

00:45:19 **18** there are presented by Moody's in the 2010 time frame?

00:45:23 **19 A I don't recall with certainty.**

00:45:31 **20 Q** Well, there's six; right? Six. That's correct; isn't

00:45:33 **21** it? Six different Moody's scenarios?

00:45:36 **22 A That could be correct. Actually, my vague**

00:45:39 **23** **recollection was that there were five. But I could --**

00:45:43 **24** **I could be wrong. It could be six.**

00:45:45 **25 Q** Okay. So when we say 3, S3, we're actually talking

33

00:45:50 **1** about Scenario 3 as provided for by Moody's Analytics;

00:45:54 **2** correct?

00:45:54 **3 A Yes.**

00:45:55 **4 Q** And there was some question yesterday about what time

00:45:58 **5** frame you looked at to determine this S3 analysis, and

00:46:03 **6** I think you said you used numbers as of June 30th. Do

00:46:07 **7** you know which specific Moody's Analytics tool you

00:46:11 **8** used?

00:46:11 **9 A I testified yesterday that I didn't know what data set**

00:46:16 **10** **we used. But we had regular access to the Moody's**

00:46:22 **11** **Analytics. I presume that we used the most recent**

00:46:26 **12** **available at the time.**

00:46:26 **13 Q** So while we may not know the exact tool you used,

00:46:31 **14** you'd agree with me that the tool you used would have

00:46:34 **15** been somewhere in the mid 2010 time frame?

00:46:37 **16 A I believe that's correct.**

00:46:39 **17 Q** So let's go to the scenarios.

00:46:43 **18** You'd agree that in Moody's parlance, Scenario 1,

00:46:50 **19** that's sort of the -- well, in your own words, what's

00:46:54 **20** the difference between the scenarios as you go from

00:46:57 **21** Scenario 1 to Scenario 2 and you climb up that ladder?

00:47:00 **22 A Well, Moody's Analytics describes those scenarios. If**

00:47:08 **23** **there's a reference document that you're familiar**

00:47:11 **24** **with, we could look at that.**

00:47:13 **25 Q** Well --

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00:47:15 **1 A But S1 is a more optimistic scenario. S3 is less**

00:47:21 **2** **optimistic, as I testified to yesterday. Kind of,**

00:47:26 **3** **again, ah, the belief is that S1 -- or Moody's**

00:47:34 **4** **represents an S1, there's a probability -- a 90**

00:47:38 **5** **percent probability the actual outcomes may be worse**

00:47:41 **6** **than that scenario, 10 percent that they would be**

00:47:44 **7** **better.**

00:47:45 **8** **Conversely, an S3, the representations are or**

00:47:50 **9** **their expectations are that the actual outcomes, 90**

00:47:55 **10** **percent of the actual outcomes would be better than**

00:47:57 **11** **the S3 estimate, 10 percent worse than.**

00:48:01 **12 Q** So just to follow up on what you just described, as

00:48:04 **13** you go from Scenario 1 to Scenario 2, Scenario 1 is

00:48:09 **14** assuming a better case economic forecast --

00:48:12 **15 A That's correct.**

00:48:13 **16 Q** -- than Scenario 2 is; right?

00:48:14 **17 A That's correct.**

00:48:15 **18 Q** And Scenario 2 is assuming a better case economic

00:48:19 **19** forecast than Scenario 3?

00:48:21 **20 A That's correct.**

00:48:21 **21 Q** And Scenario 3 is assuming a better-off economic

00:48:27 **22** forecast than Scenario 4; right?

00:48:30 **23 A I believe that's correct. But I -- you know, I**

00:48:37 **24** **haven't looked at each of those scenarios. There are**

00:48:41 **25** **scenarios that are, you know, that predict essentially**

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00:48:48 **1** **another Great Depression, yeah.**

00:48:50 **2 Q** Well, let's assume, you know, five or six scenarios.

00:48:55 **3** I think you said you thought there were five. Whether

00:48:59 **4** there's five or six, the modeling you did and OCI did

00:49:03 **5** was with respect to Scenario 3. That's the one you

00:49:05 **6** described for the Court yesterday, S3?

00:49:08 **7 A Yes.**

00:49:08 **8 Q** Did OCI also conduct modeling using the information at

00:49:16 **9** S4?

00:49:17 **10 A No, we did not.**

00:49:18 **11 Q** Was that option considered?

00:49:23 **12 A We believed that the modeling using S3 as well as**

00:49:32 **13** **additional judgmental cushion and prudence that we**

00:49:41 **14** **built into the Plan is adequate to protect policies**

00:49:47 **15** **from that risk that you're describing, that the**

00:49:53 **16** **25-cent cash payment couldn't be sustained and that**

00:49:58 **17** **recoveries of the 25 cents previously made may be**

00:50:04 **18** **difficult to achieve.**

00:50:05 **19 Q** So can you give us a sense, was the idea, hey, maybe

00:50:11 **20** we ought to check out S4, just run it real quickly and

00:50:15 **21** see what the numbers -- did that even come up?

00:50:21 **22 A I don't recall whether it did or didn't at this point.**

00:50:24 **23 Q** Who was the one responsible for deciding whether the

00:50:27 **24** modeling would be done in S3 as opposed to S2 or S4 or

00:50:32 **25** some other S?

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00:50:33 **1 A I would work through those kind of decisions in**
00:50:38 **2 conjunction with the financial advisors.**
00:50:41 **3 Q** So there were various people involved.
00:50:43 **4** Who had the ultimate decision on that issue? Was
00:50:46 **5** that you, sir?
00:50:47 **6 A Perhaps I had as much influence on that decision as**
00:50:52 **7 anyone. You know, ultimately, information was**
00:50:58 **8 provided to the Commissioner as Rehabilitator and**
00:51:05 **9 Deputy Commissioner Shawl as Special Deputy, you know,**
00:51:10 **10 at perhaps more summarized fashion. So as to a detail**
00:51:18 **11 like that, ah, I may have had as much influence on**
00:51:22 **12 that decision as anybody, yes.**
00:51:23 **13 Q** So to tie the pieces together here, as we're looking
00:51:28 **14** at the four scenarios that are modeled in the
00:51:32 **15** disclosure forms presented to the Court, all of those
00:51:35 **16** models are based on or a foundation of those models is
00:51:39 **17** the S3 Moody's financial outlook; right?
00:51:45 **18 A If you refer to the stress case, yes.**
00:51:46 **19 Q** There's been discussion in this room about what might
00:51:54 **20** happen in the future. There's been lots of talk about
00:51:57 **21** double-dip session, whether it might happen, whether
00:52:00 **22** it not. I'm not gonna ask you all those questions.
00:52:03 **23** But I am gonna ask you this.
00:52:05 **24** What is the assumption in the S3 scenario with
00:52:11 **25** respect to the economic outlook compared to, for

37

00:52:16 **1** example, what we just went through in 2008 and 2009?
00:52:20 **2 A Well, S3 is essentially a double-dip scenario. You**
00:52:30 **3 know, the severity of that second dip I'm not prepared**
00:52:34 **4 to -- I don't recall or I couldn't make a comparison**
00:52:37 **5 as to, ah, the previous 24, 36 months.**
00:52:43 **6 Q** Sir, isn't it true that S3 assumes an outlook that is
00:52:50 **7** less severe than the 2008 and 2009 downturn?
00:52:55 **8** MR. VAN SICKLEN: Objection. The witness just
00:52:57 **9** answered the question to the best he could.
00:52:58 **10** THE COURT: Sustained.
00:53:00 **11 Q** Sir, do you know whether the S3 scenario, one way or
00:53:09 **12** the other whether it assumes an outcome less severe
00:53:11 **13** than the 2008 and 2009 downturn?
00:53:15 **14 A I answered the question previously. I can't -- I'm**
00:53:18 **15 not in a position to compare the out year projections**
00:53:23 **16 of scenario S3 as to the conditions that exist -- you**
00:53:31 **17 know, could I evaluate that? Yes. I don't have that**
00:53:34 **18 information in my -- in my memory.**
00:53:37 **19 Q** You would agree you wouldn't have to evaluate that.
00:53:40 **20** You could just go to the website economy.com and look
00:53:44 **21** and see what Moody's has to say; right? Right?
00:53:47 **22 A I'm not familiar with what information is available**
00:53:51 **23 through their website. These are subscriptions that**
00:53:54 **24 you need to get, but --**
00:53:57 **25 Q** I thought it was you yesterday, sir, that said you'd

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00:54:01 **1** have to go to economy.com. I thought those were your
00:54:06 **2** words.
00:54:06 **3 A That is the name of the service, as I understand it.**
00:54:14 **4 I didn't personally go to the Moody's Analytics site**
00:54:21 **5 to obtain the information.**
00:54:24 **6 Q** Let's assume S3 for a moment. Yesterday you testified
00:54:29 **7** about the difference between a 10 percent versus a 90
00:54:33 **8** percent probability under S3. I think you referenced
00:54:37 **9** it again today.
00:54:39 **10** Am I correct that under S3, there's still a 10
00:54:43 **11** percent chance that the modeling will result in
00:54:46 **12** something worse than what S3 has presented?
00:54:50 **13 A That's -- yes, that's what I testified to.**
00:54:52 **14 Q** And is that a weighted average? You're familiar with
00:54:55 **15** the concept of weighted average; right?
00:54:57 **16 A I am familiar with the concept of weighted average,**
00:54:59 **17 yes.**
00:54:59 **18 Q** Is that 10 percent a weighted average?
00:55:02 **19 A I don't know how they developed that -- that**
00:55:07 **20 allocation of possible outcomes in comparison to the**
00:55:11 **21 scenario.**
00:55:12 **22 Q** As you're looking at probabilities in the world of
00:55:15 **23** finance, if you were to say there was a probability of
00:55:18 **24** distribution of 90/10, you would agree that really
00:55:21 **25** doesn't tell you anything unless you know whether it's

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00:55:23 **1** a weighted average; right?
00:55:24 **2 A Ah, I don't think that's necessarily true.**
00:55:29 **3 Q** Well, you'd agree that a weighted average tells you a
00:55:31 **4** lot more than what you'd know without a weighted
00:55:34 **5** average?
00:55:35 **6** MR. VAN SICKLEN: Your Honor, I think we're kind
00:55:36 **7** of straying from the relevant point.
00:55:38 **8** THE COURT: I believe we are too. I'll sustain
00:55:40 **9** the objection.
00:55:40 **10 Q** Sir, you'd agree with me that the projections that OCI
00:55:45 **11** --
00:55:45 **12** THE COURT: Well, I had to tell Mr. Bensky
00:55:47 **13** yesterday, and I'll have to tell you, "you would agree
00:55:49 **14** with me," that compounds the question to start with.
00:55:53 **15** Then you make a statement; then you ask a question.
00:55:55 **16** So, please, unless you want to inform the witness of
00:56:01 **17** what you know, what your understandings are, ah, so
00:56:05 **18** that he then can evaluate those, you're asking an
00:56:09 **19** improper question.
00:56:11 **20** BY MR. WHITMER:
00:56:11 **21 Q** Sir, am I correct that -- okay.
00:56:16 **22** Sir, the projections that OCI has presented to the
00:56:20 **23** Court --
00:56:20 **24** THE COURT: Mr. Whitmer, you do that again and
00:56:23 **25** Mr. Bensky is gonna hit you with that cheesehead.

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00:56:27 **1 Q** The projections that OCI has presented to this Court
00:56:32 **2** may be materially understated; correct?
00:56:36 **3 A** **There is a possible for that to be the case.**
00:56:41 **4 Q** Let me be more specific.
00:56:43 **5** The ultimate losses resulting from General Account
00:56:49 **6** policies may exceed both the General Account base-case
00:56:54 **7** loss estimates and the General Account stress-case
00:56:58 **8** loss estimates perhaps materially; correct?
00:57:03 **9 A** **That sounds as if you're reading from a portion of the**
00:57:06 **10 Plan.**
00:57:06 **11 Q** It's right in there. So you agree with that
00:57:09 **12** statement?
00:57:10 **13 A** **Yes. It's possible.**
00:57:11 **14 Q** And the same goes for the Segregated Account policies.
00:57:16 **15** The ultimate losses resulting from the policies may
00:57:21 **16** exceed both the Segregated Account base-case loss
00:57:25 **17** estimates and the Segregated Account stress-case loss
00:57:30 **18** estimates perhaps materially; correct?
00:57:35 **19 A** **That's correct. I would also testify that, as I've**
00:57:41 **20 noted before, the Plan as its devised is flexible and**
00:57:46 **21 that we -- OCI is not precluded from taking additional**
00:57:53 **22 action to protect the policyholders in some of those**
00:57:59 **23 worst-case scenarios if they were in fact to develop.**
00:58:03 **24 Q** Okay.
00:58:04 **25 A** **We're not --**

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00:58:06 **1 Q** Go ahead.
00:58:10 **2 A** **This isn't designed to be cast in stone for today. We**
00:58:13 **3 intend to monitor the financial condition of the**
00:58:17 **4 Segregated Account and the General Account very**
00:58:19 **5 closely going forward. And we'll be in a position, I**
00:58:24 **6 believe, to make appropriate decisions and take**
00:58:29 **7 reasonable actions if and when they become necessary.**
00:58:34 **8 Q** We've been talking about these questions in the
00:58:38 **9** context of loss development. I'm going to turn your
00:58:41 **10** attention to the context of R and W remediation
00:58:44 **11** recoveries. This is another issue discussed at length
00:58:49 **12** in the Disclosure Statement.
00:58:51 **13** You would agree -- sorry.
00:58:54 **14** With respect to the R and W remediations,
00:58:57 **15** increasing the cash percentage also increases the risk
00:59:01 **16** that adverse R and W remediation recoveries will
00:59:05 **17** negatively impact long-tail claimants in favor of
00:59:08 **18** short-tail; correct?
00:59:09 **19 A** **Similarly to that criteria, the loss development**
00:59:13 **20 criteria, yes.**
00:59:14 **21 Q** So the point being made on this issue in the
00:59:17 **22** Disclosure Statement, isn't it really that as you
00:59:20 **23** lower the cash percentage payout, that lowers the risk
00:59:25 **24** to long-tail claimants?
00:59:29 **25 A** **Yes, there's -- that is true.**

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00:59:32 **1 Q** So if you were at 30 cents on the dollar as an initial
00:59:38 **2** cash payout and you lowered that number to 20 cents,
00:59:43 **3** that -- the net --the effect of that is lowering the
00:59:47 **4** risk to long-tail claimants?
00:59:49 **5 A** **I would point out that under S4 or Scenario 4 of our**
00:59:54 **6 Disclosures, assuming those adverse outcomes in terms**
01:00:00 **7 of loss development and remediation, that the**
01:00:05 **8 projected ultimate value of the surplus notes is still**
01:00:13 **9 somewhere in the range of 45 cents on the dollar.**
01:00:15 **10 That shows that there is a significant cushion above**
01:00:21 **11 the 25-cent cash payments that we have set the Plan**
01:00:28 **12 at.**
01:00:28 **13 Q** But what you just testified to, that's not actually
01:00:32 **14** accurate. You didn't use S4. You used S3. You meant
01:00:35 **15** S3; right?
01:00:36 **16 A** **No. When I said S4, I was referring to our scenarios**
01:00:40 **17 in the Disclosure Plan, Scenario 4 of our Disclosures.**
01:00:44 **18 Q** Different Scenario 4. I understand.
01:00:47 **19 A** **Yes.**
01:00:49 **20 Q** The assumption that's built into the answer that you
01:00:55 **21** just made is that, number one, the Moody's S3 was the
01:00:59 **22** right economic forecast to use; correct?
01:01:03 **23 A** **It was a reasonable forecast to use. And on top of**
01:01:07 **24 that, we put a certain amount of additional -- we've**
01:01:12 **25 judgmentally provided for additional cushion beyond**

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01:01:18 **1 the loss development that would result to the**
01:01:22 **2 Segregated Account, the RMBS policies resulting from**
01:01:27 **3 an S4 -- or excuse me -- S3 loss development.**
01:01:33 **4 Q** So there's a 10 percent chance that under the S3
01:01:38 **5** economic forecast, this is going to be something worse
01:01:41 **6** than what was modeled?
01:01:42 **7** MR. VAN SICKLEN: Objection. We're getting very
01:01:44 **8** cumulative.
01:01:45 **9** THE COURT: Sustained.
01:01:45 **10 Q** Sir, as we were discussing, as you go from 20 cents
01:01:48 **11** down to 15 cents down to 10 cents down to 5 cents,
01:01:52 **12** every increment as you go down closer to zero, you are
01:01:56 **13** lowering the risk that long-tail claimants won't
01:02:00 **14** ultimately get paid on par with the short-tail
01:02:03 **15** claimants?
01:02:04 **16** MR. VAN SICKLEN: Objection. Cumulative.
01:02:05 **17** THE COURT: Sustained.
01:02:07 **18 Q** If the Segregated Account became unable to continue
01:02:14 **19** paying the initial cash percentage, holders of
01:02:18 **20** long-dated policy claims would clearly be treated
01:02:21 **21** inequitably in comparison with holders of short-dated
01:02:25 **22** policy claims; correct?
01:02:26 **23** MR. VAN SICKLEN: Same objection.
01:02:27 **24** THE COURT: Sustained.
01:02:30 **25** MR. WHITMER: Your Honor --

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01:02:31 **1** MR. VAN SICKLEN: I think part of the problem
01:02:34 **2** here is that Mr. Bentley and Mr. Whitmer represent the
01:02:36 **3** same economic perspective from the same policy. So
01:02:39 **4** we're getting a double dose of exactly the same line
01:02:43 **5** of questioning and it's extremely cumulative.
01:02:46 **6** MR. WHITMER: Your Honor, this is what my last
01:02:48 **7** question -- and it's an interesting objection. It's
01:02:51 **8** right out of the Disclosure Statement, so perhaps we
01:02:53 **9** could turn there.
01:02:54 **10** The Disclosure Statement, as I understand, was
01:02:56 **11** not submitted to this Court, you know, pursuant to an
01:03:00 **12** affidavit or under oath. I'm just trying to verify
01:03:02 **13** that the statements made in there, and specifically
01:03:04 **14** that one, are true and accurate based on
01:03:07 **15** Mr. Peterson's testimony.
01:03:08 **16** MR. VAN SICKLEN: Same objection. Mr. Peterson
01:03:10 **17** has been asked and re-asked multiple times this same
01:03:16 **18** line of questioning about the uncertain future and
01:03:18 **19** will he adjust it.
01:03:19 **20** THE COURT: The broad themes have certainly been
01:03:22 **21** gone over. You can twist it and you can turn it, but
01:03:25 **22** they still have been looked at. And his answer I
01:03:29 **23** think has been consistent.
01:03:30 **24** **Q** Sir, I just -- could we turn to Exhibit 27 at page 70.
01:03:34 **25** And I'm going to direct the witnesses and the Court's

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01:03:37 **1** attention to the sentence from the Disclosure
01:03:42 **2** Statement that we're referring to. Page 70, Exhibit
01:03:47 **3** 27.
01:03:47 **4** **A** I'm looking at it.
01:03:48 **5** **Q** Paragraph E. Under "Conclusion," second sentence.
01:04:01 **6** I'm just gonna ask you, that sentence, "If the
01:04:05 **7** Segregated Account became unable to continue paying
01:04:09 **8** the initial cash percentage, holders of long-dated
01:04:10 **9** policy claims would clearly be treated inequitably in
01:04:15 **10** comparison with holders of short-dated policy claims,"
01:04:17 **11** do you agree with that statement?
01:04:19 **12** **A** Yes, I do.
01:04:20 **13** **Q** And the best way -- well, let's turn for a moment and
01:04:33 **14** come back. Let's turn to surplus notes for a moment.
01:04:36 **15** You've been here in the room -- there's been a lot
01:04:42 **16** of talk about when the surplus notes will be paid out,
01:04:44 **17** and you were here when the Commissioner explained that
01:04:46 **18** the goal is to have these paid out by 2020. That's
01:04:51 **19** your understanding too, 2020 is the goal?
01:04:54 **20** **A** Um, I wouldn't -- no, I wouldn't agree that there's a
01:05:01 **21** goal to have the surplus notes paid out by 2020.
01:05:07 **22** **Q** Why not?
01:05:08 **23** **A** We're going to annually evaluate the ability, the
01:05:15 **24** reasonableness of making payments on surplus notes.
01:05:18 **25** And if it can be done such, you know, that things

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01:05:24 **1** develop positively and we can act still with prudence
01:05:31 **2** and make payments and pay them out in total by 2020,
01:05:36 **3** that would be great.
01:05:37 **4** But the risk that long-dated policyholders might
01:05:46 **5** not get paid in the same percentage that shorter-date
01:05:51 **6** policyholders is likely to exist for some time, and
01:05:54 **7** we're gonna continue to, as best we can, balance that
01:06:01 **8** and protect those long-term policyholders without --
01:06:09 **9** to a reasonable extent, to a prudent and reasonable
01:06:13 **10** extent, not to the 99.99999 percent protection, but to
01:06:19 **11** a high degree of protection. And we're gonna evaluate
01:06:22 **12** that. If that puts us in a position where we can't
01:06:25 **13** fully pay out on the surplus notes by 2020, then the
01:06:31 **14** Plan will have to be adjusted, notes reissued, some
01:06:37 **15** kind of amendment to continue some type of
01:06:43 **16** rehabilitation plan post-2020.
01:06:44 **17** **Q** Whether the goal is to pay out by 2020 or not, one
01:06:48 **18** thing that's clear is that the maturity date for the
01:06:51 **19** surplus notes is 2020?
01:06:52 **20** **A** That's clear, yes.
01:06:53 **21** **Q** And if we were to look at the four scenarios that
01:06:59 **22** we've been talking about in this courtroom and were to
01:07:02 **23** evaluate under any of the four scenarios, the
01:07:05 **24** number-one case scenario, which is the best-case, all
01:07:09 **25** the way down to the fourth, which is the worst, would

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01:07:13 **1** there be sufficient claims-paying resources for the
01:07:18 **2** surplus notes to be paid in 2020 under any of those
01:07:23 **3** four scenarios?
01:07:25 **4** **A** We haven't modeled assumptions about that that include
01:07:37 **5** payment assumptions through the model.
01:07:40 **6** In Scenario 1 of our -- of our Disclosure, it
01:07:50 **7** shows full payment on the surplus notes. Whether in
01:07:55 **8** fact that would be possible by the year 2020 is not
01:08:00 **9** demonstrated in that model.
01:08:04 **10** **Q** Can't you just look at the first scenario and look at
01:08:11 **11** 2020 and just tell right there and then that there are
01:08:15 **12** insufficient claims-paying resources to pay the
01:08:17 **13** surplus notes on that date? Am I misunderstanding
01:08:20 **14** that?
01:08:21 **15** **A** Well, that also makes -- I'd have to give that some
01:08:28 **16** thought, actually.
01:08:30 **17** **Q** Isn't it important that we do give that some thought?
01:08:33 **18** I mean, if the Scenario 1, the best-case scenario
01:08:36 **19** being presented to this Court, if it were correct that
01:08:39 **20** under the very best set of circumstances as projected
01:08:42 **21** by OCI, there still would be insufficient
01:08:45 **22** claims-paying resources in 2020?
01:08:46 **23** MR. VAN SICKLEN: I think that mischaracterizes
01:08:48 **24** the witness's testimony about the best possible case.
01:08:53 **25** MR. WHITMER: Your Honor, what I'm referring to

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01:08:55 **1** are the four scenarios that are before this Court.

01:08:57 **2** THE COURT: I understand that. And I would

01:08:58 **3** agree with the objector. Not yourself. The other

01:09:01 **4** one.

01:09:04 **5** BY MR. WHITMER:

01:09:04 **6** **Q** Just to close out this topic, is it your testimony you

01:09:12 **7** just don't know one way or the other whether there

01:09:14 **8** would be sufficient claims-paying resources under the

01:09:17 **9** best of the four scenarios to pay out surplus notes in

01:09:20 **10** full in 2020?

01:09:21 **11** **A Not while I sit here on this witness stand.**

01:09:25 **12** **Q** So, moving on, sir, to the issue we've been talking

01:09:36 **13** about, which is the equal probability of payout to

01:09:40 **14** both short- and long-term policyholders, we've talked

01:09:43 **15** about how if we were here in 2070, we would all know,

01:09:47 **16** but we're here in 2010, so we don't.

01:09:49 **17** I'm going to present to you about three options,

01:09:52 **18** talk to you briefly about each of the three options.

01:09:55 **19** And let me know whether this would ensure equal

01:09:57 **20** probability to short-term and long-term policyholders

01:10:00 **21** of getting paid out equally.

01:10:02 **22** The first one is one that we've had a lot of

01:10:05 **23** discussion about why this isn't something that OCI

01:10:07 **24** wants to do. But one thing we can do is just not pay

01:10:10 **25** any initial cash payment out until 2070, and then we

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01:10:14 **1** would know for certain how to allocate those monies

01:10:17 **2** fairly. That's conceptually, at least, one option?

01:10:20 **3** **A Conceptually, that's an option. We could put the**

01:10:23 **4** **funds on deposit with the -- with Lafayette County.**

01:10:28 **5** **Q** You've given me a fourth option I wasn't planning on

01:10:31 **6** going into. But we'll talk briefly about that too.

01:10:34 **7** Ah, the second option --

01:10:35 **8** **A Pay the County a hefty administration fee.**

01:10:39 **9** **Q** Ah, okay. A second option would be a clawback

01:10:44 **10** provision. So to the extent the short-tail

01:10:47 **11** policyholders received something more than at the end

01:10:51 **12** of the day we think they should have, there would be

01:10:53 **13** some provision to claw back those monies and give them

01:10:55 **14** to long-tail policyholders to make sure there was

01:10:59 **15** parity. That's something that conceptually could

01:11:02 **16** happen?

01:11:02 **17** **A Conceptually. Practically, we believed that that was**

01:11:05 **18** **-- would be quite difficult to do.**

01:11:07 **19** **Q** There are some logistical difficulties in clawing back

01:11:12 **20** a payment that was made 40 years earlier, for example;

01:11:15 **21** right?

01:11:16 **22** **A Yeah. I think that's fair to say there would be some**

01:11:19 **23** **difficulties in doing that.**

01:11:22 **24** **Q** So let's turn to a third option. And it's the one

01:11:27 **25** that my client Wells Fargo as Trustee for the LVM

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01:11:32 **1** Bondholders has proposed as a way to ensure equal and

01:11:36 **2** fair payments to long- and short-tail policyholders

01:11:38 **3** alike. And this one has to do with a reserve.

01:11:41 **4** When you were testifying on direct, Mr. Van

01:11:48 **5** Sicklen was asking you questions about the reserve,

01:11:51 **6** and you provided him with an answer to the effect of

01:11:55 **7** that you didn't think a reserve was necessary because

01:12:01 **8** it would be somewhat duplicative of the conservative

01:12:05 **9** analysis that OCI has already done. Is that fair

01:12:09 **10** generally?

01:12:09 **11** **A That's fair with my testimony, yes.**

01:12:11 **12** **Q** I'm going to ask you from a different perspective,

01:12:22 **13** what would be the downside to setting up a reserve?

01:12:28 **14** Just put to the side the question of whether you think

01:12:31 **15** it's something necessary. I'm asking you just a very

01:12:35 **16** different question, which is what would be the

01:12:37 **17** difficulty or the downside to actually effecting a

01:12:45 **18** process by which payments are reserved for future

01:12:48 **19** long-tail claimants?

01:12:52 **20** MR. VAN SICKLEN: I guess I object to the

01:12:54 **21** question being vague. I'm not sure what counsel means

01:12:57 **22** by "the reserve." Maybe he could describe what

01:13:01 **23** amount's being reserved and how that's happening so

01:13:03 **24** the witness can give an intelligent answer.

01:13:06 **25** THE COURT: Mr. Whitmer?

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01:13:08 **1** MR. WHITMER: Well, I'm basically following up

01:13:09 **2** with the testimony Mr. Peterson provided. He was

01:13:11 **3** asked questions on direct of whether it would be --

01:13:15 **4** whether they have incorporated a reserve or not.

01:13:19 **5** **Q** Mr. Peterson, when those questions were asked to you

01:13:21 **6** on direct, you had no question as to what Mr. Van

01:13:23 **7** Sicklen was referring to as the concept of what about

01:13:26 **8** setting up reserves for specific policyholders. You

01:13:29 **9** understood that; right?

01:13:31 **10** **A Yes. But as you try to drill down and be more**

01:13:35 **11** **specific as to what the negative consequences might be**

01:13:42 **12** **with reasons not to pursue it, it brings into question**

01:13:46 **13** **or it is necessary to better understand the detail of**

01:13:51 **14** **what you mean by "reserve," how you might calculate**

01:13:54 **15** **it, how it might be presented and so forth.**

01:13:56 **16** **Q** Right. And as you were explaining with the clawback

01:13:58 **17** provision, you just viscerally told me that's

01:14:01 **18** something that's difficult, it's impractical, it's

01:14:04 **19** problematic. But when we came to reserve, it's laid

01:14:09 **20** out there, it's been presented for quite -- several

01:14:12 **21** weeks now, um, by the LVM Bondholders and Wells Fargo

01:14:18 **22** and proposed, Hey, this is a good way to ensure that

01:14:21 **23** at the end of the day, our clients are being treated

01:14:23 **24** equally with all the short-tail policyholders.

01:14:25 **25** So my question to you is what level of effort has

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01:14:28 **1** there been made by OCI to investigate that as a
01:14:32 **2** potential opportunity here?
01:14:34 **3 A** **Again, it wasn't seen as a -- as any particular**
01:14:45 **4** **advantage of pursuing that reserving scenario. So it**
01:14:53 **5** **wasn't given a lot of consideration. It wasn't deemed**
01:14:55 **6** **as creating an advantage to the Rehabilitator in terms**
01:15:01 **7** **of its understanding.**
01:15:02 **8** **We have estimates of future expected loss that**
01:15:09 **9** **we've -- that we continue to do on a regular basis.**
01:15:16 **10** **We're enhancing our understanding of potential loss**
01:15:19 **11** **because of real development in the world and, you**
01:15:23 **12** **know, continued work on it all the time. To try to**
01:15:28 **13** **also keep an additional reserve is, like I testified**
01:15:33 **14** **to previously, I believe that's simply duplicative of**
01:15:37 **15** **the processes that we're engaged in already.**
01:15:40 **16 Q** You explained you didn't believe it was advantageous
01:15:42 **17** to the Rehabilitator. You would agree that a reserve
01:15:45 **18** would be advantageous to the long-tail policyholders
01:15:49 **19** as a safety net to ensure equal payment?
01:15:51 **20 A** **No, I wouldn't. I believe the Rehabilitator is**
01:15:54 **21** **providing that safety net in our analysis currently.**
01:15:59 **22 Q** I've got two more questions for you.
01:16:01 **23** I'm going to first come back to your testimony
01:16:05 **24** that under the Plan, OCI made efforts to treat
01:16:09 **25** policyholders as fair as possible, given the

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01:16:13 **1** circumstances. That's your position; correct?
01:16:18 **2 A** **Yes.**
01:16:18 **3 Q** Isn't it certainly possible to set up a reserve to
01:16:27 **4** ensure that long-tail claimants receive equal payments
01:16:28 **5** at the end of the day?
01:16:29 **6 A** **That presumes that every dollar in excess of that**
01:16:34 **7** **reserve is available to make payments on the surplus**
01:16:38 **8** **notes. That has not been the Rehabilitator's plan.**
01:16:42 **9** **It's not going to be the Rehabilitator's plan.**
01:16:45 **10** **The Rehabilitator intends to maintain conservatism**
01:16:51 **11** **as to the payment -- making any payment to be made on**
01:16:56 **12** **the surplus notes, and in that case, that reserve that**
01:17:00 **13** **you're talking about is duplicative because there's no**
01:17:06 **14** **intent to pay every dollar available beyond the**
01:17:12 **15** **current surplus amount or the current surplus amount**
01:17:16 **16** **reduced by a particular reserve.**
01:17:19 **17** MR. WHITMER: Mr. Peterson, thank you for your
01:17:21 **18** time. I have no more questions.
01:17:22 **19** MR. PETERSON: Thank you.
01:17:23 **20** THE COURT: All right. Next up?
01:17:37 **21** Maybe this would be an appropriate time, since
01:17:39 **22** we're going to be shifting in a few minutes into the
01:17:42 **23** recess, to take the morning recess. And then we can
01:17:45 **24** start with the next questioner at that time. So let's
01:17:51 **25** take about a 15-minute morning recess.

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01:17:53 **1** MR. PETERSON: Thank you, your Honor.
01:34:20 **2** (Recess taken at 10:15 a.m.)
01:34:20 **3** (Proceedings continuing at 10:30 a.m.)
01:34:31 **4** THE COURT: All right. Be seated.
01:34:32 **5** All right. The Court will be in session again
01:34:52 **6** In the Matter of the Rehabilitation of the Segregated
01:34:59 **7** Account of Ambac Assurance Corporation. Mr. Peterson
01:35:05 **8** is on the stand. And state your name, counsel.
01:35:08 **9** MR. DEVORE: Andrew Devore for One State Street,
01:35:10 **10** LLC.
01:35:11 **11** THE COURT: All right. You may proceed.
01:35:11 **12** **CROSS EXAMINATION**
01:35:13 **13** **BY MR. DEVORE:**
01:35:13 **14 Q** Good morning, Mr. Peterson.
01:35:15 **15 A** **Good morning.**
01:35:16 **16 Q** You testified at length previously that you spent a
01:35:18 **17** significant amount of time in New York at Ambac's
01:35:23 **18** offices; is that right?
01:35:24 **19 A** **That's correct.**
01:35:24 **20 Q** And where are those offices located?
01:35:27 **21 A** **One State Street Plaza.**
01:35:30 **22 Q** And those would be the offices that are leased by my
01:35:33 **23** client, One State Street, to Ambac?
01:35:37 **24 A** **That's correct.**
01:35:37 **25 Q** Now, the operations of Ambac Assurance Corporation

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01:35:46 **1** continue to be based out of the One State Street
01:35:48 **2** building?
01:35:48 **3 A** **They are currently, yes.**
01:35:50 **4 Q** And AAC employees remain in that space?
01:35:54 **5 A** **They do.**
01:35:54 **6 Q** Are there any employees of the Segregated Account in
01:35:57 **7** that space?
01:35:57 **8 A** **The Segregated Account doesn't have employees**
01:36:01 **9** **directly.**
01:36:01 **10 Q** That's what I thought. Thank you.
01:36:03 **11** Now, with respect to the One State Street
01:36:08 **12** liability, are you familiar with its allocation to the
01:36:11 **13** Segregated Account?
01:36:12 **14 A** **The contingent claim from One State Street has been**
01:36:18 **15** **allocated to the Segregated Account, that's correct.**
01:36:21 **16 Q** And could you explain by what you mean as contingent?
01:36:24 **17 A** **Well, the -- it's the Rehabilitator's position that**
01:36:30 **18** **the lease as it exists is an obligation of the holding**
01:36:34 **19** **company. If it were to be found otherwise, the**
01:36:40 **20** **contingent -- that liability would be contained within**
01:36:45 **21** **the Segregated Account.**
01:36:46 **22 Q** So the concept you're saying is if AAC is found to be
01:36:53 **23** liable under the lease, that liability has been
01:36:56 **24** allocated to the Segregated Account?
01:36:59 **25 A** **That's generally true, yes.**

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01:37:00 **1 Q** Okay. Just want to make sure I'm on the same page.

01:37:02 **2 A** **Again, I'm not an attorney, but --**

01:37:05 **3 Q** Yeah.

01:37:06 **4** Do you know why the lease was allocated, this

01:37:10 **5** contingent liability was allocated to the Segregated

01:37:15 **6** Account?

01:37:15 **7 A** **In the contingency developed, at kind of its**

01:37:22 **8** **worst-case scenario, it may have been a material --**

01:37:26 **9** **had a material impact on our potential Rehabilitation.**

01:37:31 **10 Q** Would it have had a material impact on the entire

01:37:36 **11** Rehabilitation? I'm sorry. Strike that.

01:37:37 **12** When you say "rehabilitation," what are you

01:37:39 **13** referring to?

01:37:40 **14 A** **Well, the overall Plan, the Rehabilitation Plan.**

01:37:47 **15 Q** And does that include the prospect of the General

01:37:51 **16** Account going forward?

01:37:53 **17 A** **It does.**

01:37:54 **18 Q** Okay. The majority of Ambac Assurance Corporation is

01:38:06 **19** not in these Rehabilitation proceedings. Would you

01:38:09 **20** agree with that?

01:38:10 **21** MR. VAN SICKLEN: I guess I object on what

01:38:12 **22** counsel means by "majority." If he could define that.

01:38:16 **23 Q** How many policies remain in the General Account?

01:38:19 **24 A** **Ah, 13,000 to 14,000.**

01:38:23 **25 Q** And those policies are not part of this proceeding?

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01:38:26 **1 A** **That's correct.**

01:38:27 **2 Q** And how many policies are in the Segregated Account?

01:38:31 **3 A** **The current count is in the 700 to 800 range.**

01:38:37 **4 Q** So would you agree that the majority of policies are

01:38:40 **5** not before this Court?

01:38:41 **6 A** **That's correct.**

01:38:41 **7 Q** Would you agree that if Ambac Assurance Corporation

01:38:59 **8** leases office space to run its business, they will

01:39:01 **9** have to sign a lease and pay rent?

01:39:06 **10 A** **Typically, that's the case. Yes, you need to sign a**

01:39:10 **11** **lease and pay rent.**

01:39:11 **12 Q** Have there been any other non-policy liabilities

01:39:20 **13** allocated to the Segregated Account?

01:39:23 **14 A** **Ah, there are reinsurance liabilities allocated to the**

01:39:32 **15** **Segregated Account. And I'm having a difficult time**

01:39:40 **16** **recalling, but I believe there's another subclass of**

01:39:44 **17** **liabilities.**

01:39:45 **18 Q** Would you be referring to the tax liability?

01:39:48 **19 A** **Well, yes. Certainly that's recently, the tax**

01:39:52 **20** **liability, potential lawsuits from the FG Bondholders,**

01:40:01 **21** **so forth.**

01:40:02 **22 Q** Are you aware of any other non-policy liabilities

01:40:07 **23** allocated to the Segregated Account?

01:40:09 **24 A** **I recall something with regard to a CAPCO liability,**

01:40:17 **25** **perhaps.**

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01:40:18 **1 Q** But, for example, equipment leases?

01:40:26 **2 A** **No.**

01:40:26 **3 Q** Those have not been allocated?

01:40:26 **4 A** **No. Equipment leases have not been allocated.**

01:40:30 **5 Q** And is it correct to state that the reason that

01:40:33 **6** equipment lease is not allocated was because of the

01:40:35 **7** scope of the potential liability?

01:40:36 **8 A** **I think that is fair to say, yes.**

01:40:38 **9 Q** Now, you testified Tuesday that the determination of

01:40:52 **10** adequate capital that OCI made when the Segregated

01:40:55 **11** Account was created was based on the cash flow needs

01:41:00 **12** of the Plan; is that correct?

01:41:02 **13 A** **That and the fact that substantially all the resources**

01:41:09 **14** **of the General Account have been made available to the**

01:41:13 **15** **Segregated Account through the note and the Excess of**

01:41:17 **16** **Loss Reinsurance Agreement.**

01:41:18 **17 Q** So the -- just so I understand, the adequate

01:41:25 **18** capitalization determination was made because OCI

01:41:30 **19** determined that the cash flow needs of the Segregated

01:41:34 **20** Account would be met under the Secured Note and

01:41:37 **21** Reinsurance Agreement; is that right? Is that

01:41:40 **22** accurate?

01:41:40 **23 A** **And as I just testified, and the fact that**

01:41:44 **24** **substantially all the assets of the General Account**

01:41:49 **25** **would be made available through those agreements.**

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01:41:51 **1 Q** So through those agreements. Okay.

01:41:53 **2** Now, in determining that there was adequate

01:41:57 **3** capital in surplus, did OCI conclude that the Secured

01:42:02 **4** Note and Reinsurance Agreement would provide

01:42:05 **5** sufficient resources to pay any liabilities under the

01:42:08 **6** One State Street lease?

01:42:09 **7 A** **Ah, the scenarios that we presented in the Disclosure**

01:42:21 **8** **Statement illustrate possible outcomes and the --**

01:42:28 **9** **under what conditions funds may be available to make**

01:42:34 **10** **payment on a surplus note or a junior surplus note**

01:42:38 **11** **issued to One State Street if that contingency**

01:42:42 **12** **develops.**

01:42:42 **13 Q** I'll get to the scenarios in a few minutes. But I

01:42:45 **14** want to turn back to the time that the Segregated

01:42:48 **15** Account was created.

01:42:49 **16** Was the One State Street liability even considered

01:42:51 **17** in determining adequate capitalization?

01:42:54 **18 A** **It's -- the law creates a junior status for general**

01:43:05 **19** **creditors.**

01:43:07 **20 Q** But that's in the Rehabilitation, arguably, and

01:43:12 **21** certainly in a liquidation; is that right?

01:43:14 **22** MR. VAN SICKLEN: Objection. I think that

01:43:16 **23** mischaracterizes the law.

01:43:19 **24** MR. DEVORE: He can correct me if I'm wrong.

01:43:21 **25** THE COURT: Well, maybe he can. He's said

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01:43:23 **1** several times he's not an attorney. Sustain the
01:43:25 **2** objection.
01:43:27 **3** BY MR. DEVORE:
01:43:27 **4** **Q** Do you recall any conversations at the time the
01:43:39 **5** Segregated Account was created whether there was
01:43:43 **6** sufficient capital in the surplus to pay the One State
01:43:47 **7** Street liability?
01:43:48 **8** **A** **Not specifically, no.**
01:43:59 **9** MR. VAN SICKLEN: Mr. Devore, just so I don't
01:44:01 **10** have to interrupt your flow and object every time, can
01:44:03 **11** we just agree that when you say -- ask questions about
01:44:06 **12** a liability, we're on the same page, that it's a
01:44:09 **13** disputed contingent liability?
01:44:12 **14** MR. DEVORE: Correct.
01:44:13 **15** MR. VAN SICKLEN: Okay.
01:44:14 **16** MR. DEVORE: As defined in the Plan, just to
01:44:18 **17** make the record clear.
01:44:19 **18** **Q** So I take it that the lease was not discounted to
01:44:26 **19** present value at the time the Segregated Account was
01:44:28 **20** created to determine adequate capitalization?
01:44:33 **21** MR. VAN SICKLEN: The form of the question I
01:44:34 **22** object to. The lease or the contingent disputed
01:44:37 **23** liability?
01:44:38 **24** MR. DEVORE: The liability.
01:44:39 **25** THE COURT: Or he understands, which was the

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01:44:42 **1** preface, making it compound. Sustain the objection.
01:44:47 **2** BY MR. DEVORE:
01:44:47 **3** **Q** Do you know if the contingent liability of the One
01:44:53 **4** State Street lease was discounted to present value in
01:44:56 **5** determining adequate capitalization?
01:44:59 **6** **A** **I don't know that it was. But if I recall terms of**
01:45:08 **7** **the lease correctly, there are provisions that it**
01:45:13 **8** **could accelerate the amount due under the lease so**
01:45:19 **9** **that a present value of that -- of those payments may**
01:45:24 **10** **not have been appropriate.**
01:45:25 **11** **Q** So what you're saying if I'm understanding you
01:45:29 **12** correctly is that in acceleration, a hundred percent
01:45:34 **13** of the contingent liability, if it exists, would be
01:45:37 **14** accrued?
01:45:40 **15** **A** **That involves certain contract rights. Whether they**
01:45:46 **16** **could be enforced against the Segregated Account or**
01:45:51 **17** **not involves legal questions that I am not in a**
01:45:59 **18** **position to respond to.**
01:46:00 **19** **Q** Fair enough. I'll move on.
01:46:02 **20** Now, I'd like to turn to the recovery scenarios
01:46:08 **21** that were presented to this Court. And as a Class 5
01:46:12 **22** claimant, I come at this from a different perspective
01:46:15 **23** than the policyholders, so I apologize if it seems
01:46:18 **24** that we're re-plowing any old ground. But we have a
01:46:21 **25** different perspective.

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01:46:21 **1** With respect to Class 5 claimants, would you agree
01:46:28 **2** that the most likely outcome of future events is
01:46:31 **3** within the scenarios that are presented, you know, 1
01:46:35 **4** being the most positive and 4 being the most
01:46:39 **5** unfavorable?
01:46:40 **6** **A** **It's reasonable, I think, to say that the central**
01:46:44 **7** **probability is within the range between Scenario 1 and**
01:46:49 **8** **Scenario 4.**
01:46:51 **9** MR. DEVORE: Can we get Exhibit 31 in front of
01:46:54 **10** the witness, please.
01:47:19 **11** **Q** And are these the four scenarios that were presented
01:47:23 **12** to the Court?
01:47:27 **13** MR. VAN SICKLEN: I'm confused. I don't think
01:47:28 **14** Exhibit 31 has the four scenarios. I think you're
01:47:34 **15** talking about the Disclosure Statement, which would be
01:47:35 **16** Exhibit 27.
01:47:37 **17** MR. DEVORE: Yes. And I believe there was an
01:47:38 **18** amendment.
01:47:38 **19** MR. PETERSON: It's actually in this Exhibit 31
01:47:41 **20** for some reason too.
01:47:42 **21** THE COURT: Wait a minute. One at a time.
01:47:44 **22** MR. VAN SICKLEN: Go ahead.
01:47:45 **23** BY MR. DEVORE:
01:47:45 **24** **Q** Just for the record, to be clear, there was an
01:47:50 **25** amendment that OCI submitted to clarify I believe it

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01:47:51 **1** was some heading irregularity in the original version
01:47:56 **2** of the scenario, so that's why I have Exhibit 31.
01:47:59 **3** It's the most recent version?
01:48:01 **4** **A** **That appears to be correct, yes.**
01:48:02 **5** **Q** Now, if you look at page 14 of Scenario 1, the
01:48:09 **6** scenario provides a beginning balance of junior
01:48:12 **7** surplus notes in the year 2021?
01:48:15 **8** **A** **Just a moment.**
01:48:15 **9** **Q** Oh, I'm sorry.
01:48:20 **10** **A** **Wow. The printing is rather small, but yes, I have**
01:48:34 **11** **page 14 in front of me.**
01:48:36 **12** **Q** Now, is that -- I believe if I'm reading this
01:48:38 **13** correctly, there is a \$69 million beginning balance of
01:48:41 **14** junior surplus notes in the year 2021. Is that right?
01:48:48 **15** **A** **Yes. That appears to be the case. It's -- the**
01:48:54 **16** **printing is a little bit blurred, but in 2022 it**
01:48:58 **17** **appears to go to \$70 million.**
01:49:00 **18** **Q** And if we turn to Scenario 2, same page 14, that also
01:49:04 **19** lists -- I'll wait for you to get there.
01:49:16 **20** **A** **Yes. \$69 and \$70 million in years 2021 and 2022.**
01:49:23 **21** **Q** But then if we turn to Scenarios 3 and 4, I have a
01:49:28 **22** question. We can turn to those scenarios. The number
01:49:31 **23** is different.
01:49:45 **24** (Pause)
01:49:52 **25** **Q** And do you see what the beginning balance of junior

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01:49:56 **1** surplus notes in 2021 is under Scenarios 3 and 4?

01:50:00 **2 A** **I'm looking at Scenario 4. And I actually haven't**

01:50:09 **3 found page 14 yet.**

01:50:10 **4 Q** I'm sorry. It's actually on page 15 of Scenario 4.

01:50:13 **5 A** **Ah. That avoids a little bit of my confusion.**

01:50:34 **6 Junior surplus notes, it appears to be \$137**

01:50:45 **7 million in 2021 and \$140 million in 2022. Is that**

01:50:53 **8 correct?**

01:50:53 **9 Q** Do you know the reason for the difference between the

01:50:56 **10** beginning balance under Scenarios 1 and 2 and the

01:51:01 **11** beginning balance under Scenarios 3 and 4?

01:51:03 **12 A** **No, I don't recall.**

01:51:12 **13 Q** Do you know if those numbers include only reinsurance

01:51:15 **14** claims?

01:51:17 **15 A** **No, I don't know specifically. I think that would be**

01:51:26 **16 a reasonable presumption that the additional amounts**

01:51:29 **17 have to do with reinsurance claims, but I -- I can't**

01:51:34 **18 say that with certainty.**

01:51:36 **19 Q** Okay. Now, are you aware that OCI's counsel

01:51:40 **20** previously estimated the One State Street liability to

01:51:43 **21** be as much as \$94 million?

01:51:49 **22 A** **I don't remember that specifically. It may be**

01:51:50 **23 correct.**

01:51:51 **24 Q** So if we're going forward, let's assume that it's a

01:51:55 **25** \$94 million liability. And we understand that that

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01:51:58 **1** can be contested. But just going forward so we are

01:52:01 **2** working on the same page, can we assume that it's a

01:52:04 **3** \$94 million liability?

01:52:06 **4 A** **We could make that assumption, sure.**

01:52:07 **5 Q** Now, Scenario 1 projects Class 5 claimants to receive

01:52:15 **6** a recovery; is that correct?

01:52:17 **7 A** **It does, yes.**

01:52:18 **8 Q** And that's a 100-cent recovery?

01:52:24 **9 A** **It does, yes.**

01:52:25 **10 Q** And Scenario 2, by contrast, provides no expectation

01:52:30 **11** of recovery to Class 5 claimants?

01:52:33 **12 A** **That's correct as well.**

01:52:34 **13 Q** Okay. Now, the only difference between Scenario 1 and

01:52:40 **14** Scenario 2 are the R and W remediation recoveries; is

01:52:44 **15** that correct?

01:52:44 **16 A** **That's correct as well.**

01:52:45 **17 Q** And Scenario 1 assumes a \$2 billion remediation

01:52:49 **18** recovery in the very near term, I believe.

01:52:55 **19 A** **In the next two to three years I believe is the time**

01:52:58 **20 frame.**

01:52:58 **21 Q** But it's a \$2 billion estimate that's baked into

01:53:04 **22** Scenario 1?

01:53:04 **23 A** **Approximately \$2 billion, yes.**

01:53:06 **24 Q** You were present in court, I believe it was Tuesday,

01:53:12 **25** when Commissioner Dilweg testified that OCI had always

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01:53:17 **1** had a difference of opinion with AAC as to the R and W

01:53:20 **2** recoveries. Do you recall that testimony?

01:53:23 **3 A** **In general I do, yes.**

01:53:26 **4 Q** And yesterday you testified that OCI's view of R and W

01:53:30 **5** remediation was confidential. Do you recall that?

01:53:34 **6 A** **Yes.**

01:53:35 **7 Q** And can you explain how it is confidential? Is there

01:53:39 **8** an agreement with a party? Or what is the basis for

01:53:41 **9** the confidentiality?

01:53:43 **10 A** **No. Our ongoing examination of the company gives --**

01:53:54 **11 provides confidentiality under Wisconsin Statutes, I**

01:54:02 **12 believe.**

01:54:02 **13 Q** Is there a confidentiality agreement with any party

01:54:08 **14** that would preclude testimony regarding R and W

01:54:11 **15** remediation? Or is it simply under your claim of

01:54:15 **16** under the statute?

01:54:17 **17 A** **I'm not aware of any confidentiality agreement with a**

01:54:24 **18 party as to that number.**

01:54:28 **19** MR. DEVORE: Your Honor, if I could ask for a

01:54:30 **20** ruling on this.

01:54:30 **21** Commissioner Dilweg testified, and I would argue

01:54:36 **22** that he waived the privilege generally, and further by

01:54:39 **23** submitting the Disclosure Statement and putting the R

01:54:42 **24** and W remediations at issue, I believe that it's a

01:54:46 **25** proper scope of examination to inquire into what OCI's

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01:54:50 **1** actual view of R and W remediations are. Remediation

01:54:57 **2** recoveries, as we've established, are fundamental to

01:55:00 **3** my client's prospective recoveries in this case.

01:55:14 **4** MR. VAN SICKLEN: Just one second, your Honor.

01:55:15 **5** I was just looking for the copy of the statute.

01:55:30 **6** (Pause)

01:55:30 **7** MR. VAN SICKLEN: Two positions, your Honor.

01:55:32 **8** One is the Wisconsin statute regarding confidentiality

01:55:35 **9** of OCI's analysis of regulated insurers makes clear

01:55:41 **10** that there can be no waiver unless it's expressly set

01:55:44 **11** forth in writing signed by a representative of OCI, I

01:55:49 **12** believe in 601.465. And perhaps if the witness even

01:55:53 **13** remembers it, I think it's a statute that's near and

01:55:55 **14** dear to him.

01:55:56 **15** And then secondly, I would indicate that the R

01:56:01 **16** and Ws are basically an assessment of litigation which

01:56:05 **17** any kind of analysis or knowledge that OCI or

01:56:08 **18** Mr. Peterson has is based on privileged communications

01:56:11 **19** with counsel. And so it's a two-fold problem.

01:56:15 **20** MR. DEVORE: May I respond to the

01:56:16 **21** attorney/client issue?

01:56:19 **22** THE COURT: Yes.

01:56:20 **23** MR. DEVORE: I'm not asking him for what the

01:56:21 **24** communications are. I'm asking him for the basis or

01:56:25 **25** what OCI 's actual expectations are.

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01:56:37 **1** THE COURT: All right. The ruling is under
01:56:38 **2** 601.465, that would not be available. It is not -- it
01:56:46 **3** is subject to the nondisclosure.
01:56:48 **4** MR. DEVORE: Thank you for the ruling.
01:57:05 **5 Q** Mr. Peterson, the R and W remediation recoveries are
01:57:09 **6** based on lawsuits against mortgage originators. Is
01:57:14 **7** that a fair assessment of the --
01:57:17 **8 A** **It's a reasonable general description, yes.**
01:57:19 **9 Q** Are you aware if any of these -- strike that.
01:57:22 **10** Are you aware of whether or not AAC's projected
01:57:27 **11** recoveries are based -- I'm sorry. Strike that.
01:57:30 **12** Are you aware of whether or not AAC's \$2 billion
01:57:37 **13** projection is based on a 100 percent recovery in those
01:57:40 **14** lawsuits?
01:57:41 **15 A** **Ah, a number of factors are incorporated in their**
01:57:51 **16** **estimate.**
01:57:52 **17** MR. VAN SICKLEN: And just -- your Honor, just
01:57:53 **18** so we're not getting into a waiver argument if the
01:57:57 **19** witness answers this, I'm prepared to let him answer
01:57:59 **20** it if counsel is not gonna immediately turn around and
01:58:02 **21** argue waiver. If he is, then I would instruct the
01:58:04 **22** witness to not answer.
01:58:06 **23** MR. DEVORE: I'm asking what his understanding
01:58:08 **24** of AAC's position is.
01:58:10 **25** MR. VAN SICKLEN: His understanding is based

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01:58:13 **1** upon the sheltered communications that the witness
01:58:15 **2** just outlined and are set forth in the statute.
01:58:18 **3** MR. DEVORE: I believe your Honor has already
01:58:20 **4** ruled that there can be no waiver, so I won't be
01:58:23 **5** arguing that point.
01:58:24 **6** THE COURT: Sustain the objection.
01:58:32 **7** BY MR. DEVORE:
01:58:32 **8 Q** Do you know if in the past that there have been any R
01:58:35 **9** and W remediation suits brought against other mortgage
01:58:39 **10** originators?
01:58:40 **11** MR. VAN SICKLEN: Other than which?
01:58:45 **12 Q** The current -- other than the current -- the currently
01:58:47 **13** pending suits, are you aware of any other R and W
01:58:51 **14** remediation suits?
01:58:53 **15** MR. VAN SICKLEN: By parties other than Ambac?
01:58:57 **16** I'm confused.
01:58:59 **17** MR. DEVORE: I think it's fairly clear.
01:59:04 **18 Q** Other than these lawsuits that are currently pending
01:59:07 **19** that form the basis for the \$2 billion estimate, are
01:59:09 **20** you aware of any other lawsuits brought by Ambac to
01:59:14 **21** recover on remediation claims?
01:59:18 **22 A** **No, no.**
01:59:29 **23** MR. VAN SICKLEN: Just so I'm clear on the
01:59:30 **24** question, counsel, do you mean suits that were brought
01:59:32 **25** and went to conclusion and are over?

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01:59:35 **1** MR. DEVORE: I think the witness answered the
01:59:37 **2** question. He understood the question.
01:59:38 **3** MR. VAN SICKLEN: I would move to strike in the
01:59:41 **4** sense that it's incomprehensible, the question. Other
01:59:44 **5** than the cases that exist, does he know of others?
01:59:48 **6** MR. DEVORE: That Ambac brought on remediation
01:59:53 **7** claims.
01:59:53 **8** THE COURT: Is that your question?
01:59:54 **9** MR. DEVORE: Could the court reporter read the
01:59:54 **10** question back?
02:00:10 **11** (Question read back.)
02:00:10 **12** THE COURT: The answer is no. Let's proceed.
02:00:17 **13** BY MR. DEVORE:
02:00:17 **14 Q** I'd like to turn your attention to the \$700 million
02:00:21 **15** tax liability.
02:00:22 **16** When did OCI first become aware of the \$700
02:00:27 **17** million potential liability?
02:00:29 **18 A** **Um, which party are you referring to?**
02:00:35 **19 Q** Let's take them in turn. An IRS enforcement action?
02:00:41 **20** MR. VAN SICKLEN: Wait, wait. Objection. It
02:00:42 **21** mischaracterizes the IRS action.
02:00:49 **22** MR. DEVORE: I don't believe it does. I think
02:00:51 **23** the witness understands exactly what I'm asking.
02:00:53 **24** MR. VAN SICKLEN: There isn't a pending
02:00:54 **25** enforcement action.

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02:00:56 **1** MR. DEVORE: A potential enforcement action.
02:00:59 **2** THE COURT: Now, is your question about a
02:01:00 **3** potential enforcement action?
02:01:03 **4** MR. DEVORE: Yes. When did OCI first become
02:01:06 **5** aware of a potential tax enforcement action for \$700
02:01:10 **6** million?
02:01:10 **7** THE COURT: Where? How? Against whom?
02:01:12 **8** MR. DEVORE: The question is when.
02:01:14 **9** THE COURT: The question is against whom?
02:01:17 **10** MR. DEVORE: Against --
02:01:17 **11** THE COURT: That's a very vague question. Is it
02:01:20 **12** -- are you asking \$700 million enforcement action
02:01:26 **13** against --
02:01:26 **14** UNIDENTIFIED ATTORNEY: Ambac.
02:01:30 **15** THE COURT: Ambac.
02:01:30 **16 A** **Somewhere within a few days of November 1st of this**
02:01:38 **17** **year.**
02:01:38 **18 Q** So is it fair to say that that potential liability,
02:01:46 **19** that \$700 million potential tax liability, was not
02:01:50 **20** factored into adequate capital, the adequate capital
02:01:53 **21** determination?
02:01:56 **22 A** **Not directly, no.**
02:01:58 **23 Q** Now, before several days, before when -- strike that.
02:02:03 **24** Now, AAC and its advisors have assured the OCI
02:02:10 **25** that the tax refunds were proper; is that correct?

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02:02:15 **1 A** **There is a statement -- I don't recall the proper name**
02:02:23 **2 of it, but the auditors of Ambac Financial Group and**
02:02:31 **3 Ambac Assurance have issued an opinion that in some**
02:02:38 **4 form that the tax treatment was reasonable.**
02:02:43 **5 Q** To clarify your -- are the auditors the same for AFG
02:02:50 **6 as for AAC?**
02:02:52 **7 A** **I believe they are.**
02:02:53 **8 Q** Is OCI concerned about any potential conflict there?
02:02:57 **9 A** **Between the auditor -- between the audited finances of**
02:03:05 **10 AFG versus AAC?**
02:03:07 **11 Q** Is OCI concerned about any potential conflicts of
02:03:12 **12 having the same auditors at the AFG level as at the**
02:03:16 **13 AAC level?**
02:03:17 **14 A** **We haven't had a concern about that, no.**
02:03:21 **15 Q** Had OCI looked at any tax liability issues before this
02:03:30 **16 \$700 million potential liability arose?**
02:03:36 **17 A** **Well, that seems to be a broad question. Yes, we've**
02:03:41 **18 -- potential tax liabilities have been considered as**
02:03:45 **19 to the possibility that the IRS might seek this -- may**
02:03:54 **20 potentially take action on these refunds. That's a**
02:03:59 **21 separate question.**
02:04:00 **22 Q** Could you answer that question?
02:04:06 **23 A** **We didn't specifically identify that potential. We**
02:04:13 **24 relied on the tax treatment as being appropriate and**
02:04:20 **25 the representations of auditors that that treatment**

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02:04:25 **1 was appropriate. As refunds were pursued, ah, related**
02:04:33 **2 to the government -- government as part of TARP**
02:04:42 **3 provided I believe \$5 billion of additional**
02:04:49 **4 availability for loss carry-backs under the code, and**
02:04:58 **5 Ambac filed and received a refund for \$440-some**
02:05:03 **6 million on that basis, and we -- our tax advisors were**
02:05:10 **7 involved in the -- in looking at that filing.**
02:05:17 **8 So, you know, there was involvement through**
02:05:25 **9 counsel's tax advisors to review certain of the tax**
02:05:31 **10 filings as to their reasonableness.**
02:05:34 **11 Q** Now, would this \$700 million potential tax liability
02:05:41 **12 be paid ahead of One State Street under Scenario 1?**
02:05:47 **13 A** **I -- I believe they're in the same class. As to how**
02:05:52 **14 that may be determined is a legal issue I'm not**
02:06:00 **15 prepared to answer.**
02:06:00 **16 Q** But it's generally OCI's position that the tax
02:06:03 **17 liability would be a Class 5 claim?**
02:06:05 **18** MR. VAN SICKLEN: Objection; foundation.
02:06:07 **19** MR. DEVORE: I'm just clarifying his answer.
02:06:10 **20** THE COURT: Sustain the objection.
02:06:14 **21 Q** Does OCI have a view of what priority tax liabilities
02:06:20 **22 would have?**
02:06:23 **23** MR. VAN SICKLEN: Same question -- objection.
02:06:26 **24** MR. DEVORE: I'm laying the foundation asking if
02:06:27 **25 they have a view.**

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02:06:28 **1** THE COURT: Sustain the objection.
02:06:32 **2 Q** If it were determined that the \$700 million potential
02:06:43 **3 tax liability could not be allocated to the Segregated**
02:06:48 **4 Account and was instead a liability of the General**
02:06:53 **5 Account, what would that -- what effect would that**
02:06:57 **6 have on the Plan?**
02:06:58 **7 A** **It would have some impact on the Plan.**
02:07:03 **8 Q** A material impact?
02:07:04 **9 A** **Material, yes. But I don't -- that's not to say that**
02:07:15 **10 it would necessarily cause the Plan to not be**
02:07:22 **11 sustainable.**
02:07:24 **12 Q** But it would certainly reduce claims-paying resources?
02:07:28 **13 A** **That's correct, yes.**
02:07:29 **14 Q** Now, if we could turn to Scenario 3 -- you don't have
02:07:35 **15 to turn to it. I think you can answer it, unless you**
02:07:38 **16 say otherwise. Scenario 3 contemplates stress-case**
02:07:42 **17 loss estimates and full realization of R and W**
02:07:45 **18 remediation?**
02:07:46 **19 A** **That's correct.**
02:07:46 **20 Q** And then the only difference between Scenario 3 and 4
02:07:50 **21 is that in Scenario 4 there's no remediation**
02:07:54 **22 recoveries?**
02:07:55 **23 A** **That's correct as well, yes.**
02:07:56 **24 Q** And, of course, in Scenarios 3 and 4, Class 5
02:08:00 **25 claimants are projected to receive no recovery?**

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02:08:04 **1 A** **Again, those are correct.**
02:08:06 **2 Q** Okay. You testified earlier in these proceedings that
02:08:16 **3 OCI went through some pains to obtain a No-Action**
02:08:19 **4 Letter for the surplus notes. Do you recall that?**
02:08:21 **5 A** **I don't recall that phrase being associated with the**
02:08:26 **6 No-Action Letter.**
02:08:27 **7 Q** But OCI did take action to obtain -- obtain the
02:08:33 **8 No-Action Letter for the surplus notes?**
02:08:36 **9 A** **Yes. OCI through counsel and advisors took action,**
02:08:42 **10 yes.**
02:08:42 **11 Q** Now, did OCI ever request a No-Action Letter for the
02:08:45 **12 junior surplus notes?**
02:08:49 **13** MR. VAN SICKLEN: Objection as to relevance and
02:08:52 **14 calling for a legal conclusion as to whether one is**
02:08:54 **15 even necessary, but --**
02:08:56 **16** MR. DEVORE: Your Honor, I didn't ask -- I asked
02:08:57 **17 if they asked for one.**
02:08:58 **18** MR. VAN SICKLEN: Well, the question is whether
02:08:59 **19 the existing one covers both. That's the legal issue.**
02:09:02 **20** THE COURT: Sustain the objection.
02:09:04 **21** BY MR. DEVORE:
02:09:04 **22 Q** You testified yesterday that the surplus notes issued
02:09:11 **23 to the banks were trading "cents on the dollar." Do**
02:09:18 **24 you recall that?**
02:09:18 **25 A** **There was some discussion about the trading of those**

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02:09:25 **1** -- of those notes.

02:09:28 **2 Q** Now, the junior notes that my -- that One State Street

02:09:32 **3** would be receiving under this Plan are subordinated to

02:09:35 **4** those surplus notes; is that correct?

02:09:37 **5 A** **That's correct.**

02:09:37 **6 Q** So is it fair to say that the junior surplus notes by

02:09:42 **7** their subordinated nature are worth less than the

02:09:45 **8** surplus notes?

02:09:47 **9 A** **That's reasonable to conclude, yes.**

02:09:49 **10 Q** Is it OCI's position as we sit here today that the

02:10:00 **11** Segregated Account is adequately capitalized as to the

02:10:04 **12** contingent liability of One State Street?

02:10:10 **13 A** **We didn't make a separate determination on that fact.**

02:10:14 **14** **The Segregated Account was determined to be adequately**

02:10:18 **15** **capitalized.**

02:10:19 **16 Q** Looking back, as we sit here today, would you make

02:10:27 **17** that same determination?

02:10:28 **18 A** **We're making that representation to the Court, yes.**

02:10:34 **19 Q** Now, I'd like to turn to the Liquidation Analysis that

02:10:43 **20** was filed with this Court on Friday, this past Friday.

02:10:49 **21** Now, you testified regarding your familiarity with

02:10:51 **22** it already; is that correct?

02:10:53 **23 A** **I'm generally familiar, yes. We had some testimony**

02:10:58 **24** **about it.**

02:10:58 **25 Q** Would you agree that under the scenarios presented,

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02:11:02 **1** there would be no recovery for shareholders in a

02:11:05 **2** liquidation?

02:11:06 **3 A** **Yeah, I believe that's correct. I don't have a**

02:11:11 **4** **document in front of me.**

02:11:13 **5** MR. DEVORE: Could we get the document in front

02:11:15 **6** of him?

02:11:15 **7** Thank you. Could we read back the last

02:11:38 **8** question?

02:11:50 **9** (Question read back.)

02:11:50 **10 A** **I would agree to that, yes.**

02:11:52 **11 Q** Now, I'd like to read you a statement made by OCI's

02:11:55 **12** counsel on September 9th.

02:11:57 **13** "I submit that there would be one and only one

02:12:00 **14** beneficiary had OCI chosen liquidation, the path that

02:12:04 **15** Depfa suggests, Deutsche suggests, and several of

02:12:07 **16** these other parties.

02:12:08 **17** And who would that party be?

02:12:11 **18** It would be the shareholders of Ambac because it

02:12:13 **19** would create a tremendous value for them."

02:12:15 **20** Do you agree with that statement?

02:12:21 **21** THE COURT: Do you understand the context in

02:12:22 **22** which counsel made that statement?

02:12:25 **23 A** **I think I do. That One State Street may also be in**

02:12:32 **24** **the position to benefit from that treatment.**

02:12:36 **25 Q** In a liquidation.

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02:12:38 **1 A** **Um, that may be the case.**

02:12:44 **2 Q** Okay. So now I'd like to ask a specific question

02:12:47 **3** about that statement.

02:12:48 **4** In a liquidation, would shareholders receive a

02:12:52 **5** "tremendous value"?

02:12:54 **6 A** **I don't know at what threshold value becomes**

02:13:01 **7** **tremendous.**

02:13:01 **8 Q** Well, I'll make it simple. One cent. One penny.

02:13:10 **9 A** **Could you repeat your question?**

02:13:12 **10 Q** Yeah. In a liquidation -- would you agree with the

02:13:16 **11** statement that in a liquidation, the shareholders

02:13:20 **12** would receive one penny?

02:13:24 **13 A** **No. Our expectation is that the shareholders won't**

02:13:28 **14** **receive any money.**

02:13:30 **15 Q** Okay. So that statement by your counsel was

02:13:33 **16** inaccurate?

02:13:37 **17 A** **Perhaps it was, yes.**

02:13:43 **18 Q** Did any facts regarding the liquidation scenarios

02:13:48 **19** change between September 9th and this past Friday?

02:13:52 **20 A** **Well, if you're referring to the IRS investigation,**

02:14:01 **21** **yes.**

02:14:01 **22 Q** And that would reduce a liquidation recovery?

02:14:05 **23 A** **As to -- as to shareholders, certainly, yeah.**

02:14:10 **24 Q** Okay. Now, the liquidation scenarios that you have in

02:14:31 **25** front of you that were presented to this Court include

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02:14:34 **1** future non-CDS policy losses as Class 5 claims. Is

02:14:40 **2** that correct?

02:14:40 **3 A** **Yes.**

02:14:50 **4 Q** And those are estimated under these scenarios as of

02:14:56 **5** March 24th; is that correct?

02:14:58 **6 A** **Yes, yes, as of March 24th.**

02:15:00 **7 Q** And as of March 24th, those future non-incurred claims

02:15:06 **8** were forecasted at \$6 billion under the base scenario

02:15:10 **9** and \$9.4 billion under the stress scenario?

02:15:15 **10 A** **Rounded, yes.**

02:15:17 **11 Q** Do you know what the projected non-CDS policy losses

02:15:23 **12** would be as of today?

02:15:26 **13 A** **Well, there's been some commutation of those losses in**

02:15:32 **14** **the interim period, the Weinstein deal. With that**

02:15:41 **15** **modification, there's some additional change. I can't**

02:15:44 **16** **-- I can't quote the exact numbers off the top of my**

02:15:50 **17** **head.**

02:15:50 **18 Q** Would the numbers be higher or lower?

02:15:52 **19 A** **They're very close to that same range now.**

02:15:57 **20 Q** So they're very close to 6 and 9.4?

02:16:01 **21 A** **I believe the stress-case number is actually somewhat**

02:16:06 **22** **lower. The base-case number is near \$6 billion, 5.8,**

02:16:14 **23** **something like that, I believe. I don't recall**

02:16:16 **24** **specifically.**

02:16:20 **25 Q** But they're within a few percentage points. We're not

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02:16:24 **1** talking material differences?

02:16:25 **2 A** **They're not half of what they are presented here.**

02:16:29 **3 Q** Okay. Now, it is OCI's position that future

02:16:36 **4** non-incurred policy claims are not entitled to any

02:16:40 **5** payment in a liquidation scenario; is that correct?

02:16:44 **6 A** **You'll have to repeat the question.**

02:16:49 **7 Q** Could you just read back the question.

02:17:03 **8** (Question read back.)

02:17:03 **9 A** **Well --**

02:17:04 **10** MR. VAN SICKLEN: I object to the form of the

02:17:06 **11** question. Not entitled to it or wouldn't be receiving

02:17:09 **12** one?

02:17:10 **13** MR. DEVORE: Not entitled to.

02:17:15 **14 A** **I think as the claims that would develop after the**

02:17:21 **15** **termination of the policy, a position would be taken**

02:17:26 **16** **that the policies were effectively terminated and so**

02:17:29 **17** **forth. I think as we've discussed, we would expect**

02:17:33 **18** **that that position might be litigated.**

02:17:36 **19 Q** Of course. And I would expect no less.

02:17:38 **20** But the liquidation scenarios that you presented

02:17:45 **21** include that \$6 billion and \$9.4 billion under the

02:17:50 **22** base- and stress-case scenarios respectively; correct?

02:17:54 **23 A** **They do.**

02:17:56 **24 Q** Okay. Now, with the Court's permission, I'd like to

02:18:03 **25** walk you through how the Liquidation Analysis would

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02:18:08 **1** change if those future non-incurred policy losses were

02:18:09 **2** excluded from the analysis.

02:18:11 **3** Now, you have the liquidation scenario in front of

02:18:23 **4** you still?

02:18:23 **5 A** **I do.**

02:18:24 **6 Q** Now. The claims-paying resources as of March 24th

02:18:28 **7** were \$8.2 billion?

02:18:34 **8 A** **Yes.**

02:18:35 **9 Q** And the admin claims were \$250 million?

02:18:43 **10 A** **That is the number used in this case.**

02:18:46 **11 Q** Do you know what the basis is for that number?

02:18:49 **12 A** **I wasn't involved in developing the number**

02:18:54 **13** **specifically, no.**

02:18:56 **14** MR. DEVORE: Your Honor, with your permission, I

02:18:57 **15** would just write these numbers on the easel so it's

02:19:00 **16** easier for everyone to follow, if that's okay.

02:19:02 **17** THE COURT: Well, I don't know if everyone is

02:19:05 **18** having any difficulty since we've gone over this so

02:19:07 **19** much.

02:19:08 **20** Do you want them written down?

02:19:10 **21** MR. DEVORE: I can give you a notepad.

02:19:12 **22** MR. PETERSON: I have them in front of me.

02:19:13 **23** MR. DEVORE: Okay.

02:19:14 **24** MR. PETERSON: Or I could do math in my head

02:19:16 **25** fairly well.

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02:19:17 **1** MR. DEVORE: Good. 'Cause we'll get there.

02:19:20 **2 Q** So then there's loss claims that would be paid as

02:19:23 **3** Class 3 claims; is that right?

02:19:27 **4 A** **Yes, there's loss claims issued there.**

02:19:29 **5 Q** And how much would those be?

02:19:32 **6 A** **Well, under treatment on whether mark-to-market**

02:19:43 **7** **terminations were treated as Class 3 or not, it varies**

02:19:46 **8** **from \$130 million to \$16.4 billion.**

02:19:51 **9 Q** Correct. And for this scenario, which I'm going to

02:19:53 **10** call Liquidation Scenario 3, let's assume that those

02:19:58 **11** \$16.3 billion in mark-to-market damages claims are

02:20:04 **12** Class 5, because I think you'll probably agree that if

02:20:08 **13** those are determined as Class 3, there's no recovery

02:20:11 **14** to Class 5. And I think that's already presented in

02:20:14 **15** the liquidation scenario.

02:20:16 **16 A** **That's presented, yes.**

02:20:16 **17 Q** So assuming that mark-to-market damages are not

02:20:21 **18** included in Class 3, the next claim that would be paid

02:20:25 **19** out of those claims-paying resources would be the

02:20:29 **20** unearned premiums; is that correct?

02:20:32 **21 A** **Yes. After the \$130 million presented in Scenario 1**

02:20:45 **22** **of the Liquidation Analysis, then the unearned premium**

02:20:56 **23** **claim is next.**

02:20:56 **24 Q** And that is a \$2.3 billion figure?

02:21:01 **25 A** **It is. As of March 24th.**

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02:21:03 **1 Q** So if we do the math, after you pay Classes 1, 3, and

02:21:10 **2** 4, you would have availability for Class 5 out of

02:21:13 **3** those claims-paying resources of \$5,509,000,000; is

02:21:21 **4** that correct?

02:21:21 **5 A** **8.2 minus 250 minus 130 and minus 2.311 billion, ah,**

02:21:34 **6** **gets you to five and a half billion dollars.**

02:21:38 **7 Q** I don't mean to test your skills in public. I have a

02:21:40 **8** calculator if you'd like.

02:21:42 **9 A** **It gets you to five and a half billion, approximately.**

02:21:46 **10 Q** Okay. Now, if you exclude future non-incurred policy

02:21:53 **11** claims from Class 5, the figures -- the only claims in

02:22:01 **12** Class 5 would then be those \$16.3 billion in

02:22:05 **13** mark-to-market claims; is that right?

02:22:10 **14 A** **Um, yes. I believe that's correct.**

02:22:12 **15 Q** Now, this might require the calculator.

02:22:21 **16** MR. PETERSON: Thank you, your Honor.

02:22:22 **17** MR. DEVORE: Oh thank you. I had one for you.

02:22:26 **18 Q** If we add a \$94 million One State Street liability

02:22:32 **19** into Class 5, there would be \$16,394,000,000 in Class

02:22:39 **20** 5 claims. Is that --

02:22:42 **21 A** **Yes. I trust the math is correct.**

02:22:45 **22 Q** And if we add \$94 million for the One State Street

02:22:56 **23** liability into Class 5, Class 5 would consist of

02:23:00 **24** \$16,394,000,000 in claims.

02:23:09 **25** So now what I'd like to do is determine what the

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02:23:12 **1** Class 5 recovery would be in that situation. And do
02:23:16 **2** you know what the percent recovery would be? Have you
02:23:19 **3** calculated it?
02:23:19 **4 A Well, it's -- it's approximately 30 percent.**
02:23:46 **5 Q** About 33.6 percent?
02:23:50 **6 A I trust that those numbers are correct. I didn't**
02:23:54 **7 input the exact numbers that you had given me, but --**
02:23:57 **8 Q** Now, the liquidation scenarios presented and the one
02:24:00 **9** that we just went through do not include any R and W
02:24:04 **10** remediation recoveries; is that correct?
02:24:06 **11 A Um, yeah. I guess that is correct.**
02:24:12 **12 Q** All right. Now, to compare apples to apples, I'd like
02:24:18 **13** to add in the \$2 billion recovery that was assumed in
02:24:22 **14** Scenario 1.
02:24:23 **15 A All right.**
02:24:23 **16 Q** And if we were to do that, would you agree that the
02:24:26 **17** claims-paying resources for Class 5 would increase
02:24:29 **18** from \$5,509,000,000 to \$7,509,000,000?
02:24:38 **19 A That's correct.**
02:24:39 **20 Q** And could we do what the recovery would be in that
02:24:43 **21** situation?
02:24:44 **22 A It would be 46 percent probably.**
02:24:48 **23 Q** Remarkably accurate. 45.8.
02:24:52 **24** Now, you testified yesterday that these
02:24:58 **25** claims-paying resources, the \$8.2 billion that we

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02:25:02 **1** started with, that was a conservative estimate?
02:25:08 **2 A Well, there's some conservatism built into that**
02:25:12 **3 estimate, yes.**
02:25:13 **4 Q** Okay. One more question on this scenario.
02:25:20 **5** We assume that there was a \$16.3 billion
02:25:26 **6** mark-to-market damage claim; is that correct?
02:25:28 **7 A Yes.**
02:25:29 **8 Q** Is that consistent with BlackRock's independent
02:25:37 **9** analysis of what the mark-to-market damage claims
02:25:38 **10** would have been as of March 24th?
02:25:42 **11 A I believe it is, other than the 16.3 includes a**
02:25:48 **12 broader range of credit default or CDS form**
02:25:55 **13 liabilities.**
02:25:57 **14 Q** Okay. So it's consistent.
02:25:59 **15** Now, I'd like to run through one more scenario as
02:26:04 **16** to what would happen as of today. Okay? Do you
02:26:09 **17** follow where I'm going?
02:26:11 **18 A I do.**
02:26:12 **19 Q** Okay. Now, in the Disclosure Statement at page 52, if
02:26:17 **20** we could get that in front of the witness. I believe
02:26:20 **21** it's Exhibit 27.
02:26:52 **22** Could you help us understand what the
02:26:53 **23** claims-paying resources would be as of today in a
02:26:56 **24** liquidation scenario?
02:26:59 **25 A What page are we looking at?**

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02:27:01 **1 Q** I'm sorry. Page 52 on the Disclosure Statement.
02:27:20 **2 A All right. I have it.**
02:27:21 **3 Q** Okay. And it states -- I'm sorry. It states there
02:27:26 **4** that claims-paying resources are \$6.8 billion, and
02:27:30 **5** those include certain amounts; is that correct?
02:27:36 **6 A Yes.**
02:27:37 **7 Q** And one of the amounts that are included in that \$6.8
02:27:41 **8** billion are future installment premiums; is that
02:27:44 **9** correct?
02:27:44 **10 A That's correct.**
02:27:45 **11 Q** So if we backed out future installment premiums,
02:27:51 **12** which, of course, in a liquidation scenario would not
02:27:53 **13** be received, I think we would get to about \$5.8
02:27:58 **14** billion in claims-paying resources as of today. Is
02:28:02 **15** that a good estimate?
02:28:03 **16 A That's correct, yes. On a present-value basis, yeah.**
02:28:07 **17 Q** Okay. Do you have that calculator in front of you?
02:28:11 **18 A I have His Honor's calculator, yes.**
02:28:16 **19 Q** Great. Now, I'd like to back out from that \$5.8
02:28:20 **20** billion the administrative expense claims, which have
02:28:24 **21** first priority. Would those still be \$250 million,
02:28:29 **22** give or take?
02:28:31 **23 A I wouldn't have a basis to make an adjustment on that,**
02:28:35 **24 no.**
02:28:35 **25 Q** So if we back those out, then gets us to Class 3

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02:28:42 **1** claims?
02:28:42 **2 A So --**
02:28:45 **3 Q** And we previously established that as of March 24th,
02:28:49 **4** there are approximately \$130 million of those claims;
02:28:54 **5** correct?
02:28:54 **6 A Yes.**
02:28:55 **7 Q** And then we obviously need to establish what the loss
02:28:59 **8** claims would be between March 24th and today if we
02:29:02 **9** were to liquidate today; is that correct?
02:29:06 **10 A Sure. That sounds like a good idea as well.**
02:29:09 **11 Q** And I believe that there were \$856 million in
02:29:13 **12** accumulated Segregated Account losses through
02:29:19 **13** September 30th. Does that sound accurate?
02:29:23 **14 A I'm trying to keep up with the calculator. I may be**
02:29:37 **15 better if I just did this in my head.**
02:29:42 **16 Um, what was the figure that you were referring to**
02:29:58 **17 for claims between March 24th and now?**
02:30:01 **18 Q** About \$856 million.
02:30:03 **19 A Okay.**
02:30:04 **20 Q** And I calculate \$856 million as of today -- I'm
02:30:09 **21** sorry -- for March 24th through today, plus 130 as of
02:30:13 **22** March 24th, and that gets me to about \$930 million.
02:30:18 **23** Is that right?
02:30:18 **24 A Ah, yes. Well, I have been deducting it from the**
02:30:23 **25 claims-paying resources, so I have \$4,564,000,000.**

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02:30:29 **1 Q** I'm sorry?

02:30:30 **2 A** **\$4,564,000,000.**

02:30:36 **3 Q** Okay. And then we obviously have to back out unearned

02:30:39 **4** premiums from that, and as of March 24th, those were

02:30:42 **5** \$2.3 billion. Would those be the same today?

02:30:46 **6 A** **Ah, no. There would have been some premium earned**

02:30:50 **7** **during that period.**

02:30:51 **8 Q** So do you know approximately how much that would be?

02:30:54 **9 A** **No. I wouldn't be able to do that.**

02:30:57 **10 Q** So if we use the \$2.3 billion number, that will give

02:31:02 **11** us a conservative estimate?

02:31:03 **12 A** **It would.**

02:31:04 **13 Q** Okay. So after you back out the unearned premiums,

02:31:11 **14** what do you have for classified availability?

02:31:13 **15 A** **\$2,253,000,000.**

02:31:17 **16 Q** I'm sorry. Could you say that again?

02:31:19 **17 A** **\$2,253,000,000.**

02:31:21 **18 Q** Okay. So now, of course, we have to get to what's in

02:31:25 **19** Class 5.

02:31:29 **20 A** **We do.**

02:31:30 **21 Q** Now, you testified yesterday that there continue to be

02:31:36 **22** approximately \$3 billion worth of mark-to-market CDS

02:31:41 **23** exposure; is that correct?

02:31:42 **24 A** **Yes.**

02:31:42 **25 Q** Is that approximately where that exposure would be

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02:31:47 **1** today?

02:31:48 **2 A** **To the best of my knowledge, yes.**

02:31:50 **3 Q** And I believe you testified that's the worst-case

02:31:53 **4** scenario?

02:31:55 **5 A** **Well, that -- that presumes some litigation as to our**

02:32:03 **6** **-- the Segregated Account's or Ambac in general's**

02:32:08 **7** **liabilities on a mark-to-market basis versus, ah,**

02:32:13 **8** **economic damage basis.**

02:32:14 **9 Q** So if we assume that \$3 billion falls within Class 5,

02:32:20 **10** that's a fairly worst-case scenario?

02:32:23 **11 A** **Yeah, I guess.**

02:32:25 **12 Q** And then if we add in our meager \$94 million lease

02:32:30 **13** liability, we get about \$3,094,000,000 in Class 5?

02:32:36 **14 A** **Yes.**

02:32:36 **15 Q** Am I missing any other Class 5 claims?

02:32:40 **16 A** **Ah, not that I recall. But this is a rather**

02:32:46 **17** **difficult, complex plan to keep all the different**

02:32:51 **18** **types of claims, classes of claims in one's head.**

02:32:55 **19 Q** So now if we divide the \$2,253,000,000 in Class 5

02:33:05 **20** availability by the \$3,094,000,000 in Class 5 claims,

02:33:13 **21** what is the Class 5 recovery?

02:33:19 **22 A** **72.8 percent.**

02:33:22 **23 Q** And then if we add in \$2 billion in R and W

02:33:28 **24** remediation recoveries, we would get to \$4,253,000,000

02:33:37 **25** in Class 5 availability; is that correct?

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02:33:40 **1 A** **That sounds correct, yes.**

02:33:43 **2 Q** And then if we subtract out in that scenario of Class

02:33:50 **3** 5 claimants, we receive a 100-cent recovery.

02:33:52 **4 A** **I believe that is correct, yes.**

02:33:54 **5 Q** And in that scenario, there would actually be a

02:34:00 **6** \$1,159,000,000 recovery to shareholders; is that

02:34:05 **7** correct?

02:34:05 **8 A** **That sounds as if that's the case, yes.**

02:34:07 **9 Q** You would consider that a tremendous value?

02:34:10 **10 A** **If I had it, it certainly would be tremendous, yes.**

02:34:15 **11 Q** I apologize. I'm going to do one more short variation

02:34:23 **12** of this so I'm not accused of leaving out the

02:34:26 **13** policyholders that sit behind me.

02:34:28 **14 A** **All right.**

02:34:28 **15 Q** I want to figure out what my recovery would be as of

02:34:32 **16** today if the policyholders were included as classified

02:34:35 **17** claimants.

02:34:38 **18 A** **The non-CDS --**

02:34:41 **19 Q** Yes.

02:34:41 **20 A** **-- policyholders?**

02:34:42 **21 Q** Correct. So that we get the whole range of

02:34:45 **22** possibilities here.

02:34:46 **23** So if we add in the \$6 billion base-case, you

02:34:55 **24** testified that was approximately what it was today?

02:34:57 **25 A** **I did.**

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02:34:58 **1 Q** Okay. So we have \$3,094,000,000 plus the

02:35:08 **2** \$6,000,000,000 base-case. That gets me to

02:35:13 **3** \$9,094,000,000 under the base-case?

02:35:19 **4 A** **It does.**

02:35:19 **5 Q** All right. And if I divide the \$2,253,000,000 of

02:35:30 **6** Class 5 availability by that \$9,094,000,000 in Class 5

02:35:37 **7** claims, I'd get a 25 percent recovery; correct?

02:35:45 **8 A** **I haven't been following along on --**

02:35:47 **9 Q** I'm happy to represent --

02:35:49 **10 A** **-- His Honor's calculator anymore, but I'll trust that**

02:35:54 **11** **those calculations are -- they sound accurate.**

02:35:57 **12 Q** So that's a 25 percent. And if I were to add in the

02:36:05 **13** \$2 billion in R and W remediation recoveries to that,

02:36:09 **14** we'd get \$4,253,000,000 in Class 5 availability. And

02:36:16 **15** if we divide that by the \$9,094,000,000, Class 5

02:36:25 **16** claimants would receive 47 percent. Does that sound

02:36:29 **17** about right?

02:36:31 **18 A** **Yes, it sounds about right.**

02:36:32 **19 Q** And those dollars would be paid today in a liquidation

02:36:40 **20** scenario?

02:36:41 **21 A** **I'm quite sure that a liquidation wouldn't be paying**

02:36:44 **22** **out any money today or anytime in the next few years,**

02:36:52 **23** **I believe.**

02:36:53 **24 Q** Would my clients need to wait until 2050?

02:36:57 **25 A** **It's likely that payments in a liquidation would be**

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02:37:02 **1** **made somewhere between now and 2050.**

02:37:04 **2 Q** More likely on the now side of that spectrum?

02:37:08 **3 A** **Well, perhaps before 2020 even.**

02:37:11 **4 Q** Great. Thank you.

02:37:15 **5** That's all the math I have for you.

02:37:19 **6** A couple more questions.

02:37:20 **7 A** **Thank you.**

02:37:20 **8 Q** Now, all of the liquidation analyses that we've been

02:37:30 **9** discussing are based on the termination of policies;

02:37:34 **10** is that correct?

02:37:35 **11 A** **Yes.**

02:37:36 **12 Q** Because -- okay.

02:37:39 **13** Now, Mr. Peterson, based on your experience in the

02:37:44 **14** liquidation of insurance companies, can value be

02:37:47 **15** realized by transferring the policies to other

02:37:50 **16** insurers?

02:37:52 **17 A** **In the case of liquidation of a life insurance**

02:37:55 **18** **company, it's common to transfer the policies to**

02:38:00 **19** **another insurer, yes.**

02:38:02 **20 Q** How about a municipal bond insurer? Could value be

02:38:07 **21** realized by transferring policies?

02:38:08 **22 A** **To my knowledge, a municipal bond insurer has never**

02:38:12 **23** **been liquidated.**

02:38:13 **24 Q** But it is possible to transfer the policies to obtain

02:38:16 **25** value?

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02:38:17 **1** MR. VAN SICKLEN: Objection. Now we're really

02:38:19 **2** getting speculative.

02:38:20 **3** THE COURT: Sustained.

02:38:23 **4 Q** OCI's conducted various valuations of the assets of

02:38:37 **5** Ambac; is that correct?

02:38:38 **6 A** **Yes.**

02:38:39 **7 Q** Has any valuation been placed on the policies that are

02:38:45 **8** located in the General Account?

02:38:47 **9 A** **We have reviewed the value of the runoff of the**

02:38:56 **10** **municipal bond book, yes.**

02:38:58 **11 Q** And what is that value?

02:38:59 **12 A** **I would -- that figure would be confidential.**

02:39:05 **13 Q** Are you willing to give me a range that it's more

02:39:08 **14** than, say, \$2 billion?

02:39:11 **15** MR. VAN SICKLEN: I guess I object.

02:39:12 **16 A** **No.**

02:39:13 **17** MR. VAN SICKLEN: If it's confidential, it's

02:39:14 **18** confidential.

02:39:17 **19** THE COURT: Sustained.

02:39:20 **20 Q** Did OCI ever attempt to obtain a buyer for these

02:39:24 **21** policies in the General Account?

02:39:28 **22 A** **There have been inquiries. The substance of any of**

02:39:37 **23** **those discussions I believe would also be**

02:39:41 **24** **confidential.**

02:39:42 **25 Q** Would it be fair to say that those inquiries proposed

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02:39:48 **1** substantial value as consideration?

02:39:52 **2** MR. VAN SICKLEN: Same objection.

02:39:53 **3** THE COURT: Sustained.

02:40:00 **4 Q** Is it fair to say that my client's recoveries in a

02:40:04 **5** liquidation scenario increase by any value that is

02:40:08 **6** realized in the sale of policies?

02:40:16 **7** MR. VAN SICKLEN: I guess I object to that as

02:40:17 **8** speculative. There's a lot of moving parts.

02:40:20 **9** MR. DEVORE: The whole Liquidation Analysis is

02:40:23 **10** speculation.

02:40:23 **11** THE COURT: That's correct. Everything you've

02:40:27 **12** been doing is speculation, your questioning.

02:40:30 **13 A** **Um, yes. I suppose if you could realize value that**

02:40:37 **14** **adds to, ah, the amounts that could be distributed in**

02:40:42 **15** **the liquidation.**

02:40:44 **16 Q** Okay. I have one last topic of conversation, and that

02:40:50 **17** has to do with the releases that are provided in the

02:40:53 **18** Plan.

02:40:53 **19** I believe we've already established that Ambac

02:41:04 **20** Assurance Corporation's sole shareholder is Ambac

02:41:09 **21** Financial Group; is that correct?

02:41:09 **22 A** **We have, yes.**

02:41:10 **23 Q** And AFG is not within the jurisdiction of OCI?

02:41:15 **24 A** **That's correct as well.**

02:41:15 **25 Q** And that's because it's not an insurer?

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02:41:17 **1 A** **Well, to say that it's not within the jurisdiction is**

02:41:21 **2** **not wholly accurate. There are holding company**

02:41:28 **3** **regulations that exist that require reporting of**

02:41:32 **4** **holding company transactions, financial statements of**

02:41:35 **5** **holding companies, and so forth. There are also**

02:41:41 **6** **collateral examination provisions within our -- within**

02:41:46 **7** **our law that allow for some examination of affiliates**

02:41:53 **8** **of the insurance company and parties that have, you**

02:42:01 **9** **know, an integral relationship with the insurance**

02:42:06 **10** **company. But certainly the control, the regulatory**

02:42:11 **11** **control that exists over AFG is less than as to an**

02:42:17 **12** **insurance company.**

02:42:21 **13 Q** But OCI could not bring AFG into this court for

02:42:27 **14** rehabilitation?

02:42:29 **15 A** **That's correct.**

02:42:30 **16 Q** Okay. Are you aware that no rent payment was made to

02:42:45 **17** my clients for November?

02:42:47 **18 A** **I was informed of that within the last few days, yes.**

02:42:51 **19 Q** Now, is it OCI's intent through the Plan to release

02:42:57 **20** AFG from liability for that rent payment?

02:43:01 **21 A** **I can't answer that question. I don't know.**

02:43:05 **22 Q** You don't know what the intent of OCI is with respect

02:43:08 **23** to releasing AFG? Does OCI have any intent to let AFG

02:43:17 **24** get off the hook of paying rent payments?

02:43:19 **25** MR. VAN SICKLEN: I guess I object. The witness

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02:43:20 **1** doesn't have foundation. AFG is in a federal
02:43:23 **2** bankruptcy. There's so many layers of
02:43:23 **3** speculativeness.
02:43:26 **4** MR. DEVORE: Your Honor, I'm asking him what the
02:43:28 **5** intent of OCI is under the Plan, which he's testified
02:43:31 **6** at great length as to what the intent of certain
02:43:34 **7** provisions are. And my question is, is this plan
02:43:37 **8** designed to release AFG from having to pay rent?
02:43:42 **9** THE COURT: I'll allow you to answer that if you
02:43:44 **10** can.
02:43:44 **11 A** **There was no goal in -- in that respect. We have**
02:43:51 **12 taken -- OCI has taken the position that the lease is**
02:43:55 **13 an obligation of AFG, the holding company, and that,**
02:44:01 **14 ah, is a relation or an obligation between One State**
02:44:06 **15 Street and AFG.**
02:44:09 **16 There are contingencies that have been addressed**
02:44:13 **17 in the Plan if that obligation becomes one of Ambac**
02:44:20 **18 Assurance.**
02:44:26 **19 Q** I apologize. I do have just a couple follow-up
02:44:29 **20** questions of things that were testified to earlier.
02:44:32 **21 A** **Is that a double-dip?**
02:44:34 **22 Q** I sure hope not.
02:44:38 **23** Does the Plan prevent Ambac from writing new
02:44:47 **24** policies?
02:44:48 **25 A** **Not specifically.**

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02:44:52 **1 Q** And it's OCI's hope that Ambac will in the future be
02:44:57 **2** able to write new policies?
02:44:59 **3 A** **Well, it's our hope primarily that policyholders are**
02:45:04 **4 made whole. And, you know, beyond that, if Ambac**
02:45:13 **5 could write policyholders policies again, that would**
02:45:16 **6 be just fine with us. If somehow Everspan, for**
02:45:24 **7 example, can begin to write policies and that enhances**
02:45:28 **8 value to the policyholders, that may be acceptable to**
02:45:32 **9 OCI as well.**
02:45:34 **10 Q** Now, as we sit here today, are there any controls that
02:45:37 **11** would prevent Ambac from issuing policies on risky
02:45:41 **12** financial instruments going forward?
02:45:45 **13 A** **I think there's absolutely no market ability for them**
02:45:50 **14 to do so.**
02:45:50 **15 Q** Does OCI have the ability to prevent the General
02:45:55 **16** Account from issuing such policies?
02:45:57 **17 A** **We would have that ability if we felt it necessary to**
02:46:02 **18 exercise it.**
02:46:03 **19 Q** Okay. Now, you testified on direct on Tuesday
02:46:12 **20** afternoon, I believe, that you are not aware of
02:46:15 **21** previous rehabilitations in Wisconsin that included an
02:46:20 **22** opt-out provision. Do you recall that testimony?
02:46:23 **23 A** **Yes.**
02:46:23 **24 Q** I believe you also testified that you don't recall
02:46:25 **25** previous rehabilitations where claimants were allowed

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02:46:33 **1** to recover the liquidation value of their claim?
02:46:37 **2 A** **That's consistent with my testimony, yes.**
02:46:40 **3 Q** Do you recall if in any of those cases the issues were
02:46:44 **4** actually litigated?
02:46:47 **5 A** **I don't know that they were.**
02:46:51 **6 Q** In any of these prior rehabilitations you were
02:47:01 **7** referring to, do you know if plan objectors -- or I'm
02:47:06 **8** sorry -- if claimants calculated the liquidation value
02:47:10 **9** of their claim independently?
02:47:14 **10 A** **I don't know that they did.**
02:47:15 **11 Q** So you have no idea if a claimant actually received
02:47:19 **12** its liquidation value in those other rehabilitations?
02:47:24 **13 A** **That hasn't been evaluated, to my knowledge. Or I'm**
02:47:31 **14 not aware of that kind of evaluation.**
02:47:34 **15 Q** So it is entirely possible that claimants have in fact
02:47:39 **16** received liquidation values in other rehabilitations?
02:47:45 **17** MR. VAN SICKLEN: Back to the possibilities in
02:47:46 **18** the word. Object.
02:47:47 **19** THE COURT: Sustained. He's answered the
02:47:49 **20** question.
02:47:50 **21** MR. DEVORE: With that, I thank Mr. Peterson for
02:47:52 **22** his testimony.
02:47:54 **23** THE COURT: Are there any other persons?
02:47:58 **24** MR. BLOOMGARDEN: Your Honor would be pleased to
02:47:59 **25** hear that the ground that I was going to plow has

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02:48:01 **1** already been plowed or covered by other counsel, so I
02:48:06 **2** have no questions at this time. But I would reserve
02:48:09 **3** the right to examine Mr. Peterson within the scope of
02:48:12 **4** any redirect.
02:48:15 **5** THE COURT: Anyone else here who wanted to --
02:48:22 **6** among the objectors that wanted to question? I know
02:48:28 **7** you're all resisting the urge to come up and do that.
02:48:32 **8** All right. Anyone on the telephone?
02:48:39 **9** All right. There apparently is no one who
02:48:42 **10** wishes.
02:48:43 **11** MR. HOOPER (speaking via telephone): No, your
02:48:43 **12** Honor. Thank you.
02:48:44 **13** THE COURT: Just a moment. Was there someone?
02:48:47 **14** MR. HOOPER (speaking via telephone): No. No,
02:48:48 **15** your Honor. Sorry. The phone had been muted while my
02:48:54 **16** clients were trying to speak. But we do not have any
02:48:57 **17** questions, your Honor.
02:48:57 **18** THE COURT: All right. Is there any redirect?
02:48:58 **19** MR. VAN SICKLEN: Yes, your Honor. And just to
02:49:00 **20** respond to Mr. Bloomgarden's point, I would object to
02:49:05 **21** recross. I mean, we only have so much time in this
02:49:09 **22** proceeding. If Mr. Bloomgarden has a question, he
02:49:12 **23** should get it out. If we're going to go through
02:49:15 **24** endless cycles, we'll never be done in time to get to
02:49:20 **25** closing arguments on the 29th.

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02:49:21 **1** THE COURT: Well, Mr. Bloomgarden, do you have
02:49:23 **2** anything?
02:49:23 **3** MR. BLOOMGARDEN: Your Honor, I indicated I have
02:49:26 **4** nothing now, Depending what I hear on redirect. If he
02:49:28 **5** goes into something on redirect, then I think any
02:49:31 **6** counsel -- it's fair to ask a follow-up question
02:49:34 **7** within the scope of the redirect. So nothing at this
02:49:37 **8** moment, your Honor.
02:49:37 **9** THE COURT: Do you have any redirect?
02:49:38 **10** MR. VAN SICKLEN: Yes, I do.
02:49:39 **11** THE COURT: All right. You want to take a break
02:49:42 **12** now for lunch and then start with redirect after
02:49:45 **13** lunch?
02:49:45 **14** MR. VAN SICKLEN: Sure. That would be fine.
02:49:47 **15** THE COURT: All right. We'll be in -- we'll
02:49:49 **16** take the noon recess. Be back at one o'clock. And
02:49:53 **17** you'll be on for redirect.
02:49:56 **18** MR. PETERSON: Thank you, your Honor.
02:50:01 **19** (Lunch Recess taken at 11:50 a.m.)
02:50:01 **20** (The following proceedings reported
03:26:05 **21** by Reporter Flakne.)
04:03:51 **22** THE COURT: All right. Be seated. Are the
04:04:26 **23** telephone participants on the line.
04:04:29 **24** A VOICE: Yes, Your Honor.
04:04:30 **25** THE COURT: All right. The Circuit Court for

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04:04:33 **1** Dane County is again in session. The matter of the
04:04:37 **2** Rehabilitation of the Segregated Account of Ambac
04:04:45 **3** Assurance Corporation, and we were at the point of
04:04:47 **4** redirect with Mr. Peterson who is now on the stand.
04:04:50 **5** Mr. Van Sicklen, you may proceed.
04:04:54 **6** MR. VAN SICKLEN: And, Your Honor, before I
04:04:54 **7** start questioning, just two small housekeeping
04:04:57 **8** matters:
04:04:57 **9** One is there has been some discussion among
04:05:00 **10** counsel about just trying to keep the schedule in
04:05:02 **11** place. And so I just want all the objecting counsel
04:05:04 **12** to know that we're thinking that the most efficient
04:05:07 **13** and quickest use of the last two witnesses is to start
04:05:10 **14** with Mr. Barranco and then have Ms. Matanle. There
04:05:15 **15** was some uncertainty, so I just want everybody to have
04:05:17 **16** a fair heads up on that.
04:05:19 **17** The second procedural point is we've been using
04:05:23 **18** all these volumes of exhibits that the RMBS movants
04:05:28 **19** have conveniently brought to us and I would -- I
04:05:31 **20** think most of it is already in evidence through my
04:05:34 **21** original motion, but just for the record, since we
04:05:37 **22** keep referring to it, I would move for admission into
04:05:40 **23** evidence and as part of the record all of their
04:05:43 **24** documents other than Exhibit 38A. They have -- I'm
04:05:49 **25** sorry, 38. They've moved in the Commissioner's

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04:05:52 **1** letter, which is the 38A, so everything in their
04:05:57 **2** binders, 1 through 64, other than Exhibit 38 and
04:06:01 **3** Exhibit 39.
04:06:02 **4** And then in addition various parties have used
04:06:06 **5** the separately marked copy of the amended order, which
04:06:10 **6** would be Exhibit 65, so I'd also move that into
04:06:13 **7** evidence.
04:06:16 **8** MR. GREENWALD: Your Honor, if I could be heard
04:06:17 **9** on the motion?
04:06:19 **10** THE COURT: Yes.
04:06:20 **11** MR. GREENWALD: I would object. There is a
04:06:21 **12** reason that I only moved into evidence one document
04:06:23 **13** where the foundation had been laid. Mr. Van Sicklen's
04:06:26 **14** motion would effectively sweep in many of the
04:06:28 **15** documents that we objected to admission prior to this
04:06:31 **16** at the beginning of the hearing. I believe that we as
04:06:35 **17** objectors are able to move the documents into evidence
04:06:40 **18** which we believe are appropriate into evidence and we
04:06:44 **19** would object to en mass admitting documents into
04:06:48 **20** evidence that are really not evidence. They're
04:06:50 **21** documents we have used for evidence, for example,
04:06:54 **22** affidavits and other documents. If Mr. Van Sicklen
04:06:57 **23** wants to make specific motions to admit specific
04:07:00 **24** documents, I think that would be a more appropriate
04:07:02 **25** way to proceed.

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04:07:04 **1** MR. DEVORE: May I be heard?
04:07:04 **2** THE COURT: We just heard from you.
04:07:09 **3** MR. DEVORE: This is Devore. I also object,
04:07:10 **4** would join in the objection. I want to state the One
04:07:14 **5** State Street Incorporated's objection stated at the
04:07:16 **6** beginning of these proceedings.
04:07:17 **7** THE COURT: All right. The motion will be
04:07:19 **8** granted. In this type of proceeding this type of use
04:07:22 **9** of these documents, and consistent with the prior
04:07:26 **10** ruling, recognizing these are documents that are
04:07:30 **11** created generally in the normal course of the business
04:07:33 **12** of this agency, they are appropriate to be received,
04:07:38 **13** so I'll grant that motion. Does the clerk have any
04:07:42 **14** questions on that for your minutes? All right.
04:07:45 **15** Proceed.
04:07:46 **16** MR. GREENWALD: Your Honor, with the Court's
04:07:47 **17** indulgence I just want to make it clear and these are
04:07:49 **18** the bases that we raised earlier in the week including
04:07:52 **19** hearsay, hearsay within hearsay, and other objections.
04:07:55 **20** I just wanted to make sure they were incorporated by
04:07:59 **21** reference to the earlier motion for the record, Your
04:08:01 **22** Honor.
04:08:01 **23** THE COURT: You made that record and the Court's
04:08:03 **24** ruling previously would cover that I believe.
04:08:14 **25** Mr. Bentley is the one with the cheese hat.

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04:08:14 **1** **REDIRECT EXAMINATION**

04:08:14 **2** BY MR. VAN SICKLEN:

04:08:19 **3 Q** He's the man of many hats we've seen. Mr. Peterson,

04:08:24 **4** to borrow or steal Mr. Welsh's analogy, I think we've

04:08:28 **5** plowed, disk, seeded, applied a couple of times

04:08:32 **6** herbicides, and I think it's time to harvest and get

04:08:34 **7** you off the stand and allow you to proceed?

04:08:36 **8 A** **That would be appreciated.**

04:08:38 **9 Q** So I just have some follow-up questions. They're

04:08:41 **10** going to be a little bit scattered because so many

04:08:43 **11** different counsel asked you different types of

04:08:45 **12** questions, so bear with me in the organization.

04:08:49 **13** Mr. Owen, counsel for Lloyds, asked you a number

04:08:54 **14** of questions about the Excess of Loss reinsurance

04:08:57 **15** agreement and the secured note, which would be

04:09:00 **16** Exhibits 5 and 6. I've lost my assistant, but can I

04:09:07 **17** borrow the assistant.

04:09:26 **18 A** **Thank you.**

04:09:27 **19 Q** Thank you, Kaija. I'm going to start with Exhibit 6,

04:09:31 **20** which is the Excess of Loss reinsurance agreement, and

04:09:35 **21** I would like you -- I would like to kind of go

04:09:38 **22** backwards and start where Mr. Owen left off on Section

04:09:41 **23** 4.01 the follow the fortune's provision and that's on

04:09:46 **24** page four.

04:09:47 **25 A** **I have it.**

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04:09:47 **1 Q** Okay. About five lines down there is a reference

04:09:53 **2** about the true intent of the agreement. Do you see

04:09:56 **3** that?

04:10:05 **4 A** **Yes.**

04:10:06 **5 Q** What is your and OCI's intent and understanding

04:10:13 **6** regarding the type of obligation that this reinsurance

04:10:17 **7** agreement creates?

04:10:18 **8 A** **It creates an absolute obligation for the General**

04:10:25 **9** **Account to fund claim payments authorized or made by**

04:10:33 **10** **the Segregated Account.**

04:10:36 **11 Q** Okay. And turning earlier to Section 1.02 on page two

04:10:41 **12** of the reinsurance agreement.

04:10:48 **13 A** **All right.**

04:10:49 **14 Q** You have some questions about -- starts off at line

04:10:53 **15** one about reinsurance shall provide payments and goes

04:10:56 **16** on.

04:10:56 **17 A** **Mm-hmm (Yes).**

04:10:57 **18 Q** Again what is your understanding and that of OCI's and

04:11:01 **19** your intent regarding the type of obligation that this

04:11:04 **20** provision creates?

04:11:06 **21 A** **Again it is intended to create that absolute**

04:11:11 **22** **obligation for the General Account to fund claim**

04:11:16 **23** **payments as made or authorized by the Segregated**

04:11:23 **24** **Account.**

04:11:23 **25 Q** And as we drop down after the introduction about the

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04:11:27 **1** reinsurance -- And, by the way, is the reinsurer, the

04:11:32 **2** General Account and the Segregated Account is the

04:11:36 **3** ceding company as used in this document?

04:11:41 **4 A** **Yes. As used in this document, yep.**

04:11:43 **5 Q** Okay. And after the provision about the reinsurer

04:11:48 **6** shall provide payments, it describes four different

04:11:51 **7** types of payments, and then there is a provision that

04:11:53 **8** says "provided that in each case." Do you see that?

04:11:57 **9 A** **Mm-hmm (Yes).**

04:11:58 **10 Q** What -- Is your understanding that that provided in

04:12:02 **11** each case modifies the foregoing -- the above four

04:12:06 **12** types of payments or something else?

04:12:09 **13 A** **It just modifies those types of payments and is in**

04:12:15 **14** **recognition of the Plan terms that are 25-cent cash**

04:12:23 **15** **and notes.**

04:12:23 **16 Q** It's not qualifying the absolute nature of the

04:12:27 **17** obligation?

04:12:28 **18 A** **That's correct in my opinion.**

04:12:29 **19 Q** And then going forward, I'm sorry, earlier to

04:12:33 **20** Exhibit 5, the secured note if you can look that, the

04:12:38 **21** second page of the secured note?

04:12:40 **22 A** **Just a moment. I have it.**

04:12:49 **23 Q** In paragraph 1A is that essentially the identical

04:12:55 **24** language that we just looked at at the start of the

04:12:57 **25** reinsurance agreement except it here's not referring

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04:13:02 **1** to cedant and reinsurer.

04:13:05 **2 A** **Yeah. That's the same language.**

04:13:06 **3 Q** And what is your understanding in regard to this

04:13:09 **4** provision in terms of its obligations?

04:13:11 **5 A** **Again it requires or establishes an absolute duty for**

04:13:16 **6** **the General Account to fund payments made or**

04:13:25 **7** **authorized by the Segregated Account through this**

04:13:27 **8** **surplus note in this case.**

04:13:29 **9 Q** Is that how OCI intends to go forward in use of that

04:13:36 **10** note and reinsurance agreement if the Plan's approved?

04:13:40 **11 A** **It certainly is.**

04:13:40 **12 Q** And again there is the same phrase there in the middle

04:13:44 **13** of the paragraph about provided in each case is -- is

04:13:47 **14** your understanding the same in this context as in the

04:13:49 **15** reinsurance agreement?

04:13:50 **16 A** **It is.**

04:13:51 **17 Q** Okay. Mr. Greenwald asked you several questions about

04:13:56 **18** a subsidiary named Everspan, formerly Connie Lee. Do

04:14:02 **19** you recall that?

04:14:02 **20 A** **I do.**

04:14:03 **21 Q** Who was a hundred percent owner of Everspan?

04:14:07 **22 A** **Ambac Insurance Corporation.**

04:14:09 **23 Q** And does AFG, the holding company, have any ownership

04:14:13 **24** or reinsurance agreements or any other direct ties

04:14:17 **25** with Everspan to your knowledge?

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04:14:19 **1 A No direct ties.**

04:14:20 **2 Q** And you were asked some questions about if in the

04:14:23 **3** future the General Account was in a position to

04:14:30 **4** attract capital or capitalize Everspan so it could

04:14:35 **5** write new business or generate profits, what entity

04:14:38 **6** would be the beneficiary of any such profits?

04:14:42 **7 A All of those profits would flow through Ambac**

04:14:46 **8 Assurance Corporation.**

04:14:46 **9 Q** And would those -- all those profits be available to

04:14:49 **10** support the Plan obligations?

04:14:52 **11 A They would.**

04:14:53 **12 Q** You were asked a number of questions by several of the

04:14:57 **13** attorneys about the -- the recent allocation of

04:15:04 **14** the -- of these tax-related, refund-related

04:15:07 **15** liabilities and the issue of NOL, so I'll turn to that

04:15:12 **16** area. These questions of NOLs, is it fair to say that

04:15:17 **17** there is a difference of opinion about whose NOLs

04:15:22 **18** those are and what steps could be taken as between AAC

04:15:27 **19** on the one hand and the bondholder creditors of the

04:15:33 **20** bankrupt parent company?

04:15:35 **21 A The AFG bondholders have made it quite clear that they**

04:15:40 **22 believe they have a right to those NOLs and are**

04:15:44 **23 willing to litigate that point.**

04:15:46 **24 Q** And have they made to your knowledge threats to the

04:15:49 **25** effect that absent some other negotiated resolution

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04:15:54 **1** that they would try to exercise their rights through

04:15:57 **2** rejection of the tax-sharing agreement or

04:16:00 **3** deconsolidation or some other steps to try to take all

04:16:04 **4** of those NOLs?

04:16:07 **5** MR. GREENWALD: Objection, leading and compound.

04:16:08 **6** THE COURT: Overruled. It doesn't suggest the

04:16:12 **7** answer, so it's not leading. Compound questions are

04:16:15 **8** the bread and butter of this whole proceeding by

04:16:21 **9** anybody who's asked questions, including yourself, so

04:16:24 **10** I'm not going to change that at this point. You may

04:16:28 **11** answer.

04:16:29 **12** THE WITNESS: I understand that they have made

04:16:31 **13** those threats.

04:16:32 **14 Q** Okay. And do you feel that OCI has -- has and is

04:16:40 **15** continuing to do everything within its power

04:16:42 **16** reasonably to protect AAC's interest in regard to

04:16:46 **17** those NOLs?

04:16:47 **18 A Absolutely.**

04:16:48 **19 Q** You were asked some questions about the rep and

04:16:56 **20** warranty litigation under the subject of remediation;

04:17:00 **21** do you recall that?

04:17:01 **22 A I do.**

04:17:01 **23 Q** Okay. Several times probably. Which of the two

04:17:04 **24** accounts of Ambac is funding 100 percent of the cost

04:17:08 **25** of those lawsuits?

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04:17:16 **1** MR. DEVORE: Objection. We were foreclosed from

04:17:19 **2** inquiry into the R and W remediation and counsel

04:17:21 **3** should not now be inquire into that subject.

04:17:26 **4** THE COURT: I don't think he's doing that. I

04:17:27 **5** think the question is quite simple and that is who is

04:17:29 **6** funding it. I'm assuming that's as far as it goes.

04:17:29 **7** BY VAN SICKLEN:

04:17:33 **8 Q** Yeah.

04:17:33 **9 A The General --**

04:17:35 **10 Q** I've been asking for an appraisal of the expected

04:17:38 **11** recovery which was the concern that Mr. Devore raised.

04:17:42 **12** I'm asking what is paying for the litigation costs.

04:17:46 **13 A The General Account is funding those costs.**

04:17:48 **14 Q** And to the extent there are recoveries in any of those

04:17:51 **15** different pieces of litigation, will one hundred

04:17:57 **16** percent of those recoveries, net of expenses, be

04:17:59 **17** available to help fund the Plan?

04:18:01 **18 A They will go into the General Account and be available**

04:18:03 **19 to fund the Plan.**

04:18:06 **20 Q** You were asked some questions about subrogation. Mr.

04:18:10 **21** Greenwald had an example about if you were trying to

04:18:14 **22** recover a hundred dollars, do you recall that?

04:18:17 **23 A I do.**

04:18:18 **24 Q** Okay. Explain to the Court what most of these -- Do

04:18:22 **25** these recoveries relate to the present to payments

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04:18:26 **1** that were made after the Rehabilitation or before?

04:18:31 **2 A Cash recoveries, if any, would likely relate to**

04:18:36 **3 payments made before the Rehabilitation.**

04:18:38 **4 Q** And is there an approximate amount in total of those

04:18:43 **5** types of pre-Rehabilitation payments that would be

04:18:47 **6** theoretically subject to these recovery claims?

04:18:50 **7 A Well, my -- my recollection is that there's -- there**

04:18:54 **8 has been about \$2 billion of RMBS claims payments made**

04:18:59 **9 prior to the commencement of the Rehabilitation**

04:19:03 **10 action.**

04:19:03 **11 Q** And those pre-Rehabilitation payments were one hundred

04:19:08 **12** cents on the dollar?

04:19:08 **13 A They were.**

04:19:09 **14 Q** Mr. Owen asked you some questions about whether

04:19:15 **15** financial statements had been prepared for the

04:19:18 **16** Segregated Account and the General Account. Could you

04:19:21 **17** explain what fact has been occurring in that regard?

04:19:26 **18 A Both the General Account and Segregated Account have**

04:19:30 **19 issued statutory financial statements on a quarterly**

04:19:35 **20 basis, as is normally required for insurance entities,**

04:19:40 **21 and those are been issued on a timely basis. The**

04:19:46 **22 third quarter statement --**

04:19:47 **23 Q** When was the most recently filed financial statement?

04:19:50 **24 A The third quarter financial statement was filed and**

04:19:55 **25 made available Monday of this week.**

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04:19:57 **1 Q** And are certain of those financial statements in the
04:20:01 **2** recent periods referenced on the website as part of
04:20:06 **3** the materials submitted with the Plan?
04:20:08 **4 A** **Those through June 30th. The June 30th quarter are**
04:20:13 **5** **certainly on the website, and I -- whether it's been**
04:20:16 **6** **-- the third quarter statements have been put on yet**
04:20:19 **7** **or not, I -- I don't know, but I've -- if they**
04:20:22 **8** **haven't, I'm sure that they will be quite soon.**
04:20:25 **9 Q** Does the expectation that that past practice will
04:20:28 **10** continue in regard to posting the financial
04:20:30 **11** statements?
04:20:30 **12 A** **Yes. That's the expectation.**
04:20:32 **13 Q** And what is OCI's anticipation in regard to
04:20:36 **14** preparation of -- of financial statements in the
04:20:38 **15** future for the two accounts?
04:20:40 **16 A** **We intend to continue to have statutory financial**
04:20:47 **17** **statements prepared and released on a quarterly basis**
04:20:51 **18** **consistent with the types of reporting on any other**
04:20:55 **19** **insurance company.**
04:20:57 **20 Q** Okay. You were asked some questions about the annual
04:21:00 **21** reporting process, annual review process. Why did you
04:21:04 **22** choose to make it annual as opposed to a more frequent
04:21:08 **23** basis?
04:21:09 **24 A** **Well, the factors that weigh into OCI's evaluation of**
04:21:20 **25** **the financial condition of the General Account or**

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04:21:24 **1** **Segregated Account don't change typically very**
04:21:29 **2** **materially from one month to another or one quarter to**
04:21:33 **3** **another, and so that an annual report seemed to be**
04:21:40 **4** **adequate. I guess I would add, too, that if somehow**
04:21:44 **5** **there was a material change in the financial position**
04:21:51 **6** **of the General Account or Segregated Account**
04:21:56 **7** **through -- through perhaps a success -- a major**
04:22:02 **8** **success on the reps and warranties litigation, OCI**
04:22:06 **9** **wouldn't be precluded from making an additional report**
04:22:11 **10** **to the Court and perhaps -- and seeking some payment**
04:22:16 **11** **on the surplus notes more promptly than as part of the**
04:22:20 **12** **annual reporting process.**
04:22:22 **13 Q** And did you -- Well, strike that. Mr. Owen on behalf
04:22:27 **14** of Lloyds -- Let me step back. Both counsel for
04:22:33 **15** Depfa and counsel for All/Lloyds have asked you a
04:22:39 **16** number of questions. Are all three of those entities
04:22:42 **17** pertaining to the same student loan deal?
04:22:44 **18 A** **I believe they have interest in the same deals, yes.**
04:22:48 **19 Q** Okay. And ALL is the issuer and --
04:22:51 **20 A** **Yeah. ALL Student Loan is the issuer, Depfa, Lloyds**
04:22:56 **21** **are holders of those securities.**
04:22:58 **22 Q** Okay. And Mr. Owen on behalf of ALL/Lloyds asked you
04:23:03 **23** some questions about why there -- at least as I
04:23:06 **24** understood it, never been an explanation about why OCI
04:23:11 **25** regarded that particular transaction to be risky or

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04:23:18 **1** have reason to be allocated. Do you recall that?
04:23:21 **2 A** **I -- Yes. I recall those -- that questioning.**
04:23:25 **3 Q** And in evidence already is your fourth affidavit, so,
04:23:30 **4** Kaija, Exhibit 20, please? I'm sorry to be on a
04:23:39 **5** first-name basis. I never -- I only got the first
04:23:41 **6** name from Mr. Greenwald. I don't mean to be overly
04:23:45 **7** informal. Kaija. I'm wrong completely.
04:23:51 **8 A** **Thank you.**
04:23:53 **9** THE COURT: You want to correct the record on
04:23:54 **10** that?
04:23:55 **11 Q** Yes. I apologize. The correct name is Kaija. And I
04:24:01 **12** do appreciate your assistance. Thank you.
04:24:04 **13** Is Exhibit 20 what we've been referring to as
04:24:08 **14** your fourth affidavit?
04:24:12 **15 A** **Yes, it is.**
04:24:13 **16 Q** And calling your attention to page three, paragraph
04:24:16 **17** six, there is a discussion there. If you could take a
04:24:23 **18** minute and review it.
04:25:07 **19 A** **Yes.**
04:25:07 **20 Q** Does that refresh your recollection about some of the
04:25:10 **21** reasons for the allocation of that transaction?
04:25:12 **22 A** **It does. And it's consistent with my prior testimony,**
04:25:17 **23** **too, I believe.**
04:25:17 **24 Q** Okay. And just to avoid any concern that you haven't
04:25:22 **25** been clear, why is it in summary that OCI chose to

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04:25:26 **1** allocate that particular student policy at the outset
04:25:29 **2** rather than put it into the assessment process?
04:25:32 **3 A** **One, the trust is in a negative asset position, it is**
04:25:40 **4** **utilizing principal to make current interest payments**
04:25:44 **5** **on the securities, and so that there is -- there is a**
04:25:51 **6** **loss pending on that -- on that policy -- or on that**
04:25:55 **7** **security. And in addition there were contractual**
04:26:01 **8** **rights to increase the interest rates at which, you**
04:26:07 **9** **know, funds would be -- and would result in**
04:26:11 **10** **additional funds being drawn from the trust and**
04:26:14 **11** **increase the loss if those rights hadn't been enjoined**
04:26:22 **12** **in as part of the Segregated Account first-day**
04:26:27 **13** **actions.**
04:26:29 **14 Q** And what's the general attitude of the General
04:26:32 **15** exposure or loss and when would that occur?
04:26:35 **16 A** **Well, as of June 30th, 2010, the negative position in**
04:26:44 **17** **the trust was about -- was approximately**
04:26:47 **18** **\$19.8 million, it's expected to increase from there.**
04:26:53 **19** **It's my recollection that the -- there is an option**
04:26:59 **20** **to close the transaction in -- in the year 2013.**
04:27:06 **21 Q** Turning to a different subject, Mr. Owen asked you
04:27:10 **22** some questions about I think some other people, as
04:27:13 **23** well, the adequacy of OCI's oversight of the
04:27:16 **24** Management Service Provider's claim review process.
04:27:20 **25** Do you recall that?

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04:27:21 **1 A Yes.**
04:27:21 **2 Q** Okay. If any claimant like Mr. Owen's client at some
04:27:29 **3** point in the future was dissatisfied with the outcome
04:27:32 **4** of that claim review process, either by the company or
04:27:35 **5** as reviewed by OCI, would they have recourse to go to
04:27:40 **6** another place to have a final decision made?
04:27:44 **7 A The Plan provides that an aggrieved policyholder can**
04:27:50 **8 come to this Court to -- for -- to have their**
04:27:56 **9 concerns heard.**
04:27:57 **10 Q** A third layer of review, if you will?
04:28:00 **11 A Yes. One that doesn't exist in kind of the direct**
04:28:06 **12 course for your average policyholder.**
04:28:11 **13 Q** You're asked some questions about in the ordinary
04:28:15 **14** course the custom and practice with having this kind
04:28:18 **15** of a reviewer process for reinsurers in those
04:28:22 **16** situations. Is there a court you know with
04:28:26 **17** jurisdiction to review decisions?
04:28:29 **18 A Not established in advance, no.**
04:28:34 **19 Q** Okay. And if at any point in the future OCI becomes
04:28:38 **20** dissatisfied with the Management Service Provider's
04:28:41 **21** services, what options does OCI have in regard to
04:28:46 **22** changing vendors?
04:28:48 **23 A OCI's Rehabilitator has retained its right to change**
04:28:54 **24 vendors and has structured the agreement in a way that**
04:28:58 **25 protects information and so forth, so if that**

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04:29:03 **1 contingency is deemed necessary we can effectively**
04:29:07 **2 make that transition.**
04:29:09 **3 Q** Okay. Switching subjects, Mr. Johnson, counsel for
04:29:14 **4** several of the trustee banks, asked you some questions
04:29:18 **5** about the -- his clients' concern about possible
04:29:22 **6** inconvenience in regard to handling the distribution
04:29:28 **7** of notes and the claim process. Do you recall that?
04:29:31 **8 A Yes.**
04:29:31 **9 Q** Yeah. Has OCI directly and through its advisors
04:29:37 **10** endeavored to reach out and confer in advance of
04:29:41 **11** bringing the Plan here about developing a process that
04:29:45 **12** would be workable with these trustees?
04:29:47 **13 A Yes, we have, and I testified to that to some extent**
04:29:51 **14 previously.**
04:29:52 **15 Q** And is that process ongoing and continuing right up to
04:29:56 **16** the present?
04:29:56 **17 A It is.**
04:29:58 **18 Q** And there was a question about whether -- Why don't
04:30:03 **19** you explain the role of DTC first of all, relative to
04:30:07 **20** the trustees in regard to the surplus notes, just
04:30:10 **21** generally?
04:30:10 **22 A Well, the Depository Trust Corporation is a**
04:30:16 **23 recordkeeping entity for the most part in terms of**
04:30:22 **24 tracking securities that are issued in the market and**
04:30:27 **25 we had communications with the DTC early on as we were**

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04:30:34 **1 developing this Plan and, you know, those -- those**
04:30:40 **2 communications involved asking if the DTC would**
04:30:45 **3 distribute those -- all of the surplus notes that**
04:30:52 **4 were to be issued.**
04:30:54 **5 Q** And DTC, did they agree to do so?
04:30:58 **6 A They declined to do so.**
04:30:59 **7 Q** And was that fact communicated to Mr. Johnson, at
04:31:02 **8** least last night?
04:31:03 **9 A Yes, it was.**
04:31:04 **10 Q** Okay. And have these trustees provided OCI with any
04:31:08 **11** specific type of -- of dollar or time estimates about
04:31:13 **12** their alleged inconvenience?
04:31:16 **13 A The only dollar figure that I'm aware of is that**
04:31:23 **14 relates to needing to get certain lists of the**
04:31:27 **15 security's cusip lists they're called, and what could**
04:31:33 **16 be considered normal charge related to that, somewhere**
04:31:36 **17 in \$180.**
04:31:40 **18 THE COURT: What list, cusip?**
04:31:43 **19 THE WITNESS: Cusip is an identifier related to**
04:31:46 **20 a security -- I don't recall the -- what the acronym**
04:31:52 **21 means, but each security that is issued in the market**
04:31:57 **22 has this identifier, this cusip, C-U-S-I-P --**
04:32:02 **23 THE COURT: All right.**
04:32:03 **24 THE WITNESS: -- related to it.**
04:32:05 **25 THE COURT: All right. I follow you.**

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04:32:10 **1 Q** Kaija, Exhibit 41, please.
04:32:32 **2 A I have it.**
04:32:33 **3 Q** Okay. And this is the questions and answers to
04:32:37 **4** objector's questions that OCI put into the record?
04:32:42 **5 A Mm-hmm (Yes).**
04:32:42 **6 Q** And calling your attention to the -- the last
04:32:46 **7** question/answer on page 37.
04:32:50 **8 A All right.**
04:32:58 **9 Q** Is that covering the subject matter of what you were
04:33:04 **10** just describing for these cusip reports?
04:33:07 **11 A It is, yes.**
04:33:09 **12 Q** And the information there is that they cost
04:33:12 **13** approximately \$175 per cusip?
04:33:16 **14 A That's right.**
04:33:16 **15 Q** And that cost at least as estimated here can be
04:33:19 **16** reduced by up to 90 percent through an annual
04:33:23 **17** subscription?
04:33:24 **18 A That's what it says here, yes.**
04:33:26 **19 Q** Yep. And that's your understanding based on --
04:33:28 **20 A That's my understanding.**
04:33:29 **21 Q** Okay. And that's the only specific cost item that has
04:33:33 **22** been brought to OCI's attention that you recall?
04:33:37 **23 A To the best of my knowledge.**
04:33:38 **24 Q** Okay. And at the very end of that paragraph here it
04:33:42 **25** indicates that to the extent this -- this cost

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04:33:47 **1** becomes onerous that the trustees should come to you
04:33:52 **2** and that you'll work fairly with them, is that a fair
04:33:55 **3** reflection of your attitude in regard to this
04:33:57 **4** particular issue?
04:33:58 **5 A That's the intent of the last statement and, yes, we**
04:34:01 **6 have been and are continuing to be willing to work**
04:34:06 **7 with the trustees on the issues.**
04:34:09 **8 Q** Okay. And do you have Exhibit 40 in front of you?
04:34:24 **9 A I do. Just one minute while I find it.**
04:34:57 **10 Q** And I'd like to -- You were asked some questions
04:35:01 **11** yesterday about the recoveries and reimbursement
04:35:04 **12** provisions that start at page four of the exhibit.
04:35:07 **13 A Yes. I have page four up.**
04:35:13 **14 Q** Okay. And in the block -- And these are changes that
04:35:19 **15** were made or amendments to the Disclosure Statement
04:35:22 **16** based on some of the objections that OCI received; is
04:35:26 **17** that correct?
04:35:26 **18 A That's my understanding, yes.**
04:35:27 **19 Q** Okay. And the first paragraph talks about in the
04:35:32 **20** typical type of a transaction that the majority, goes
04:35:37 **21** on and describes it the majority of transactions.
04:35:40 **22** Explain to the Court what's going on in -- in the
04:35:43 **23** typical or majority situation in regard to these
04:35:47 **24** recovery issues?
04:35:49 **25 A Well, it talks about the application of recoveries and**

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04:36:11 **1 that -- that those would be first applied to losses**
04:36:15 **2 in the current period, and it goes on to describe how**
04:36:25 **3 excess cash flows are applied.**
04:36:27 **4** MR. JOHNSON: Your Honor, Michael Johnson on
04:36:30 **5** behalf of Wells Fargo, Bank of America as Trustee,
04:36:33 **6** Wilmington Trust and Trustees. I object to this line
04:36:34 **7** of questioning, I'd move to strike the answer. During
04:36:37 **8** his testimony on cross yesterday Mr. Peterson
04:36:40 **9** yesterday averted that he was not familiar with these
04:36:41 **10** transactions. And it was clear from the answer to
04:36:44 **11** this last question he was simply reading from this
04:36:46 **12** document which is in front of him right now. I
04:36:50 **13** therefore don't think it has been established for this
04:36:53 **14** witness to testify in this that area and I do think
04:36:56 **15** his answer should be stricken from the record.
04:36:58 **16** THE COURT: Mr. Van Sicklen.
04:36:59 **17** MR. VAN SICKLEN: I disagree and I'm trying to
04:37:01 **18** lay some foundation to the very last provision which
04:37:04 **19** Mr. Johnson conveniently left out of his questioning
04:37:07 **20** yesterday.
04:37:07 **21** THE COURT: All right. Overruled the objection.
04:37:10 **22** It's noted.
04:37:10 **23** BY MR. VAN SICKLEN:
04:36:22 **24 Q** Okay. In the next paragraph, Mr. Peterson, talks
04:36:26 **25** about the minority of transactions?

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04:36:26 **1 A Mm-hmm (Yes).**
04:36:28 **2 Q** And that's where there actually is a recovery issue so
04:36:32 **3** you understand it?
04:36:34 **4 A Yes.**
04:36:34 **5 Q** Okay. And then the next page explains some of the
04:36:38 **6** practical problems of addressing Mr. Johnson's concern
04:36:40 **7** in regard to dealing with that minority of
04:36:44 **8** transactions?
04:36:46 **9 A Those are some of the points that were discussed**
04:36:48 **10 previously, yes.**
04:36:50 **11 Q** Okay. And at the very bottom, last paragraph it sets
04:36:56 **12** forth what OCI is prepared to do and what is that, in
04:37:02 **13** the minority of transactions where there are actually
04:37:04 **14** is a problem?
04:37:06 **15 A It -- Perhaps I'll take a moment just to read it,**
04:37:12 **16 but --**
04:37:18 **17** MR. JOHNSON: Your Honor, again I renew my
04:37:18 **18** objection.
04:37:20 **19** THE COURT: If it -- If it states this, isn't
04:37:26 **20** it already in the record?
04:37:28 **21** MR. JOHNSON: Yes. It's clear the document is
04:37:30 **22** in the record, Your Honor.
04:37:32 **23 Q** I'm trying to correct I think the misimpression. I'll
04:37:34 **24** go on. To the extent there are these minor types
04:37:40 **25** of -- or any types of practical problems created by

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04:37:44 **1** the complexity of the nature of the various Ambac
04:37:46 **2** policies, things like the cusip cost we just talked
04:37:50 **3** about or this particular cost, what is OCI's approach
04:37:54 **4** going forward in regard to trying to work with those
04:37:56 **5** policyholders to reach an equitable solution?
04:38:02 **6 A As I've testified to previously, it's OCI's intent to**
04:38:08 **7 try to work out efficient and equitable solutions with**
04:38:14 **8 the trustees as to these administrative procedures**
04:38:18 **9 and -- and costs that maybe incurred.**
04:38:22 **10 Q** And is the alternative resolution mechanism in the
04:38:28 **11** Plan one of the ways in which that can be effected?
04:38:30 **12 A Yes, it is.**
04:38:32 **13 Q** Mr. Greenwald has from the commencement of this
04:38:46 **14** proceeding on introduced his clients or described them
04:38:52 **15** as the RMBS policyholders and he's identified the
04:38:56 **16** entities he represents as Aurelius Capital Management
04:39:02 **17** LP; Fir Tree, Inc.; King Street Capital, LP; King
04:39:06 **18** Street Capital Master Fund Ltd.; Monarch Alternative
04:39:12 **19** Capital, LP, Montana; and Stonehill Capital
04:39:12 **20** Management, LLC. To the best of your knowledge and
04:39:18 **21** diligence over the last two plus years are any of
04:39:20 **22** those policyholders of Ambac?
04:39:24 **23** MR. GREENWALD: Objection, Your Honor. I'd say
04:39:26 **24** it goes beyond the scope of direct -- or the cross.
04:39:28 **25** Excuse me. It's redirect.

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04:39:32 **1** THE COURT: It goes beyond the scope of --

04:39:36 **2** Mr. GREENWALD: I don't believe any questions

04:39:36 **3** were asked on cross with regard to this issue, so it's

04:39:38 **4** beyond the scope of the cross.

04:39:40 **5** THE COURT: I had thought that there were,

04:39:44 **6** whether -- I thought the one issue was whether

04:39:46 **7** they're policyholders or not. I think this would be

04:39:50 **8** relevant. Overruled.

04:39:52 **9** THE WITNESS: To the best of my knowledge there

04:39:54 **10** is no policies that have ever been issued to any of

04:39:56 **11** those parties.

04:39:58 **12** MR. VAN SICKLEN: Okay. And to the best of your

04:40:00 **13** knowledge what is the nature of those entities?

04:40:02 **14** MR. GREENWALD: Objection. Lack of foundation.

04:40:04 **15** THE COURT: Well, do you know?

04:40:06 **16** THE WITNESS: It's my understanding -- Yes, I

04:40:08 **17** do know.

04:40:08 **18** THE COURT: All right. I think he's been

04:40:10 **19** grilled on this so much I would think the foundation

04:40:14 **20** is more than laid. All right. Proceed.

04:40:18 **21** THE WITNESS: It's my understanding that a major

04:40:22 **22** component of the -- the business activities of these

04:40:28 **23** entities is to -- has to do with acquiring distressed

04:40:36 **24** debt and trying -- attempting to maximize its value

04:40:42 **25** through various means, including litigation.

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04:42:14 **1 Q** So you weren't referring to some sort of internal

04:42:18 **2** people employed by the companies?

04:42:20 **3 A No. The firm is an independent certified public**

04:42:26 **4 accountant.**

04:42:32 **5** MR. VAN SICKLEN: That's all I have. Thank you.

04:42:34 **6** THE COURT: All right. That will complete --

04:42:36 **7** I'm not going to go allow any recross. I think these

04:42:40 **8** were questions in clarification and I think we've had

04:42:44 **9** a sufficient examination from the various parties of

04:42:52 **10** this witness. The Court has the discretion and the

04:42:56 **11** authority to direct the manner and method in which

04:43:00 **12** evidence is presented and controlled, exercising that,

04:43:04 **13** you may step down. You'll be excused from this --

04:43:08 **14** from your role here as testifying thus far. I don't

04:43:12 **15** know if anybody is going to recall you or not.

04:43:16 **16** MR. JOHNSON: Your Honor, I'd like just to state

04:43:18 **17** for the record for Your Honor's ruling my clients

04:43:22 **18** would have taken a recross. I'd like a specific

04:43:24 **19** ruling for the record that we will not be allowed

04:43:30 **20** recross.

04:43:30 **21** THE COURT: I just indicated the procedure for

04:43:32 **22** recross and I'm not going to allow any recross at this

04:43:36 **23** point. I think the -- Well, I'm just restating again

04:43:38 **24** what I stated before, which was these questions were

04:43:44 **25** in clarification and I believe exercising my authority

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04:40:44 **1 Q** Now, Mr. Greenwald and others faulted OCI for not

04:40:50 **2** reaching out in advance of the rehabilitation in late

04:40:54 **3** 2009 up to before March 24th of this year, that you

04:41:02 **4** should have reached out and -- and negotiated with

04:41:04 **5** them and alerted them. Is -- Is there any way that

04:41:08 **6** you know of in which you could have before the

04:41:10 **7** Rehabilitation, before Mr. Greenwald made an

04:41:14 **8** appearance here with his client known that they had

04:41:18 **9** any interest whatsoever in the Ambac policies?

04:41:20 **10 A There is no way that I'm aware of that we could have**

04:41:26 **11 had access to that information.**

04:41:28 **12 Q** And is to the best of your knowledge that also true

04:41:30 **13** for Ambac?

04:41:34 **14 A Yes. Any information -- Well, I shouldn't say any,**

04:41:38 **15 but we would have looked first through Ambac to -- to**

04:41:42 **16 get such information.**

04:41:44 **17 Q** And did they reach out at any point that you recall to

04:41:50 **18** OCI to initiate discussions before the rehabilitation

04:41:54 **19** started?

04:41:56 **20 A Not require to the Rehabilitation, no.**

04:41:58 **21 Q** You were asked some questions about the auditors of

04:42:02 **22** AFG and AAC who are at this time and for the last

04:42:06 **23** several years been the auditors of those two

04:42:10 **24** companies?

04:42:10 **25 A The public accounting firm KPMG.**

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04:43:48 **1** in this proceeding that we will proceed without

04:43:52 **2** recross. I don't see that there is a base for it. I

04:43:54 **3** realize you folks can give me a thousand reasons,

04:43:58 **4** you're skilled as to why you might want it do it, but,

04:44:02 **5** no, I will not allow recross.

04:44:04 **6** MR. GREENWALD: Your Honor, with all due

04:44:06 **7** respects, David Greenwald, just to be clear on the

04:44:08 **8** record we object as well to not being allowed to

04:44:12 **9** recross.

04:44:12 **10** THE COURT: And a assume everybody who

04:44:14 **11** questioned before would join in that objection, it

04:44:16 **12** will be noted, you can talk at the next level about

04:44:20 **13** that.

04:44:24 **14** MR. OWEN: Your Honor, it's Jim Owen on behalf

04:44:24 **15** of Lloyds, ALL and bank I would like to also add to

04:44:28 **16** that an objection and an offer of proof that if

04:44:30 **17** allowed to cross-examine the witness would state that

04:44:34 **18** even though it was his intent -- his intent as to

04:44:38 **19** what the reinsurance agreement meant on behalf of the

04:44:40 **20** Rehabilitator that his intent at this stage on behalf

04:44:44 **21** of the Rehabilitator as to what the reinsurance meant

04:44:48 **22** was only his intent, not necessarily speaking for the

04:44:50 **23** Rehabilitator, and not necessarily speaking for what

04:44:52 **24** the Rehabilitator would do for the lifetime of the

04:44:56 **25** agreements and what future Rehabilitators would do

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04:44:58 **1** with respect to those agreements, since they are the
04:45:00 **2** basis for this Court's entire finding as to whether or
04:45:04 **3** not there was adequate surplus and capitalization
04:45:06 **4** under those agreements. He could not speak for what
04:45:10 **5** all future Rehabilitators would do, and I would be
04:45:12 **6** able to elicit -- be able to elicit that testimony and
04:45:16 **7** that is part of my offer of prove that that is only
04:45:18 **8** his current intent and that a current Rehabilitator I
04:45:22 **9** think that the witness would have to testify could not
04:45:24 **10** bind all future Rehabilitators under what he already
04:45:26 **11** testified was a permanent agreement. And also as he
04:45:30 **12** testified that the maturity date of the Lloyds/ALL
04:45:36 **13** bonds were modified, and of course I would be able to
04:45:40 **14** elicit visits testimony from him that that maturity
04:45:42 **15** date could not be modified in those agreements.
04:45:46 **16** There was other testimony I would like to elicit
04:45:48 **17** but I respect the Court's ruling.
04:45:48 **18** THE COURT: Thank you. And you're noted in the
04:45:48 **19** record.
04:45:50 **20** MR. GREENWALD: Your Honor, if I could David
04:45:56 **21** Greenwald, just to make a quick offer of prove with
04:45:58 **22** regard to the matters that I would have covered in
04:46:00 **23** recross. I do believe that the testimony that Mr.
04:46:02 **24** Peterson just gave on redirect regarding my clients is
04:46:04 **25** beyond the scope of the direct -- the

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04:46:06 **1** cross-examination, and I would have elicited from Mr.
04:46:10 **2** Peterson that the positions that we've taken in this
04:46:12 **3** proceeding on behalf of our clients were for the
04:46:14 **4** benefit of all RMBS policyholders, and that there was
04:46:20 **5** no inconsistency in regard to that.
04:46:20 **6** In addition to that, although Mr. Peterson
04:46:24 **7** testified that no attempt could have been made to
04:46:24 **8** reach out to the specific RMBS policyholders, Mr.
04:46:28 **9** Peterson testified that he had not attempted -- OCI
04:46:32 **10** had not attempted to reach out to any of the trustees
04:46:34 **11** who were policyholders or holding policyholder
04:46:40 **12** benefits for their investors, and therefore the
04:46:44 **13** evidence would have shown, if I had been allowed to
04:46:46 **14** present recross-examination, that no attempt was made
04:46:50 **15** to reach out to the RMBS policyholders prior to the
04:46:54 **16** filing of this proceeding in March.
04:46:56 **17** THE COURT: All right. That is also on the
04:46:58 **18** record. You may step down.
04:47:00 **19** THE WITNESS: Thank you, Your Honor.
04:47:00 **20** (Witness excused at 1:45 p.m.)
04:47:04 **21** THE COURT: All right. Call your next witness.
04:47:06 **22** MR. VAN SICKLEN: Your Honor, I'm passing the
04:47:08 **23** mike to partner to Mr. Simmons.
04:47:10 **24** THE COURT: Mr. --
04:47:12 **25** MR. SIMMONS: Simmons. Good afternoon. We'll

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04:47:16 **1** be calling David Barranco, Your Honor.
04:47:18 **2** THE COURT: Sir, would you come up.
04:47:20 **3** MR. PETERSON: Your Honor, should these
04:47:22 **4** documents go back to you?
04:47:24 **5** THE COURT: Do you have any other exhibits?
04:47:26 **6** MR. PETERSON: These things weren't marked as
04:47:28 **7** exhibit.
04:47:28 **8** THE COURT: Who handed them to you?
04:47:50 **9** MR. PETERSON: I don't recall.
04:47:50 **10** THE COURT: Hand them back to Mr. Van Sicklen.
04:47:50 **11** Sir, come around here to the witness chair, raise your
04:47:54 **12** hand and receive the witness oath, please.
04:47:54 **13** **DAVID BARRANCO**
04:47:54 **14** was duly sworn by the Clerk and was examined and
04:48:00 **15** testified as follows:
04:48:00 **16** THE COURT: All right. Be seated. Please start
04:48:04 **17** by stating your name.
04:48:06 **18** THE WITNESS: It's David Barranco.
04:48:10 **19** THE COURT: Mr. Barranco, you've been present
04:48:14 **20** and -- I think you've been present, you heard some of
04:48:16 **21** the instructions we gave regarding procedure, which is
04:48:20 **22** that when you're answering a question, please wait
04:48:24 **23** until it's fully asked and whoever's asking the
04:48:28 **24** question will wait until it's fully answered so the
04:48:30 **25** reporter can take down without problems what is being

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04:48:34 **1** said.
04:48:34 **2** THE WITNESS: I understand, Your Honor.
04:48:36 **3** THE COURT: All right. Proceed.
04:48:36 **4** **DIRECT EXAMINATION**
04:48:36 **5** **BY MR. SIMMONS:**
04:48:40 **6 Q** Who is your employer Mr. Barranco?
04:48:40 **7 A** My employer is Ambac Assurance Corporation.
04:48:44 **8 Q** And can you describe for the Court what your
04:48:46 **9** responsibilities are at Ambac?
04:48:48 **10 A** Yes. I am a managing director in the Portfolio Risk
04:48:52 **11** Management Group at Ambac. I'm responsible for
04:48:54 **12** restructurings and commutations primarily as they
04:48:58 **13** relate to Segregated Account policies, specifically
04:49:02 **14** students loans and RMBS. I also have responsibility
04:49:04 **15** for the surveillance areas of the following product
04:49:08 **16** areas: CDOs or collateralized debt obligations,
04:49:12 **17** student loans and structured insurance.
04:49:14 **18 Q** Okay. And you describe yourself as a managing
04:49:16 **19** director. Can you tell the Court what a managing
04:49:18 **20** director is?
04:49:20 **21 A** Well, I would describe myself really as a senior line
04:49:24 **22** manager of the company of Ambac Assurance Corporation.
04:49:28 **23 Q** Are you part of the -- Are you an executive officer of
04:49:32 **24** the company?
04:49:32 **25 A** No I would describe myself as really kind of the next

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04:49:36 **1** level down from, you know, what I would call the CEO,
04:49:40 **2** the CFO and the general counsel, I would be the next
04:49:44 **3** layer down. I report to the CEO.
04:49:46 **4** **Q** Can you just describe for the Court briefly your
04:49:48 **5** history with Ambac?
04:49:50 **6** **A** Sure. I've been with Ambac for over 11 years. I
04:49:52 **7** started in 1999 as an analyst covering a lot of
04:49:58 **8** international transactions -- international
04:50:02 **9** structured transactions. After a spell I ended up
04:50:06 **10** heading up our surveillance area for credit products,
04:50:08 **11** our structured credit products, which included a lot
04:50:12 **12** of collateralized debt obligations or those are
04:50:16 **13** structures that are backed by corporate bonds and
04:50:20 **14** corporate loans. I did that through about 2004 and
04:50:22 **15** then in the beginning of 2005 I moved to our UK office
04:50:26 **16** to work for an Ambac UK, where I underwrote
04:50:30 **17** international and structured finance transactions.
04:50:32 **18** And in the beginning of 2008 or probably around
04:50:36 **19** March of 2008 I was asked to come back to New York to
04:50:40 **20** help out with really the growing problem with the
04:50:42 **21** mortgage-related assets and my initial
04:50:46 **22** responsibilities were to -- to analyze, develop
04:50:50 **23** remediation plans and commutation plans for the
04:50:54 **24** \$30 billion or so of ABS CDOs. I also at the same
04:51:00 **25** time had some responsibilities in our mortgage-backed

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04:51:02 **1** surveillance group.
04:51:06 **2** **Q** How many employees does Ambac have right now?
04:51:10 **3** **A** Roughly 250.
04:51:10 **4** **Q** Can you just briefly describe for the Court kind of
04:51:14 **5** the general structure of Ambac?
04:51:14 **6** **A** Sure. You know, I would describe the area that I work
04:51:18 **7** in, in the Portfolio Control Risk Management Group is
04:51:22 **8** roughly about 85 employees. That's kind of the
04:51:24 **9** operational core of the company right now. And then
04:51:28 **10** there is a finance area which probably has an equal
04:51:30 **11** number of people, I would include I guess some of the
04:51:34 **12** treasury folks in that area. We also have a
04:51:36 **13** technology department, and we have -- in managing the
04:51:42 **14** assets we have an investment portfolio group, capital
04:51:46 **15** markets group, there's probably about 20 -- 20 or so
04:51:50 **16** people in that group, as well as we have an
04:51:52 **17** administrative function and then the executive office.
04:51:54 **18** **Q** Is there a separate structure set up to deal with the
04:51:58 **19** Segregated Account?
04:51:58 **20** **A** Yes, there is.
04:51:58 **21** **Q** Can you describe that briefly?
04:52:00 **22** **A** We are -- I am one of the part of the leadership team
04:52:04 **23** for the Management Services Provider to the Segregated
04:52:08 **24** Account, and so we have organized ourselves really to
04:52:12 **25** support the policies that have been allocated to the

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04:52:16 **1** Segregated Account. And there we have, you know,
04:52:20 **2** three -- three individuals that kind of represent the
04:52:22 **3** management team for -- for the Management Services
04:52:24 **4** Provider.
04:52:24 **5** **Q** And who are those three people?
04:52:26 **6** **A** It will be myself, a fellow by the name of Ian Bruce,
04:52:30 **7** who is also in the Portfolio Risk Management
04:52:34 **8** Department, specifically responsible for RMBS, and
04:52:38 **9** then a fellow by the name of Steve Ksenak, who is
04:52:42 **10** internal counsel.
04:52:42 **11** THE COURT: Just a moment. Do you need those
04:52:44 **12** names spelled?
04:52:44 **13** THE WITNESS: Yeah, I could, so Bruce -- Ian
04:52:50 **14** Bruce, I-A-I-N, Bruce -- Surname is Bruce B-R-U-C-E,
04:52:52 **15** and then Steve Ksenak, K-S-E-N-A-K.
04:53:02 **16** **Q** And do you know how long Mr. Bruce and Mr. Ksenak have
04:53:06 **17** been with the company?
04:53:08 **18** **A** Let's see here. Mr. Bruce has been with the company
04:53:10 **19** for I'd say about 15 years or so. And Mr. Ksenak
04:53:16 **20** probably about the same amount of time, maybe slightly
04:53:18 **21** less than I have, maybe nine or ten years.
04:53:20 **22** **Q** Are there additional employees who are devoted to the
04:53:24 **23** Segregated Account in addition to those three?
04:53:26 **24** **A** Yes. Directly I would call the analytical
04:53:28 **25** responsibilities in Portfolio Risk Management we have

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04:53:32 **1** 20 -- about -- actually about 30 direct employees
04:53:36 **2** between Ian Bruce and myself and we're supported more
04:53:42 **3** broadly by operational resources, you know, throughout
04:53:44 **4** the company.
04:53:46 **5** **Q** And you said you're part of the leadership team,
04:53:48 **6** correct?
04:53:50 **7** **A** That's correct.
04:53:50 **8** **Q** Did that leadership team meet with OCI
04:53:54 **9** representatives?
04:53:54 **10** **A** Yes, we do.
04:53:54 **11** **Q** How often do you do that?
04:53:56 **12** **A** We meet once a week every Wednesday at 10 a.m.
04:54:00 **13** **Q** And who do you meet with?
04:54:00 **14** **A** We meet with Deputy Commissioner Shaul, Mr. Peterson,
04:54:04 **15** and Kevin Fitzgerald from Foley & Lardner.
04:54:10 **16** **Q** About how long do those meetings last?
04:54:12 **17** **A** Typically they last an hour.
04:54:14 **18** **Q** Who sets the agenda for the meetings?
04:54:16 **19** **A** The company sets the agenda for the meetings.
04:54:18 **20** **Q** How do you determine what gets on the agenda?
04:54:22 **21** **A** We essentially try to cover all of the major policy
04:54:24 **22** areas within the Segregated Accounts or whether
04:54:26 **23** that's, you know, activities going on with RMBS,
04:54:30 **24** student loans, swap sureties, the mono rail, et
04:54:34 **25** cetera, so we try to make sure that we cover the gamut

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04:54:38 **1** of the credit specific issues, that being the policies
04:54:40 **2** as well as any sort of administrative issues that come
04:54:44 **3** up or any other topics that are relevant.
04:54:46 **4** **Q** And what's your understanding of the purpose of those
04:54:48 **5** meetings?
04:54:50 **6** **A** That is really a management meeting to make sure --
04:54:54 **7** We use it a lot to make sure that, you know, decisions
04:54:58 **8** that have been made are, you know, what's the process
04:55:00 **9** there, you know, how far along are we with different
04:55:04 **10** activities. It's kind of a clearinghouse for a lot of
04:55:06 **11** the operational activities that occur through our --
04:55:12 **12** actually through our credit risk management functions.
04:55:14 **13** **Q** Just to give the Court a little better understanding
04:55:16 **14** of what the committee does at these meetings, can you
04:55:20 **15** will just cite some examples of recent issues that you
04:55:22 **16** brought to the attention of OCI at the meetings?
04:55:26 **17** **A** Okay. Sure. On the RMBS side, that would be a
04:55:28 **18** subject, we -- you know, some of the things that have
04:55:32 **19** been more active recently, we were going through a
04:55:34 **20** process of some servicer transfers and so it would
04:55:38 **21** really be, you know, to update, you know, folks from
04:55:40 **22** OCI on what the status of those is, and see what any
04:55:44 **23** particular issues have come up since they've given
04:55:48 **24** their approval or what have you. Also maybe an update
04:55:50 **25** on litigation strategies with RMBS. There could be,

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04:55:54 **1** you know, student loans, there is maybe some ongoing
04:55:56 **2** commutations discussions where we are in those
04:56:00 **3** discussions and so on and so forth.
04:56:02 **4** **Q** At these meetings are you looking to OCI to provide
04:56:06 **5** guidance or what are you looking for in terms of
04:56:08 **6** feedback from OCI at these meetings?
04:56:12 **7** **A** We want to make sure we're on the same page with OCI
04:56:14 **8** and we've often, you know, in other forums we've
04:56:18 **9** brought the proposal to them, given them the analysis
04:56:20 **10** and asked for their input and it's just a forum to
04:56:24 **11** make sure things are going according to plan, that
04:56:28 **12** they've giving us any sort of feedback from their
04:56:30 **13** perspective, any sort of additional steps that need to
04:56:32 **14** be made in terms of ongoing -- ongoing projects.
04:56:34 **15** **Q** And are there any plans to stop having these plans if
04:56:38 **16** the Plan of Rehabilitation is approved?
04:56:42 **17** **A** No.
04:56:42 **18** **Q** Are there other avenues for OCI to participate in
04:56:46 **19** Ambac decision making?
04:56:48 **20** **A** Yes.
04:56:48 **21** **Q** Can you describe some of those for the Court?
04:56:52 **22** **A** The primary I would call it the operational day-to-day
04:56:54 **23** meeting, the policy level meetings, so if there was
04:56:58 **24** any issue with particular policies, part of our
04:57:00 **25** central risk management function, and that would go

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04:57:04 **1** for, you know, both General Account and Segregated
04:57:06 **2** Account activities. Normally that's kind of the
04:57:08 **3** clearinghouse for internal proposals, recommendations,
04:57:10 **4** whether it's something as straightforward as a change
04:57:14 **5** in the internal classification or rating of a
04:57:18 **6** particular policy or maybe initial proposal on a
04:57:20 **7** specific remediation plan for a policy or a
04:57:24 **8** commutation plan, and so that's the forum where we
04:57:28 **9** meet with our senior internal credit risk management
04:57:32 **10** folks. And then there is, you know, OCI is made aware
04:57:36 **11** of what the agenda is for the week, which meetings are
04:57:40 **12** happening, and ones that is specific -- you know, for
04:57:42 **13** them to attend. They're open to all of these
04:57:46 **14** meetings, but ones that they need to attend, you know,
04:57:48 **15** they deal with Segregated Account issues or something
04:57:54 **16** that they need to consider and sign off on, that's a
04:57:56 **17** forum to do that. So they would have their advisors
04:57:58 **18** -- OCI would be there, they would listen to the
04:58:00 **19** analysis, listen to the proposals, listen to the
04:58:04 **20** discuss and take it away and think about it if it's
04:58:08 **21** something to sign off on.
04:58:08 **22** **Q** And who is in charge of that committee from the Ambac
04:58:12 **23** side?
04:58:12 **24** **A** The head of that committee is Cathy Matanle is the
04:58:14 **25** head of the credit risk management function.

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04:58:18 **1** THE COURT: Can you spell that name?
04:58:18 **2** THE WITNESS: Yes. Cathy Matanle,
04:58:20 **3** M-A-T-A-N-L-E.
04:58:24 **4** THE COURT: Might I suggest you slow down a
04:58:26 **5** little bit in your delivery.
04:58:26 **6** THE WITNESS: Yes.
04:58:26 **7** THE COURT: You're quite rapid.
04:58:28 **8** THE WITNESS: Okay.
04:58:30 **9** THE COURT: I want Mr. Greenwald to be able to
04:58:32 **10** take good notes. It looks like he's straining right
04:58:36 **11** now.
04:58:36 **12** THE WITNESS: I'll try to slow down. So Ms.
04:58:38 **13** Matanle is the head of that function, although the
04:58:40 **14** day-to-day credit risk -- head credit risk management
04:58:46 **15** person is a fellow by the name of Peter Cain, C-A-I-N.
04:58:52 **16** **Q** And how long has Mr. Cain run that committee?
04:58:54 **17** **A** Mr. Cain -- in its current iteration for probably two
04:58:58 **18** or three years, but Mr. Cain has, you know, been with
04:59:02 **19** Ambac for a number of years and has a lot of -- a very
04:59:08 **20** long credit background, you know, over 20 years.
04:59:12 **21** **Q** I'd like to change topics now and move to the student
04:59:14 **22** loan assessment process. Were you involved in
04:59:18 **23** assessing the student loans that were ultimately
04:59:20 **24** allocated to the Segregated Account?
04:59:22 **25** **A** Yes, I was.

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04:59:24 **1 Q** Can you describe that involvement?

04:59:26 **2 A** **Sure. The Student Loan Risk Management Group or**

04:59:28 **3 surveillance group reports to me and I was involved**

04:59:32 **4 with that student loan assessment process. And, you**

04:59:38 **5 know, really what we had was about \$11 billion net par**

04:59:42 **6 of student loan policies across maybe 20 transactions**

04:59:46 **7 and 125, 130 or so policies. And what we endeavored**

05:00:04 **8 to do per the -- you know, per the assignment was**

05:00:08 **9 really to analyze and -- and provide for the OCI**

05:00:14 **10 the -- the development of projected losses and kind**

05:00:20 **11 of the key risk points in these policies. And what it**

05:00:24 **12 broke down to is really kind of three -- three groups**

05:00:28 **13 of -- of -- three different main types of risks, I**

05:00:30 **14 should say.**

05:00:32 **15 Q** Why don't you describe those three risk for the Court.

05:00:34 **16 A** **Sure. The first group was kind of a simple analysis**

05:00:38 **17 really. For all those transactions that had fewer**

05:00:42 **18 assets than insured liabilities, meaning that, you**

05:00:46 **19 know, if you liquidate the deal today you would have a**

05:00:50 **20 claim, because there weren't enough assets to pay your**

05:00:52 **21 liabilities. Those were -- That was the first**

05:00:54 **22 bright-line test for transactions that we recommended**

05:00:58 **23 be allocated to the Segregated Account.**

05:01:02 **24** The second class of transactions -- This would

05:01:06 **25** be broadly, you know, almost the bulk of a lot of the

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05:01:10 **1** transactions, there -- A lot of these student loan

05:01:14 **2** transactions had what we call broken liability

05:01:18 **3** structures. They were originally set up with auction

05:01:22 **4** rate securities where they're -- these securities

05:01:26 **5** would reset every week, every month at very, very low

05:01:30 **6** rates. There is another product variable rate demand

05:01:32 **7** obligations, similar concept, where every week, every

05:01:36 **8** month, you know, the auction market would -- would --

05:01:40 **9** the liability structures would be reset at a new low

05:01:46 **10** interest rate.

05:01:46 **11** With the dislocation of the capital markets in

05:01:48 **12** 2008 these transactions effectively broke, these

05:01:56 **13** auctions won't occur anymore. And what happens is

05:01:58 **14** they default at a penalty rate, and that penalty rate

05:02:00 **15** is often a multiple of what the -- you know, the

05:02:06 **16** normal functioning credit market's rate would have

05:02:08 **17** been. And so what happens with these transactions is

05:02:12 **18** they have a high liability cost, so the interest is

05:02:16 **19** pretty high, but on the asset side the underlying

05:02:20 **20** student loans are still generating the same interest

05:02:22 **21** rate. And so what's happening is as interest and

05:02:26 **22** principal proceeds are generated from the underlying

05:02:30 **23** student loans, they're -- both interest and principal

05:02:32 **24** is used to pay -- to pay current interest on the

05:02:36 **25** bonds, and these are very elongated liabilities. If

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05:02:40 **1** you stretch that math out for a long time, what you

05:02:44 **2** have over time is your assets deplete and your

05:02:46 **3** liabilities don't, and so at the end of the -- end of

05:02:50 **4** the road you run into the same situation where you

05:02:54 **5** have fewer assets and liabilities, implying a loss.

05:02:56 **6 Q** And that's the second category?

05:02:58 **7 A** **That's the second category. That's really the broad**

05:03:02 **8 category for a lot of these transactions.**

05:03:04 **9 Q** What's the third category?

05:03:04 **10 A** **The third category to the extent you didn't have an**

05:03:08 **11 auction rate or a VRDO problem, there is a fair amount**

05:03:14 **12 of private student loan transactions and these would**

05:03:18 **13 contrast with transactions that had government**

05:03:22 **14 guaranties on the underlying student loans. And these**

05:03:26 **15 transactions have performed much worse than the**

05:03:28 **16 underwritten expectations. And so they're much more**

05:03:32 **17 volatile and over time we expect that these**

05:03:34 **18 transactions will also incur losses.**

05:03:38 **19 Q** And there was a limited number of policies that were

05:03:40 **20** allocated to the Segregated Account on March 24th; is

05:03:44 **21** that right?

05:03:44 **22 A** **That's correct.**

05:03:44 **23 Q** Why were those policies allocated at that time?

05:03:48 **24 A** **We had one transaction that was very clearly in the**

05:03:54 **25 negative par -- you know, where assets were fewer**

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05:03:58 **1** than liabilities and so that transaction was allocated

05:04:02 **2** early days. In addition, there were a number of

05:04:04 **3** student loan policies written on CDS or written with a

05:04:12 **4** credit default swap rather than directly with

05:04:16 **5** financial guarantee. Those transactions, because of

05:04:20 **6** the mark-to-market problem that we had -- people

05:04:22 **7** prior to me have testified about were also allocated

05:04:26 **8** to the Segregated Account.

05:04:28 **9 Q** Is that sort of a different category than the three

05:04:30 **10** you mentioned earlier?

05:04:30 **11 A** **Yes. That's a different category.**

05:04:32 **12 Q** Does that fully describe the policies that were

05:04:34 **13** allocated on March 24th, what you just described?

05:04:38 **14 A** **Yes. Yes. Yes. That would describe the ones that**

05:04:40 **15 were allocated March 24th.**

05:04:42 **16 Q** So the bulk of the policies were allocated after

05:04:46 **17** March 24th, is that correct?

05:04:48 **18 A** **That's correct. 11 billion or so of net par were**

05:04:50 **19 allocated after March 24th.**

05:04:52 **20 Q** And why was there that delay in allocating those

05:04:56 **21** policies to the Segregated Account?

05:04:58 **22 A** **Really kind in the built up of the creation of the**

05:05:00 **23 Segregated Account, the rehab -- the subsequent rehab**

05:05:02 **24 proceedings, a lot of focus on obviously the most**

05:05:06 **25 troubled area of the company, the ABS CDOs, the RMBS**

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05:05:14 **1** and there is a view that OCI wanted some additional
05:05:16 **2** time to think about understand the projected loss
05:05:20 **3** build upon generally on the student loan transactions,
05:05:22 **4** so that's what the delay for. They certainly saw,
05:05:24 **5** recognized the problem, it was just a -- allowed them
05:05:30 **6** some time to really kind of further, you know, help,
05:05:32 **7** you know, develop the losses on those transactions,
05:05:36 **8** articulate those losses and have them understand those
05:05:38 **9** losses.
05:05:38 **10** **Q** And how many meetings and conversations would you
05:05:42 **11** estimate you had with OCI and its advisors during that
05:05:44 **12** time period to discuss what policies should be
05:05:48 **13** allocated to the Segregated Account?
05:05:50 **14** **A** We had number, so this is, you know, basically, you
05:05:52 **15** know, four or five-month period. We had a number of
05:05:56 **16** in-person, you know, visits with OCI and their
05:06:00 **17** advisors on site and even perhaps even more on, you
05:06:04 **18** know, via the telephone.
05:06:06 **19** **Q** Just a fairly deliberative process?
05:06:08 **20** **A** Yeah. Fairly deliberative process.
05:06:14 **21** THE COURT: Could you pull your mike up a little
05:06:16 **22** closer.
05:06:16 **23** THE WITNESS: Sure. Is it not --
05:06:18 **24** THE COURT: You're soft spoken. I'm not sure if
05:06:22 **25** everybody is hearing.

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05:06:22 **1** THE WITNESS: All right.
05:06:22 **2** BY MR. SIMMONS:
05:06:24 **3** **Q** I'd like to change subjects now. I think you
05:06:26 **4** mentioned earlier one of your responsibilities is with
05:06:28 **5** respect to commutations; is that right?
05:06:30 **6** **A** That's correct.
05:06:30 **7** **Q** Okay. Can you just generally describe what Ambac's
05:06:34 **8** approaches when it's thinking about commuting a
05:06:36 **9** policy?
05:06:38 **10** **A** Sure. You know, we've been commuting policies really
05:06:40 **11** since about 2008, and normally these transactions, the
05:06:46 **12** way we pay under our policy is, you know, current
05:06:50 **13** interest and ultimate principal as claims are
05:06:52 **14** incurred, over -- You know, over this period of time,
05:06:56 **15** you know, folks, bondholders that have policies have
05:07:00 **16** come to us and said, gee, you know, we'd like to exit
05:07:04 **17** this relationship with your company. And what we're
05:07:08 **18** happy to think about that to the extent it makes
05:07:12 **19** sense, you know, so we have a capital base that we're
05:07:14 **20** growing at X-percent per year to pay those claims over
05:07:18 **21** time. So in order for us to think about agreeing to
05:07:22 **22** pay someone money to tear up their policy, we like to
05:07:26 **23** think about what's the appropriate return on capital.
05:07:30 **24** So simply, we're looking at the projected cash
05:07:34 **25** flow payments over time and discounting those at a

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05:07:36 **1** rate that makes sense to us, the optimum rate to
05:07:40 **2** achieve relief of reserves and something that works
05:07:44 **3** out to a bilateral negotiation.
05:07:48 **4** **Q** How has the existence of the --
05:07:50 **5** THE COURT: Just a moment. State your name,
05:07:52 **6** please.
05:07:52 **7** MR. WHITMER: Steven Whitmer. I just wanted to
05:07:54 **8** point out the witness's chair is about to fall off.
05:07:58 **9** One of his four wheels --
05:08:00 **10** THE WITNESS: All right.
05:08:00 **11** MR. WHITMER: Thank you.
05:08:02 **12** THE WITNESS: Thank you. I'll roll off the back
05:08:08 **13** here.
05:08:10 **14** THE COURT: I was worried about his speech not
05:08:12 **15** about his chair. It --
05:08:18 **16** MR. BENTLEY: We were hoping that the witness
05:08:18 **17** had adequate insurance if he fell.
05:08:18 **18** BY MR. SIMMONS:
05:08:24 **19** **Q** Mr. Barranco, has the existence of the Plan of
05:08:28 **20** Rehabilitation affected your approach to commutation
05:08:32 **21** at all?
05:08:32 **22** **A** It's simply made it a bit more complex. We have the
05:08:34 **23** same reserves, we also have a -- a payment plan which
05:08:38 **24** is proposed under the -- under the -- under the Plan,
05:08:42 **25** and so we just have to consider, you know, the element

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05:08:46 **1** of surplus notes and factor that into our discount
05:08:50 **2** rates and how we -- but again we're trying to -- to
05:08:54 **3** maximize the return on our capital against any
05:08:58 **4** particular reserve.
05:09:02 **5** **Q** You were here yesterday for -- There was some
05:09:04 **6** questioning regarding the bank group and the bank
05:09:08 **7** settlement. You were here for that testimony
05:09:10 **8** yesterday?
05:09:10 **9** **A** Yes, I was.
05:09:10 **10** **Q** And I think there was some questioning directed at
05:09:14 **11** whether CDS banks actually held the underlying
05:09:18 **12** securities for the CDS transactions at issue. Do you
05:09:22 **13** recall that discussion generally?
05:09:24 **14** **A** Yes.
05:09:24 **15** **Q** Do you have an understanding as to whether the banks
05:09:26 **16** involved in the bank deal actually held the securities
05:09:28 **17** for those transactions?
05:09:30 **18** **A** Yeah. It's my view that they did.
05:09:34 **19** **Q** And why is that your view?
05:09:36 **20** MR. BENTLEY: Your Honor -- Your Honor, before
05:09:38 **21** the witness launches into a response, can I ask that
05:09:42 **22** he lay some foundation for having personal knowledge
05:09:44 **23** of this issue.
05:09:46 **24** **Q** That was my next question, Your Honor. Why did he
05:09:50 **25** have that view -- How is it that you have that view?

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05:09:52 **1 A** My main job from 2008 until the culmination of the
05:09:56 **2** bank deal in 2010 was to interact with these banks and
05:10:00 **3** try to develop analysis on what we thought about these
05:10:02 **4** risks these ABS CDO risks and to negotiate
05:10:08 **5** commutations or restructuring plans. A lot of my
05:10:12 **6** background is a lot of interaction with all of these
05:10:14 **7** banks that were involved in the bank settlement
05:10:18 **8** agreement as well as other banks that weren't part of
05:10:20 **9** that bank settlement agreement.
05:10:22 **10** So I think the reason why would say they did hold
05:10:30 **11** these positions is in our contracts -- in our CDS
05:10:34 **12** contracts or credit derivative contracts, what the
05:10:38 **13** deal was, what the contract said was that the
05:10:44 **14** counterpart, the folks on the other side of the
05:10:48 **15** contract, had to take our direction with respect to
05:10:50 **16** controlling bondholder decisions, and these were all
05:10:56 **17** transactions where we wrote the CDS against the senior
05:11:02 **18** most tranche of debt, the controlling creditor class.
05:11:08 **19** And the consequences of not being able to follow
05:11:12 **20** our instructions was the contract would terminate what
05:11:14 **21** they call flat, so no one would owe each other any
05:11:18 **22** money. And, you know, these were huge positions, they
05:11:22 **23** were, you know, deeply distressed and so there was,
05:11:26 **24** you know, our view was there is no way a bank would --
05:11:30 **25** you know, would want to risk not being able to follow

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05:11:34 **1** our instruction.
05:11:36 **2** And indeed over -- over the two -- two or so
05:11:40 **3** years -- two or more years that I was looking at
05:11:42 **4** these transactions we did have several directing votes
05:11:46 **5** where we had to instruct the counterparty to vote, to
05:11:50 **6** do certain things, you know, things like accelerate
05:11:54 **7** the transactions to make sure we cutoff interest from
05:11:58 **8** junior classes when necessary, to instruct the removal
05:12:02 **9** of one collateral manager in the implementation of
05:12:06 **10** another collateral manager.
05:12:08 **11** In order for that to happen, you know, the trustee
05:12:10 **12** would take instruction from the -- you know, the
05:12:14 **13** registered holder of that -- of that senior note and
05:12:18 **14** so that's -- that's -- you know, that was something
05:12:22 **15** that was very important to us in terms of our overall
05:12:26 **16** feel of that control rights and that's how -- and we
05:12:30 **17** were successful and that happened. Every time we
05:12:32 **18** instructed our counterparty to do something, they did
05:12:36 **19** it and we were able to, you know, move collateral
05:12:38 **20** managers, accelerate deals, et cetera.
05:12:42 **21 Q** Just to be clear you're saying you instructed the
05:12:44 **22** banks to vote a certain way?
05:12:46 **23 A** Exactly.
05:12:46 **24 Q** And the only way they could vote a certain way is if
05:12:50 **25** they actually held the underlying securities; is that

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05:12:52 **1** right?
05:12:52 **2 A** Right. They would have to represent to the trustee
05:12:54 **3** that they were the controlling bondholder, that they
05:12:56 **4** could direct the trustee to do -- remove the
05:13:02 **5** collateral manager to accelerate the waterfall, that
05:13:04 **6** kind of thing.
05:13:06 **7 Q** And in your experience that's exactly what they did,
05:13:08 **8** they did vote the way you directed them to; is that
05:13:12 **9** correct?
05:13:12 **10 A** Yes. That's correct.
05:13:12 **11 Q** Do you know if any CES banks suffered any economic
05:13:18 **12** losses?
05:13:18 **13 A** Economic losses in the terms of -- You know, the
05:13:20 **14** worst deals had already started to incur interest
05:13:24 **15** shortfalls, so interest shortfalls were submitted to
05:13:26 **16** us and we paid those -- those claims, and then really
05:13:30 **17** the -- you know, the bulk of the loss if you look at
05:13:34 **18** our -- Ambac's impairments at the time, even more so
05:13:38 **19** or even greater so than the MBS is ABS CDO
05:13:44 **20** impairments, and those were the, you know, projected
05:13:46 **21** interest shortfalls which would happen for many, many
05:13:48 **22** years and then, you know, followed by a big principal
05:13:52 **23** payment in the year 2025 and so on.
05:14:00 **24 Q** No further questions -- One second, Your Honor.
05:14:20 **25** After the bank settlement was enter into, Mr.

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05:14:22 **1** Barranco, did you see any evidence that the banks were
05:14:24 **2** selling their positions?
05:14:26 **3 A** Yes. Shortly after the bank settlement a lot of the
05:14:30 **4** larger transactions started to liquidate. I mean,
05:14:36 **5** what these banks most wanted to do was to liquidate
05:14:40 **6** these transactions and -- and get to the underlying
05:14:44 **7** assets. The -- The ABS CDO in terms of the value of
05:14:50 **8** that position was much -- actually lower than the
05:14:54 **9** actual intrinsic value of the underlying assets.
05:14:58 **10 Q** And what is the fact that you saw the banks were
05:15:04 **11** liquidating -- selling their positions, what did that
05:15:06 **12** indicate regarding their holding of securities?
05:15:10 **13 A** Basically once --
05:15:10 **14** MR. BENTLEY: Objection, Your Honor. It's
05:15:14 **15** unclear whether the witness is about to be
05:15:18 **16** speculating, and it sound like he's being asked to
05:15:20 **17** speculate.
05:15:22 **18** THE COURT: So that's a preemptive objection?
05:15:26 **19** Mr. BENTLEY: It's an objection to the question
05:15:28 **20** before the witness answers it, that is, that the
05:15:30 **21** question calls for speculation and there is no
05:15:32 **22** foundation.
05:15:32 **23** Mr. SIMMONS: I'm asking what it indicates to
05:15:34 **24** him, Your Honor. What it indicates --
05:15:36 **25** THE COURT: Just a moment. Overrule the

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05:15:38 **1** objection. I think he can answer what -- what the
05:15:42 **2** indication was to him, and then on cross you can cover
05:15:46 **3** whether or not that was speculation on his part.
05:15:50 **4** THE WITNESS: What it tells me is the banks got
05:15:52 **5** their control rights back after our contracts were
05:15:54 **6** torn up and went ahead and went forward with a
05:15:58 **7** liquidation of these transactions.
05:16:02 **8** MR. SIMMONS: No further questions, Your Honor.
05:16:02 **9** THE COURT: Does Ambac have any questions?
05:16:04 **10** MR. STOLPER: No, Your Honor.
05:16:08 **11** THE COURT: All right. Let's take Mr.
05:16:12 **12** Greenwald. Are you leading the --
05:16:14 **13** MR. GREENWALD: I'm taking point once again.
05:16:16 **14** Yes, Your Honor.
05:16:16 **15** CROSS-EXAMINATION
05:16:16 **16** BY MR. GREENWALD:
05:16:18 **17** **Q** Just a few questions, good afternoon Mr. Barranco.
05:16:22 **18** **A** Good afternoon.
05:16:24 **19** **Q** Now, Mr. Barranco, you are an employee of AAC; is that
05:16:26 **20** correct?
05:16:26 **21** **A** That's correct.
05:16:26 **22** **Q** And who do you report to?
05:16:28 **23** **A** I report to David Wallis.
05:16:32 **24** **Q** And what is Mr. Wallis' at AAC?
05:16:34 **25** **A** He is the CEO of AAC.

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05:16:38 **1** **Q** And what is Mr. Wallis of AFF?
05:16:40 **2** **A** AFG? He's the CEO of AFG.
05:16:44 **3** **Q** And who are the executive officers of AAC?
05:16:48 **4** **A** David Trick is the CSO, Kevin Doyle is the general
05:16:54 **5** counsel, Robert Eisman is the chief accounting
05:16:58 **6** officer, and Diana Adams is the chief administrative
05:17:06 **7** officer.
05:17:10 **8** **Q** That's Mr. Trick, Mr. Doyle, Ms. Eisman -- Mr. Eisman,
05:17:14 **9** and Ms. Adams; is that correct?
05:17:16 **10** **A** Yes.
05:17:18 **11** **Q** And are those four executive officer of AAC also
05:17:22 **12** executive officers of AAC?
05:17:24 **13** MR. SIMMONS: Object to foundation, Your Honor.
05:17:26 **14** THE COURT: Well, I think he would know.
05:17:28 **15** THE WITNESS: I believe they are.
05:17:30 **16** **Q** Are there any doubts in your mind that the executive
05:17:34 **17** officers of AAC are identical to the executive
05:17:38 **18** officers of AFG?
05:17:38 **19** **A** No.
05:17:42 **20** **Q** Does the Dewey firm act as counsel to AAC?
05:17:46 **21** **A** Yes.
05:17:46 **22** **Q** And does the Dewey firm act as counsel to AFG?
05:17:54 **23** MR. SIMMONS: Object to foundation, Your Honor,
05:17:56 **24** relevance.
05:17:56 **25** THE COURT: Do you know?

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05:17:58 **1** THE WITNESS: I do know they do some work for
05:18:02 **2** the whole-co (phonetic) as well.
05:18:02 **3** THE COURT: You don't know if they are counsel
05:18:06 **4** for them?
05:18:06 **5** THE WITNESS: I am aware that they are counsel
05:18:06 **6** for Whole-co as well.
05:18:06 **7** THE COURT: All right. Proceed.
05:18:12 **8** **Q** All right. And just to clarify Whole-co means AFG?
05:18:12 **9** **A** Yes. AFG.
05:18:14 **10** **Q** Mr. Barranco, would you agree that -- Strike that.
05:18:22 **11** One moment, Your Honor. Yes. Mr. Barranco, prior to
05:18:56 **12** the filing of the Rehabilitation in March of 2010, did
05:19:02 **13** AAC reach out to Fannie Mae with regard to attempting
05:19:08 **14** to resolve the RMBS exposures?
05:19:12 **15** **A** Ambac -- Fannie Mae reached out to Ambac I believe in
05:19:18 **16** the summer of 2009.
05:19:22 **17** **Q** Was that with regard to the RMBS?
05:19:26 **18** **A** That was with regard to RMBS potential commutations.
05:19:30 **19** **Q** And did Freddie Mac reach out to -- Strike that. Did
05:19:34 **20** Ambac reach out to Freddie Mac with regard to its RMBS
05:19:40 **21** exposure prior for March of 2010?
05:19:42 **22** **A** I'm not sure who called who first. I -- But, yes, we
05:19:46 **23** were in contact with Freddie Mac before March 24th,
05:19:52 **24** 2010.
05:19:52 **25** **Q** Did -- I'm wanting to go to your testimony regarding

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05:19:56 **1** your -- I want to go directly to what you said. I
05:20:00 **2** believe your testimony was that in your role of
05:20:08 **3** reviewing commutations your job is to maximize the
05:20:12 **4** return on capital for any reserves that Ambac holds,
05:20:16 **5** correct?
05:20:16 **6** **A** That's correct.
05:20:18 **7** **Q** And you take into account what the discount factor is
05:20:24 **8** for yo ru internal reserves?
05:20:26 **9** **A** Yeah. Our reserves are -- reflect a discount rate.
05:20:30 **10** **Q** So are your reserves -- Are you saying that they're
05:20:34 **11** present valued?
05:20:34 **12** **A** Yes. All -- Yes. Our reserves are present valued.
05:20:38 **13** **Q** And what discount rate do you use to present value
05:20:42 **14** your reserves internally?
05:20:44 **15** **A** On a statutory basis it's at 5.1 percent I believe in
05:20:48 **16** the most recent quarter.
05:20:50 **17** **Q** Is there any other basis that you use?
05:20:52 **18** **A** Yes. GAAP. And for GAAP it's at a range of different
05:20:58 **19** discount rates depending upon the weighted average
05:21:02 **20** life of a particular transactions. Typically it's a
05:21:06 **21** risk-free rate.
05:21:06 **22** **Q** And what's the range of the risk-free rate?
05:21:10 **23** **A** I'm not sure. It would generally reflect a forward
05:21:14 **24** curve.
05:21:14 **25** **Q** And does the curve -- What is the risk-free curve

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05:21:18 **1** that it tracks? Is there an index? Is it treasuries?

05:21:26 **2** What's the --

05:21:26 **3** MR. SIMMONS: Your Honor, what's the relevance

05:21:28 **4** of this?

05:21:28 **5** THE COURT: What would be the relevance?

05:21:32 **6** MR. GREENWALD: Your Honor, he said -- With

05:21:34 **7** regard to commutations, it's important to Mr. Barranco

05:21:36 **8** that he maximizes his returns on his reserves. I'd

05:21:40 **9** like to know how that compares to the 5.1 percent in

05:21:44 **10** surplus notes as well as the overall return that

05:21:50 **11** people are getting or the policyholders are getting in

05:21:52 **12** their commutations.

05:21:54 **13** THE COURT: All right. I sustained the

05:21:54 **14** objection but will allow you to go forward and ask the

05:21:58 **15** direct question.

05:22:00 **16 Q** Okay. Let me ask you the direct question. What's the

05:22:04 **17** high-end rate that's applied to GAAP accounting to

05:22:06 **18** your knowledge.

05:22:08 **19 A I'm not sure.**

05:22:26 **20 Q** Mr. Barranco, when you testified that you spoke to

05:22:30 **21** Fannie Mae and Freddie Mac prior to March 24th, did

05:22:34 **22** you inform them that Ambac was considering forming a

05:22:40 **23** Segregated Account?

05:22:40 **24 A To be clear, in the summer of 2009 discussions with**

05:22:46 **25 Fannie Mae and Freddie Mac, I was actually not at**

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05:22:50 **1 those meetings.**

05:22:50 **2 Q** Do you know whether Ambac ever communicated to Fannie

05:22:54 **3** Mae prior to March 24th of its intention to form a

05:22:58 **4** Segregated Account?

05:22:58 **5 A I don't know.**

05:23:00 **6 Q** Do you know whether Ambac ever informed Freddie Mac

05:23:08 **7** prior to March 24th of its intention to form a

05:23:10 **8** Segregated Account?

05:23:10 **9 A I don't know.**

05:23:12 **10 Q** Mr. Barranco, do you have any discussions at Ambac

05:23:36 **11** regarding its long-term plans for potentially writing

05:23:42 **12** new business in the future?

05:23:44 **13 A I have not.**

05:23:44 **14 Q** Would that generally fall within your area of business

05:23:48 **15** duties?

05:23:50 **16 A No, it would not.**

05:23:50 **17 Q** Okay. Is it -- Does that fall within Ms. Matanle's

05:23:56 **18** duties?

05:23:56 **19 A Most likely not. I mean, we are both in the portfolio**

05:24:00 **20 risk management area, we've got \$350 billion worth of**

05:24:04 **21 exposure that we're trying to run down.**

05:24:10 **22 Q** At the end of the day if you successfully run off your

05:24:16 **23** reserves and there is a remainder -- Strike that.

05:24:22 **24** Part of your job is to reach settlements with

05:24:26 **25** policyholders and not run those off to the end of the

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05:24:28 **1** exposure; is that correct?

05:24:30 **2 A That's correct.**

05:24:30 **3 Q** And when you do that there is a compromise on the

05:24:36 **4** claim so that you're actually getting a positive

05:24:40 **5** return to your reserves, correct?

05:24:42 **6 A Yes.**

05:24:44 **7 Q** If at the time end of the day through commutations and

05:24:48 **8** otherwise you successfully run off your reserves and

05:24:50 **9** there is a remainder, who -- for who is benefit will

05:24:56 **10** that remainder go?

05:24:58 **11** MR. SIMMONS: Objection, calls for speculation,

05:25:00 **12** foundation.

05:25:00 **13** THE COURT: Sustained.

05:25:02 **14 Q** Your job, Mr. Barranco, is to maximize the benefit for

05:25:06 **15** AAC; is that correct?

05:25:08 **16 A Yes. For all the stakeholders of AAC.**

05:25:12 **17 Q** And one of the stakeholders is the shareholder of AAC?

05:25:16 **18 A Yes.**

05:25:16 **19 Q** And that would be AFG, correct?

05:25:20 **20 A Yes.**

05:25:22 **21** MR. GREENWALD: No further questions, Your

05:25:22 **22** Honor, and I'm going to cede point to somebody else.

05:25:28 **23** THE COURT: Mr. Bentley, are you up?

05:25:30 **24** MR. BENTLEY: Your Honor, I'm content to let

05:25:32 **25** others go first.

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05:25:34 **1** THE COURT: I'm looking forward to hearing from

05:25:36 **2** you again. Mr. Welsh.

05:25:38 **3** MR. WELSH: Thank you, Your Honor, I appreciate

05:25:40 **4** it.

05:25:40 **5** MR. BENTLEY: I would wear my cheesehead if I

05:25:42 **6** could.

05:25:52 **7** THE COURT: See Mr. Welsh, size does matter.

05:25:56 **8** MR. WELSH: It's all the cheese.

05:26:02 **9** **CROSS-EXAMINATION**

05:26:02 **10** **BY MR. WELSH:**

05:26:02 **11 Q** Mr. Barranco, my name is Tom Welsh and I represent

05:26:04 **12** Depfa, which is among other things a bondholder under

05:26:08 **13** several of the student loan deals that Ambac insured.

05:26:12 **14** Are you familiar with Depfa and its holdings?

05:26:16 **15 A Yes. Generally.**

05:26:16 **16 Q** All right. I just have a couple of quick questions.

05:26:24 **17** Let me start with the commutation process. OCI is

05:26:32 **18** involved in supervision and management of that

05:26:36 **19** process, correct?

05:26:36 **20 A That's correct.**

05:26:38 **21 Q** All right. So they're familiar with and supportive of

05:26:48 **22** Ambac's objectives, it's core objective of maximizing

05:26:52 **23** return on capital? As to any reserves that are

05:26:56 **24** commuted --

05:26:58 **25** Mr. SIMMONS: Objection foundation as to what's

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05:27:00 **1** in OCI's mind.

05:27:02 **2** THE COURT: All right. I'll sustain that

05:27:04 **3** objection, ask that you lay the foundation for that.

05:27:06 **4** MR. Welsh: Is OCI aware of Ambac's objective of

05:27:12 **5** maximizing return on capital for any reserves as a

05:27:16 **6** result of commutations?

05:27:18 **7** THE WITNESS: I believe they are.

05:27:22 **8 Q** Is it your understanding that they are also supportive

05:27:24 **9** of your pursuit of that objective?

05:27:26 **10 A** **Within their -- within their guidelines, within their**

05:27:30 **11** **stated objectives.**

05:27:32 **12 Q** Is -- Is it fair to refer to that -- or to summarize

05:27:38 **13** that objective as essentially seeking to maximize the

05:27:44 **14** profit of Ambac as a result of a commutation?

05:27:50 **15 A** **Are you asking me to answer what the OCI's objective**

05:27:54 **16** **is?**

05:27:56 **17 Q** Yours or Ambac's.

05:27:58 **18 A** **Our objective is to maximize the -- the capital**

05:28:04 **19** **that's left at AAC to, you know, pay policy claims and**

05:28:08 **20** **surplus notes.**

05:28:10 **21 Q** But what I'm trying to get at is the notion of

05:28:14 **22** maximizing the return on capital, that isn't just a

05:28:22 **23** process of essentially providing the policyholder with

05:28:30 **24** the value attributable to the reserves that you've

05:28:34 **25** posted on account of the policy, correct?

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05:28:36 **1 A** **Right. I mean I think the proposition as I explained**

05:28:40 **2** **before, you know, a lot of these policies pay out over**

05:28:42 **3** **time, so someone might get paid claims, you know,**

05:28:46 **4** **interest shortfalls, you know, smaller amounts over**

05:28:48 **5** **time and then be owed a principal bullet or principal**

05:28:54 **6** **claim, you know, 20 years from now. And that's the**

05:28:58 **7** **normal course. And in order for us to make sure that**

05:29:00 **8** **we are -- you know, maximizing that pot of capital,**

05:29:06 **9** **that's growing at, you know, whatever 5.1 percent in**

05:29:10 **10** **order to pay all claims you have to use that as a**

05:29:14 **11** **hurdle, right.**

05:29:14 **12** **So if I'm saving up money to pay that 2020 claim,**

05:29:18 **13** **I'm going to want to -- you know, the only way I'm**

05:29:22 **14** **going to settle that is for a discount in order to**

05:29:24 **15** **make sure I have, you know, the capital now to grow to**

05:29:28 **16** **satisfy other claims.**

05:29:28 **17 Q** You want to strike the best deal for Ambac?

05:29:32 **18 A** **I want to strike the best deal for AAC.**

05:29:34 **19 Q** Right. Not necessarily the best deal for your

05:29:38 **20** policyholder but the best deal for Ambac?

05:29:40 **21 A** **I want to strike the best deal to maximize, you know,**

05:29:44 **22** **the pot of capital we have.**

05:29:46 **23 Q** And OCI in its capacity as both your regulator and the

05:29:56 **24** Rehabilitator is allowing you to pursue that strategy,

05:30:04 **25** correct?

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05:30:06 **1 A** **Within -- Within their guidelines.**

05:30:12 **2 Q** Let me go back. You said that you worked at Ambac UK

05:30:16 **3** for a period of time?

05:30:16 **4 A** **That's correct.**

05:30:18 **5 Q** Were you also involved in the session in the

05:30:22 **6** reinsurance agreement between Ambac UK and Ambac the

05:30:26 **7** negotiation of that?

05:30:28 **8 A** **To be clear are you referring to the commutation?**

05:30:30 **9 Q** No. Actually the original 1997 agreement under which

05:30:36 **10** liabilities were transferred?

05:30:38 **11 A** **No, I was not.**

05:30:40 **12 Q** Okay. Were you involved in the commutation?

05:30:42 **13 A** **No.**

05:30:42 **14 Q** Who was?

05:30:48 **15 A** **From Ambac Steve Ksenak, and various other -- I'm not**

05:30:56 **16** **sure exactly who besides Steve was involved.**

05:31:00 **17 Q** Well, do you have any information other than

05:31:02 **18** information that came from Mr. Ksenak about what

05:31:08 **19** originally precipitate that commutation?

05:31:12 **20 A** **Only from what I've read, you know, in various dis --**

05:31:14 **21** **you know, various disclosures we've had in our 10Q's**

05:31:18 **22** **and et cetera.**

05:31:20 **23 Q** Okay. Let me turn quickly to the student loan

05:31:28 **24** allocation process. You mentioned that one of the

05:31:32 **25** three groups of student loans that were allocated to

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05:31:36 **1** the Segregated Account were those that involve broken

05:31:40 **2** liability structures and failed auctions, right?

05:31:42 **3 A** **That's correct.**

05:31:42 **4 Q** Okay. Isn't it true that in many respects those

05:31:48 **5** auctions were failing because of the Ambac rap on

05:31:54 **6** those deals?

05:31:54 **7 A** **Not entirely, no.**

05:31:56 **8 Q** But the presence of Ambac insurance was in fact a

05:32:02 **9** significant factor in many of the failed actions?

05:32:04 **10 A** **It was a factor in some, yes.**

05:32:10 **11 Q** And did you have a period of time where you were

05:32:12 **12** allowing policyholders -- student loan policyholders

05:32:16 **13** are any other kind of policyholders to suspend their

05:32:18 **14** -- voluntarily suspend their coverage?

05:32:22 **15 A** **I'm not sure I follow your question.**

05:32:24 **16 Q** Well, let me -- I've seen a -- an I'll represent to

05:32:30 **17** you that I've seen a letter from Ambac to the

05:32:32 **18** California Department of Insurance in which Ambac asks

05:32:36 **19** for approval of an endorsement to policy forums that

05:32:42 **20** allows policyholders who were suffering as a result of

05:32:46 **21** failed auctions to suspend their coverage, they stop

05:32:50 **22** paying premium and if a loss occurs during suspension

05:32:54 **23** they can't make a claim under the policy, and the --

05:32:58 **24** if they haven't reactivated coverage within two years,

05:33:04 **25** the policy terminates. is that an endorsement that

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05:33:08 **1** you're familiar with?

05:33:08 **2 A I'm not familiar with that letter.**

05:33:10 **3 Q** When you got into specific student loan deals that

05:33:22 **4** were allocated you mentioned the one deal was clearly

05:33:26 **5** upside down and in an asset deficit position. Which

05:33:30 **6** deal was that?

05:33:30 **7 A That was the ALL transaction.**

05:33:42 **8 Q** While you were discussing the allocation of other

05:33:48 **9** policies to the Segregated Account, other student loan

05:33:50 **10** policies with the OCI, did you make disclosure to the

05:33:58 **11** OCI as to the identity of -- of the bondholders to

05:34:02 **12** the extent you knew it?

05:34:04 **13 A To the extent we knew it, yes.**

05:34:12 **14 Q** So, for example, during these discussions it would

05:34:16 **15** have been on the table as to whether that particular

05:34:22 **16** deal was a Depfa deal or some other bondholder's deal?

05:34:26 **17 A Just for all what we would call the bank bond deals**

05:34:30 **18 like all the BRDO bonds where it was clear who the**

05:34:34 **19 bonds were put back to, that back yes OCI would be**

05:34:40 **20 aware and approve those who those bank bondholders**

05:34:44 **21 were.**

05:34:44 **22 Q** And was there any attempt to reach out to those bank

05:34:48 **23** bond holders prior to or as part of that allocation

05:34:54 **24** process?

05:34:56 **25** MR. SIMMONS: Object vague as to time, Your

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05:36:08 **1** process include attempts to reach out to the affected

05:36:14 **2** bondholders and bring them into the assessment of

05:36:18 **3** whether they should be allocated to the Segregated

05:36:22 **4** Account or left in the General Account?

05:36:24 **5 A No.**

05:36:26 **6 Q** Why?

05:36:28 **7 A From our perspective we went through an analytical**

05:36:34 **8 exercise, assessed the risk of the transactions. I --**

05:36:38 **9 I'm not -- not sure what -- what additional**

05:36:48 **10 information would be provided by the bondholders we --**

05:36:58 **11 The answer is we didn't -- we didn't reach out, we**

05:37:02 **12 had a process for analyzing these transactions.**

05:37:06 **13 Q** Did the process also consider whether allocation to

05:37:16 **14** the Segregated Account would in fact enhance Ambac's

05:37:20 **15** ability to pursue it's goal of maximizing its return

05:37:24 **16** on capital in the event of a commutation?

05:37:28 **17 A No. I think the -- you know, the clear item is that**

05:37:34 **18 deals that are in the General Account or the**

05:37:36 **19 Segregated Account still have the same capital, they**

05:37:40 **20 still have the same reserve capital against them.**

05:37:44 **21 Q** But you do recognize that if a policyholder remained

05:37:48 **22** in the General Account and suffered a loss, they would

05:37:50 **23** be paid a hundred cents on the dollar on that loss in

05:37:54 **24** cash, correct?

05:37:54 **25 A Yes.**

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05:35:00 **1** Honor.

05:35:00 **2** THE COURT: Yeah.

05:35:02 **3 Q** Do you understand the allocation process that you were

05:35:04 **4** testifying about is that process that occurred after

05:35:08 **5** March 24th when you were deciding to move -- or not

05:35:14 **6** move I think it was exhibit -- there was -- there

05:35:20 **7** was a list attached --

05:35:22 **8 A Right.**

05:35:24 **9 Q** -- to the verified petition. That's -- Do you

05:35:26 **10** understand that's the specific allocation process that

05:35:30 **11** I'm talking about?

05:35:30 **12 A And your question is with respect to that allocation**

05:35:34 **13 process?**

05:35:34 **14 Q** Let me reask the question. I'm sorry. I'm talking

05:35:36 **15** about the allocation process that started after the

05:35:40 **16** Segregated Account was created and put into

05:35:42 **17** Rehabilitation and more specifically there was a group

05:35:48 **18** of student loan deals that were being assessed as to

05:35:54 **19** whether they will stay in the General Account or move

05:35:56 **20** to the Segregated Account. Do you understand that?

05:35:58 **21 A Yes.**

05:35:58 **22 Q** Okay. And you were personally involved in that

05:36:00 **23** process?

05:36:02 **24 A Yes.**

05:36:02 **25 Q** Okay. During that process -- Strike that. Did that

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05:37:56 **1 Q** And so you would have -- policyholders who are moved

05:38:02 **2** into the Segregated Account will only receive

05:38:06 **3** 25 percent of their claim in cash and 75 percent in a

05:38:10 **4** deferred surplus note, correct?

05:38:10 **5 A That's correct.**

05:38:12 **6 Q** So clearly a policyholder of Ambac would prefer to be

05:38:18 **7** in and remain in the General Account, correct?

05:38:22 **8** MR. SIMMONS: Objection. Calls for speculation.

05:38:26 **9** THE WITNESS: I don't know.

05:38:28 **10 Q** Have you ever been approached by any policyholder

05:38:32 **11** asking to be moved to the Segregated Account?

05:38:34 **12 A Not recently.**

05:38:36 **13 Q** Not recently. Have you ever?

05:38:36 **14 A No.**

05:38:38 **15 Q** And, in fact, you never would be?

05:38:40 **16** MR. SIMMONS: Your Honor, argumentative. Where

05:38:42 **17** we going with this? This is closing argument.

05:38:44 **18** THE COURT: It is argument. Let's just move on.

05:38:46 **19** I think that's a given right there.

05:38:50 **20** MR. WELSH: Thank you, Your Honor. I agree.

05:38:54 **21** And what I'm getting at is -- is allocation to the

05:38:58 **22** Segregated Account actually creates leverage for Ambac

05:39:02 **23** as it pursues commutation, that's simply -- I'd like

05:39:06 **24** an acknowledgment of that.

05:39:08 **25** MR. SIMMONS: Objection, argumentative, Your

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05:39:12 **1** Honor.

05:39:12 **2** THE COURT: It is -- It is argument, if you're

05:39:16 **3** drawing a conclusion there.

05:39:18 **4** MR. Welsh: No, Your Honor, I'm simply asking

05:39:22 **5** Ambac to recognize the fact that there is a difference

05:39:26 **6** between negotiating a commutation with someone who is

05:39:30 **7** going to get a hundred cents on the dollar if they get

05:39:32 **8** a loss and negotiating a commutation with someone who

05:39:36 **9** is only going to get 25 percent in cash and 75 percent

05:39:38 **10** in a surplus note.

05:39:40 **11** MR. SIMMONS: Your Honor, he can argue this in

05:39:42 **12** closing arguments.

05:39:44 **13** THE COURT: That's correct. Let's move on.

05:39:44 **14** That is argument.

05:39:46 **15** MR. Welsh: May I ask one last question with

05:39:48 **16** respect to just to clarify whether that was -- that

05:39:52 **17** is part of the consideration that went into allocating

05:39:56 **18** policies into the Segregated Account.

05:39:58 **19** MR. SIMMONS: Object as vague and argumentative,

05:40:00 **20** Your Honor.

05:40:00 **21** THE COURT: What consideration, what do you

05:40:02 **22** mean?

05:40:04 **23** MR. Welsh: Well, we started the line of

05:40:06 **24** question -- the lining of questioning talking about

05:40:08 **25** the allocation process, that OCI and Ambac were

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05:40:14 **1** working on to determine which of their -- anywhere

05:40:18 **2** from 13 to 15,000 policyholders were going to end up

05:40:20 **3** in the disadvantaged bucket of the Segregated Account,

05:40:24 **4** and I simply would like to establish for the record

05:40:30 **5** that part of that allocation process when coupled with

05:40:34 **6** the fact that Ambac is pursuing commutations that will

05:40:38 **7** terminate the policies on terms favorable to Ambac,

05:40:42 **8** that there was a recognition of the fact that they

05:40:46 **9** have an easier time negotiating with people who had

05:40:48 **10** been put into the Segregated Account. That's simply

05:40:52 **11** -- That's really my simple question.

05:40:54 **12** THE COURT: That's basically an argument. Let's

05:40:56 **13** move on to a fact-type question from this witness.

05:41:02 **14** What does he know, when did he know it, so forth.

05:41:20 **15 Q** I left my reading glasses. Give me just one second.

05:41:52 **16** Jumping back to the commutation question, you were

05:41:54 **17** asked about the impact of the Rehabilitation of the

05:41:58 **18** Segregated Account on your process of entering into

05:42:02 **19** commutations, and as I recall you testified that the

05:42:06 **20** Rehabilitation actually made commutation processes

05:42:10 **21** more complex; is that correct?

05:42:12 **22 A** **Yes. I mean, simply the mechanics of those cash flows**

05:42:16 **23** **if you think about simply here's a projection of cash**

05:42:20 **24** **flows over time, you think about cash out the door,**

05:42:24 **25** **you think about the issuance of surplus notes, you**

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05:42:26 **1** **think about the carrying costs on those surplus notes**

05:42:30 **2** **and at 5.1 percent annually it just makes a -- for a**

05:42:34 **3** **more complicated analysis when you're trying to figure**

05:42:36 **4** **out what is the PV pick up for us, you know, what are**

05:42:40 **5** **we measuring against?**

05:42:42 **6 Q** And when you say PV pick up, you mean the present

05:42:44 **7** value --

05:42:46 **8 A** **Yes. I'm sorry. The present value, yes. Simply --**

05:42:48 **9 Q** What do you mine by PV pickup?

05:42:52 **10 A** **All right. So we would -- if -- Thinking about it**

05:42:54 **11** **from almost like a treasury function, we'd say, okay,**

05:43:00 **12** **we have bond X. Bond X has a projected stream of**

05:43:04 **13** **claim payments over the next 10, 20 years, whatever it**

05:43:08 **14** **may be, what is -- what is the cash that we would**

05:43:12 **15** **expect to pay under the Plan, you know, 25 cents, what**

05:43:16 **16** **is the surplus notes, the amount of surplus notes**

05:43:18 **17** **issued, what is their carry cost because they -- we**

05:43:22 **18** **have to, you know, pay interest on those and factoring**

05:43:26 **19** **all those numbers into what's the cost for us versus**

05:43:30 **20** **what would we be willing to -- you know, to try to**

05:43:34 **21** **commute, what would be we be willing to pay now today**

05:43:40 **22** **in order to diffuse the projected cash flow stream**

05:43:44 **23** **over time.**

05:44:00 **24** MR. Welsh: That's all I have your. Thanks very

05:44:02 **25** much.

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05:44:02 **1** THE COURT: All right. This will be an

05:44:04 **2** appropriate time to take the afternoon recess. We'll

05:44:06 **3** be in recess until 3:00. And you may step down, sir.

05:44:10 **4** THE WITNESS: Thank you.

05:54:16 **5** (Recess taken from 2:52 p.m. until 3:00 p.m.)

06:01:52 **6** THE COURT: All right. Be seated. All right.

06:01:58 **7** Who is up next for the objectors? Objectors must be

06:02:10 **8** going boy height.

06:02:10 **9** **CROSS-EXAMINATION**

06:02:10 **10** **BY MR. JOHNSON:**

06:02:16 **11 Q** We're saving the best for last, Your Honor. Michael

06:02:20 **12** Johnson. I represent the Bank of America, Wells Fargo

06:02:22 **13** and Wilmington Trust Trustees in this action. Mr.

06:02:28 **14** Barranco, were you involved in any communications with

06:02:34 **15** DTC concerning the Plan of Rehabilitation?

06:02:38 **16 A** **No, I was not.**

06:02:38 **17 Q** Are you familiar with communications that Ambac had

06:02:42 **18** with DTC concerning the Plan of Rehabilitation?

06:02:44 **19 A** **No.**

06:02:46 **20 Q** Do you know if Ms. Matanle was involved in

06:02:48 **21** communications with DTC concerning the Plan of

06:02:52 **22** Rehabilitation?

06:02:52 **23 A** **I'm not sure.**

06:03:00 **24** MR. JOHNSON: Thank you.

06:03:00 **25** THE COURT: All right. Who's up next?

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06:03:00 **1** **CROSS-EXAMINATION**

06:03:00 **2** **BY MR. DEVORE:**

06:03:14 **3 Q** Good afternoon, sir. Andrew Devore for One State

06:03:16 **4** Street?

06:03:16 **5 A** **Good afternoon.**

06:03:18 **6 Q** What is your business address?

06:03:20 **7 A** **One State Street Plaza.**

06:03:22 **8 Q** Okay.

06:03:24 **9 A** **New York, New York.**

06:03:24 **10 Q** Now, that's the property that's one leased from One

06:03:28 **11** State Street LLC; is that correct?

06:03:28 **12 A** **That's correct.**

06:03:30 **13 Q** Now, are you aware that the November rent has not been

06:03:32 **14** paid?

06:03:32 **15 A** **That's what I've read.**

06:03:34 **16 Q** Okay. Now, are you an employee of the Segregated

06:03:38 **17** Account?

06:03:38 **18 A** **I'm an employee of Ambac Assurance Corporation.**

06:03:40 **19 Q** Okay. Would it be a correct characterization to say

06:03:48 **20** that you are effectively an employee of the General

06:03:52 **21** Account?

06:03:52 **22 A** **I am -- Yes. That's correct.**

06:03:56 **23 Q** Are there any employees of the Segregated Account

06:03:58 **24** working out of the One State Street building?

06:04:00 **25 A** **Not to my knowledge.**

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06:04:02 **1 Q** Okay. And how many employees of the General Account

06:04:06 **2** work out of the One State Street building?

06:04:10 **3 A** **Approximately 250.**

06:04:12 **4 Q** Could you give the Court just an idea of the layout of

06:04:20 **5** the building, how many floors, how much space is

06:04:22 **6** occupied?

06:04:22 **7** MR. SIMMONS: Object relevance, Your Honor.

06:04:24 **8** THE COURT: Why would I need to know that.

06:04:28 **9** MR. DEVORE: I was just putting it in context.

06:04:30 **10** THE COURT: If you have a card or brochure and

06:04:34 **11** want to move it, we can do that but I don't think I

06:04:36 **12** need to need the layout.

06:04:38 **13** MR. DEVORE: I'm just trying to establish the

06:04:40 **14** magnitude of the space that's occupied by the General

06:04:44 **15** Account.

06:04:44 **16** THE COURT: I don't know how that would be

06:04:46 **17** relevant. I just don't.

06:04:46 **18 Q** Okay. I can move on. Now, do you know how the

06:04:50 **19** decision was made to allocate the contingent liability

06:04:54 **20** that's been referred to under the lease to the

06:04:56 **21** Segregated Account?

06:04:58 **22 A** **Only from -- from what I've read in the Disclosure**

06:05:02 **23** **Statement.**

06:05:02 **24 Q** Okay. You were not involved in that decision?

06:05:04 **25 A** **I was not.**

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06:05:04 **1 Q** Now, does the General Account have other trade vendors

06:05:10 **2** like equipment lessors?

06:05:12 **3 A** **Yes.**

06:05:14 **4 Q** Okay. Electric bills?

06:05:16 **5 A** **As far as I know.**

06:05:18 **6 Q** Are any of those liabilities allocated to the

06:05:20 **7** Segregated Account?

06:05:22 **8 A** **Not to my knowledge.**

06:05:24 **9 Q** And is the General Account paying those liabilities?

06:05:28 **10 A** **I believe so.**

06:05:34 **11** MR. DEVORE: That's all I have, Your Honor.

06:05:36 **12** THE COURT: Thank you. Who is up next?

06:05:36 **13** **CROSS-EXAMINATION**

06:05:36 **14** **BY MR. WHITMER:**

06:06:04 **15 Q** Good afternoon, Mr. Barranco. My name is Steven

06:06:08 **16** Whitmer, and I represent Wells Fargo as trustee for

06:06:10 **17** the LVM bondholders.

06:06:14 **18 A** **Good afternoon.**

06:06:14 **19 Q** Sir, you've been here in the courtroom when there has

06:06:20 **20** been a lot of discussion about the four sets of

06:06:22 **21** projections that have been presented to the Court in

06:06:26 **22** support of the Rehabilitation Plan, right?

06:06:28 **23 A** **Yes.**

06:06:28 **24 Q** Did you have any role at all with respect to those

06:06:32 **25** projections?

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06:06:34 **1 A** **To the creation of those projections?**

06:06:36 **2 Q** Any role whatsoever with respect to those projections?

06:06:40 **3 A** **No.**

06:06:42 **4 Q** Had you reviewed those projections at any time prior

06:06:46 **5** to today?

06:06:48 **6 A** **Yes.**

06:06:48 **7 Q** When was the first time you reviewed them?

06:06:50 **8 A** **When the Disclosure Statement was first submitted.**

06:06:56 **9 Q** And did AAC conduct its own set of projections with

06:07:06 **10** respect to the same subject matter covered by the OCI

06:07:10 **11** projections?

06:07:10 **12 A** **No more than, you know, our current, you know,**

06:07:18 **13** **reserves and financial information has disclosed in**

06:07:22 **14** **10Q.**

06:07:22 **15 Q** Let me be more specific then. With respect to, for

06:07:26 **16** example, the loss development in the Segregated

06:07:32 **17** Account, you've heard the testimony, you've seen the

06:07:36 **18** projections that were prepared by OCI with respect to

06:07:38 **19** that issue, right?

06:07:40 **20 A** **Yes.**

06:07:40 **21 Q** Did AAC prepare its own separate set of analyses with

06:07:46 **22** respect to that same issue?

06:07:48 **23 A** **Not with respect to that same issue. AAC normally**

06:07:54 **24** **course develops its own GAAP reserves, stat reserves**

06:07:58 **25** **and projections such as that but not to -- nothing**

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06:08:02 **1** **akin to what is in the Disclosure Statement.**

06:08:08 **2 Q** Well, one of the things that AAC I assume has done

06:08:14 **3** you'll tell us over the last six months perhaps is try

06:08:16 **4** to get a sense of what loss development will be with

06:08:22 **5** respect to the Segregated Account policies?

06:08:26 **6 A** **I think again it's very clear that is our -- it's in**

06:08:30 **7** **our financial statements, those are our reserves and**

06:08:32 **8** **you can look at our statutory statements they would**

06:08:34 **9** **have the buildup to our reserves, that would be our**

06:08:38 **10** **view on projected losses.**

06:08:40 **11 Q** And that's something that AAC updates on a regular

06:08:44 **12** basis?

06:08:44 **13 A** **Updates every quarter.**

06:08:46 **14 Q** You heard the testimony that Mr. Peterson provided

06:08:50 **15** earlier today about different Moody's scenarios that

06:08:54 **16** OCI used with respect to its modeling, right?

06:09:00 **17 A** **Yes.**

06:09:00 **18 Q** Does AAC also use Moody's with respect to its model?

06:09:04 **19 A** **What modeling in particular? Can you be more**

06:09:10 **20** **specific?**

06:09:10 **21 Q** Sure. I'm talking about specifically with respect to

06:09:12 **22** loss development as it pertains to the General or

06:09:16 **23** Segregated Account.

06:09:16 **24 A** **There is some incorporation of -- of Moody's analysis**

06:09:24 **25** **in the loss development in certain asset classes.**

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06:09:28 **1 Q** Could you explain that to us?

06:09:30 **2 A** **Yeah. More specifically in terms of RMBS, things like**

06:09:36 **3** **Moodys.com financial scenarios are considered in the**

06:09:40 **4** **credit model that is used to develop projected losses**

06:09:46 **5** **or reserves for certain RMBS policies.**

06:09:52 **6 Q** Now, you've testified today about your involvement

06:09:56 **7** with respect to reserves at AAC in different facets,

06:10:02 **8** correct?

06:10:02 **9 A** **Yes.**

06:10:02 **10 Q** Would it be fair to say that you have -- Reserves at

06:10:08 **11** least in the general sense is something that is

06:10:10 **12** involved in a regular -- regular aspect of what you

06:10:14 **13** do at AAC?

06:10:14 **14 A** **It is a regular thinking about projected losses, the**

06:10:20 **15** **potential for loss is a, you know, a general**

06:10:24 **16** **responsibility of the analysts who cover specific**

06:10:28 **17** **policies.**

06:10:30 **18 Q** And what I'm trying to find out is your involvement

06:10:32 **19** with respect to determining reserves at the company.

06:10:36 **20 A** **I would be responsible for my group developing**

06:10:40 **21** **reserves, if any, specific to the asset classes that I**

06:10:46 **22** **would be response still for.**

06:10:48 **23 Q** Do you have any responsibility for setting reserves

06:10:54 **24** with respect to potential claims for the LVM policy?

06:10:58 **25 A** **I do not.**

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06:11:00 **1 Q** Now, when reserves are set up at AAC could you just

06:11:10 **2** describe for us, what does it mean just in general

06:11:14 **3** sense, what does it mean when you say that the reserve

06:11:16 **4** is set up with respect to RMBS policies, for example?

06:11:20 **5** MR. SIMMONS: Your Honor, what's the relevance

06:11:22 **6** of this at this point?

06:11:24 **7** THE COURT: What is the relevance?

06:11:26 **8** Mr. WHITMER: The relevance is we have been

06:11:28 **9** proposing that a reserve be set up for the benefit of

06:11:32 **10** the LVM policyholders and Mr. Peterson was unprepared

06:11:36 **11** to speak to how that would work, and now we have a

06:11:38 **12** representative from AAC who sounds like he's fully

06:11:42 **13** capable of speaking to how reserves work at AAC and

06:11:44 **14** what options may be plausible.

06:11:48 **15** MR. SIMMONS: And, Your Honor, Mr. Barranco

06:11:48 **16** testified he had no knowledge of reserving with

06:11:50 **17** respect to the LVM deal.

06:11:52 **18** THE COURT: That's correct.

06:11:54 **19** MR. WHITMER: He also testified as part of a

06:11:56 **20** regular part of his work he deals with reserving and

06:11:58 **21** he fully understand how they operate at AAC.

06:12:02 **22** THE COURT: I believe that his prior statement,

06:12:04 **23** though, would indicate that he would not have the

06:12:08 **24** background or knowledge to answer the questions you

06:12:10 **25** specifically are directed toward. Sustain the

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06:12:14 **1** objection.

06:12:16 **2 Q** Sir, let me find out a little bit about your

06:12:18 **3** capabilities are with respect to speaking to the

06:12:20 **4** reserves of AAC. If I were to look to speak to

06:12:24 **5** someone at AAC about how reserves work at the company,

06:12:28 **6** would you put yourself toward the top of the list of

06:12:30 **7** someone capable to speak of how those work?

06:12:34 **8 A** **With respect to certain reserves, yes.**

06:12:36 **9 Q** And those reserves that you're familiar with and you

06:12:44 **10** know how they work, would you agree with me that

06:12:50 **11** merely having a reserve on the books at AAC doesn't

06:12:54 **12** mean that the money that associates with that reserve

06:12:58 **13** is going to be there at the end of the day for the

06:13:00 **14** policyholder who makes the claim for that specific

06:13:02 **15** amount?

06:13:06 **16** MR. SIMMONS: Objection argumentative, Your

06:13:08 **17** Honor.

06:13:08 **18** THE COURT: It is. I'll sustain the objection.

06:13:12 **19 Q** Sir, are you familiar with Reg 114 trust?

06:13:18 **20 A** **No. No, I'm not.**

06:13:22 **21** MR. WHITMER: I have no further questions, Your

06:13:22 **22** Honor.

06:13:24 **23** THE COURT: All right. Next up.

06:13:24 **24** **CROSS-EXAMINATION**

06:13:42 **25** **BY MR. BENTLEY:**

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06:13:42 **1 Q** Good afternoon, Mr. Barranco?

06:13:44 **2 A** **Good afternoon.**

06:13:44 **3 Q** We haven't met. My name is Philip Bentley and I

06:13:48 **4** represent the LVM bondholders in this proceeding. I'm

06:13:54 **5** going to ask you a few questions about the CDS

06:13:58 **6** transactions that you testified about. Let me start

06:14:02 **7** by asking: Are you aware that the Plan of

06:14:06 **8** Rehabilitation that's being proposed here has some

06:14:10 **9** provisions concerning the treatment of certain CDS

06:14:14 **10** claims?

06:14:14 **11 A** **Yes.**

06:14:16 **12 Q** And are you familiar generally speaking with those

06:14:20 **13** provisions of the Plan?

06:14:22 **14** MR. SIMMONS: Object as vague and overbroad,

06:14:24 **15** Your Honor, which provisions is he talking about.

06:14:28 **16 Q** You're aware that the Plan has certain provision

06:14:30 **17** relating to the treatment of CDS claims.

06:14:34 **18 A** **Generally aware mainly through what I've heard this**

06:14:36 **19** **week.**

06:14:36 **20 Q** Okay. And what's your understanding of what those

06:14:40 **21** provisions say?

06:14:40 **22 A** **That they were to be -- had had at a certain**

06:14:48 **23** **classification that's -- that there was some issue**

06:14:50 **24** **with that, but nothing --**

06:14:52 **25 Q** Did they receive a certain kind of treatment under the

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06:14:54 **1** Plan?

06:14:54 **2 A** **Yes.**

06:14:54 **3 Q** And are you aware that the treatment they received is

06:14:58 **4** pari passu with the treatment of policyholders?

06:15:04 **5** MR. SIMMONS: Objection relevance, Your Honor.

06:15:04 **6** THE COURT: What would be the relevance, Mr.

06:15:04 **7** Bentley?

06:15:08 **8** MR. BENTLEY: Your Honor, this witness offered

06:15:10 **9** testimony going specifically to this issue, namely

06:15:14 **10** whether it's appropriate -- namely the nature of the

06:15:16 **11** CDS claims which is legally relevant because it's

06:15:20 **12** relevant to whether the treatment of these claims is

06:15:22 **13** appropriate under the Plan, so what I'd like to do --

06:15:24 **14** This is predicate, Your Honor, and I'm going to move

06:15:26 **15** on very quickly to ask some questions that are may be

06:15:30 **16** more obvious in development.

06:15:32 **17** THE COURT: Let's go to those, because he's

06:15:34 **18** indicated what he's learned he's picked up by sitting

06:15:38 **19** here and he may be one of the few that's really

06:15:40 **20** learned anything sitting here two days.

06:15:46 **21 Q** Fair enough, Your Honor. Mr. Barranco, did you have

06:15:52 **22** any involvement in the formulation of these provisions

06:15:54 **23** of the Plan, the ones that relate to the treatment of

06:15:56 **24** CDS claims?

06:15:58 **25 A** **No, I did not.**

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06:16:00 **1 Q** Now, you're aware that a settlement with the CDS banks

06:16:06 **2** -- the so-called CDS banks was negotiated back in the

06:16:12 **3** spring of this year, correct?

06:16:12 **4 A** **Yes.**

06:16:12 **5 Q** Did you have any involvement in the discussions

06:16:16 **6** leading up to that settlement?

06:16:20 **7 A** **Yes.**

06:16:22 **8 Q** What was the nature of your involvement?

06:16:24 **9 A** **I was involved throughout the process ABC CDOs were of**

06:16:32 **10** **the assets class that were my responsibility so I**

06:16:34 **11** **would -- you know, I was familiar with, you know, the**

06:16:38 **12** **view on the transaction, the impairments, the**

06:16:40 **13** **counterparties, all aspects of the actual transactions**

06:16:44 **14** **that were commuted.**

06:16:44 **15 Q** Were you involved in an evaluation of factual issues

06:16:50 **16** relating to -- relating to the dispute over

06:16:58 **17** policyholder -- over the priority of these claims that

06:17:02 **18** was one of the issues being negotiated?

06:17:04 **19 A** **You know, I would open my credit file, I see CDS and**

06:17:08 **20** **see a financial guarantee plan backing that CDS and**

06:17:12 **21** **that -- that's the extent of what I was focused on.**

06:17:14 **22 Q** Were you asked to look at any facts or give any

06:17:18 **23** opinions in connection with the negotiations or the

06:17:20 **24** related discussions?

06:17:22 **25 A** **With respect to --**

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06:17:26 **1 Q** As Ambac was evaluating its position in these

06:17:30 **2** negotiations, did anybody ask you to look at any facts

06:17:34 **3** or express any views on factual issues?

06:17:38 **4 A** **Yes.**

06:17:38 **5 Q** Which issues?

06:17:40 **6 A** **Mainly the view on the performance projected losses of**

06:17:44 **7** **these -- of these transactions.**

06:17:46 **8 Q** Did you have any discussions in connection with these

06:17:52 **9** negotiations about whether the banks held the

06:17:56 **10** underlying securities relating to the CDS claims?

06:18:00 **11 A** **Did I have any specific discussions with just**

06:18:04 **12** **clarifying with whom?**

06:18:08 **13 Q** With anybody in connection with negotiations with the

06:18:12 **14** CDS banks?

06:18:12 **15 A** **So trying to refer to my previous testimony over the**

06:18:18 **16** **previous two or more years ahead of the -- of the --**

06:18:22 **17** **of the global commutation of ABS CDOs, I had lots of**

06:18:28 **18** **interaction with specific counterparties to their**

06:18:32 **19** **positions as we tried to work on various restructuring**

06:18:36 **20** **solutions or as I mentioned before where we directed**

06:18:38 **21** **counterparties to do certain things.**

06:18:40 **22 Q** And the parties that you're referring to, the

06:18:42 **23** counterparties that you're referring to, were they

06:18:44 **24** parties to the CDS settlement?

06:18:48 **25 A** **Yes.**

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06:18:48 **1 Q** And would you say that you're generally familiar with
06:18:54 **2** the deals underlying the CDS claims that were settled?
06:18:58 **3 A Yes.**
06:19:00 **4 Q** How many deals were there underlying those claims?
06:19:04 **5 A Okay. When we started the crisis, you know, it -- or**
06:19:10 **6 crisis started in 2008, Ambac had \$30 billion net par**
06:19:16 **7 exposure across I think it was 29 transactions, and so**
06:19:22 **8 by the time we got to the bank deal and some of those**
06:19:24 **9 other transactions had been commuted we were down to**
06:19:30 **10 whatever the last 16 or so transactions or maybe it**
06:19:32 **11 was less.**
06:19:34 **12 Q** Okay. So 16 or so transaction with 14 -- with 14
06:19:38 **13** bank counterparties?
06:19:40 **14 A That's correct.**
06:19:42 **15 Q** These were CDO transactions?
06:19:46 **16 A These are what we would call ABS CDOs or asset-backed**
06:19:52 **17 CDOs, and they were a CDO structure, a**
06:19:56 **18 structured-finance vehicle backed primarily by**
06:20:00 **19 subprime-mortgage backed securities as well as other**
06:20:04 **20 CDO securities as well.**
06:20:06 **21 Q** And the latter types of CDOs would called CDO squared
06:20:12 **22** or CDO cubed?
06:20:14 **23 A Yes. Indeed a CDO with all CDOs underlying with**
06:20:20 **24 assets would be called a CDO squared in that market**
06:20:24 **25 parlance.**

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06:20:24 **1 Q** How many of the 16 or so transaction were CDO squared
06:20:28 **2** or CDO cubed?
06:20:30 **3 A So the remaining transactions in the bank group**
06:20:34 **4 settlement, I think there was only one CDO squared.**
06:20:38 **5 We did have at least -- I think we had three other**
06:20:42 **6 CDOs squared that were commuted prior to the bank**
06:20:48 **7 group settlement.**
06:20:48 **8 Q** And just to help out the Court and probably a number
06:20:52 **9** of the folks in court can you give a brief description
06:20:56 **10** of what is a CDO hopefully in layman's terms?
06:21:00 **11 A Okay. A CDO is a security, a debt obligation, a --**
06:21:06 **12 that is -- that issues notes and the proceeds from**
06:21:12 **13 those notes are used to buy other asset-backed**
06:21:16 **14 securities or structured-finance securities and the --**
06:21:20 **15 the notes are issued in -- to claim a priority where**
06:21:24 **16 you have the notes that are furthest away from risk**
06:21:28 **17 are what they call the AAA notes, and then the notes**
06:21:30 **18 closest to the risk would be either the equity or the**
06:21:34 **19 junior notes. And structures work where, you know,**
06:21:40 **20 cash flows come off the underlying assets and they're**
06:21:44 **21 used to put through a waterfall to pay interest and**
06:21:48 **22 principal on the set of notes that were issued.**
06:21:50 **23 Q** Now, some CDOs are called synthetic CDOs?
06:21:56 **24 A That's correct.**
06:21:56 **25 Q** Can you please explain again hopefully in simple terms

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06:22:00 **1** what is a synthetic CDO?
06:22:04 **2** MR. SIMMONS: Your Honor, what's the relevance
06:22:04 **3** of this testimony. It's not clear where we're going.
06:22:08 **4** MR. BENTLEY: Your Honor, the relevance will
06:22:08 **5** become very clearly in another question or two.
06:22:10 **6** THE COURT: All right. I'm waiting. Go ahead.
06:22:14 **7** THE WITNESS: A -- What I previously described
06:22:16 **8** as a cash -- as a CDO is what we would call a cash
06:22:22 **9** CDO where the bond proceeds were used to buy specific
06:22:26 **10** securities.
06:22:28 **11** A synthetic CDO simply means that there are
06:22:34 **12** instead of actually buying the securities, the
06:22:38 **13** transaction is actually buying the -- or selling risk
06:22:46 **14** against certain -- certain other security, so it's
06:22:48 **15** not physically owning those securities.
06:22:50 **16 Q** And so what does the issuer or the sponsor or the
06:22:56 **17** trust purchase?
06:22:56 **18 A The trust is essentially purchasing CDS contracts on**
06:23:02 **19 other -- on certain ABS securities.**
06:23:10 **20** MR. SIMMONS: Objection, Your Honor. The
06:23:10 **21** relevance of this has not become clear. It seems to
06:23:16 **22** be an effort just to get discovery to bolster an issue
06:23:18 **23** that's already on appeal. This is the same sorts of
06:23:20 **24** arguments we had earlier in the week.
06:23:22 **25** THE COURT: Yeah. You were going to get us

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06:23:24 **1** there in one question.
06:23:26 **2** MR. BENTLEY: I'll get here right now.
06:23:28 **3** THE COURT: All right.
06:23:30 **4 Q** How many of the 16 or so deals that were covered by
06:23:32 **5** the CDS settlement were synthetic CDO deals?
06:23:40 **6 A In the settlement --**
06:23:42 **7** MR. SIMMONS: Objection, relevance, Your Honor.
06:23:42 **8** What difference does this make to the Plan of
06:23:42 **9** Rehabilitation.
06:23:44 **10** THE COURT: Make an offer so we know this is
06:23:46 **11** going somewhere or it's just Insurance or Securities
06:23:52 **12** 101.
06:23:52 **13** MR. BENTLEY: Well, I was hoping, Your Honor,
06:23:54 **14** that all of us in the courtroom could learn something.
06:23:56 **15** But beyond that, Your Honor, the relevance here is --
06:24:02 **16** and I'm going to get to the Plan because we're really
06:24:04 **17** here about the Plan -- this witness has offered
06:24:06 **18** testimony relating to the question of whether the CDS
06:24:14 **19** claims are -- relate to -- sorry -- arise out of
06:24:18 **20** transactions where the banks own the underlying
06:24:20 **21** securities. He has said he thinks they do. For some
06:24:24 **22** reasons that I'm now going to -- I'm trying to
06:24:28 **23** explore. And what I'm trying to establish, Your
06:24:30 **24** Honor, is that -- that it may be that the deals he's
06:24:36 **25** talking about, what the banks actually hold are

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06:24:40 **1** interest in synthetic CDOs. And there --
06:24:42 **2** THE COURT: Why don't we get right to the
06:24:46 **3** question and let's just see if it's relevant or not.
06:24:50 **4 Q** Okay. How many -- You said you're familiar with the
06:24:58 **5** CDS claims that -- that the transactions that relate
06:25:02 **6** to the remaining CDS claims, how many of those were
06:25:08 **7** synthetic -- involved synthetic CDOs?
06:25:12 **8 A** **Of the 16 or so deals that were commuted as part of**
06:25:18 **9** **the bank group?**
06:25:18 **10 Q** Correct.
06:25:18 **11 A** **I think maybe one and I don't even know if this was**
06:25:24 **12** **fully synthetic either. I think it was partially**
06:25:28 **13** **synthetic and partially cash assets.**
06:25:30 **14 Q** And were some of them partially synthetic?
06:25:32 **15 A** **Yes.**
06:25:32 **16 Q** In fact weren't most of them at least partially
06:25:36 **17** synthetic?
06:25:36 **18** MR. SIMMONS: Object to the relevance, Your
06:25:38 **19** Honor.
06:25:38 **20** THE COURT: All right. I think we've heard
06:25:40 **21** enough and I'll sustain that objection. Let's move
06:25:42 **22** on, Mr. Bentley.
06:25:44 **23** MR. BENTLEY: Your Honor, if I may.
06:25:46 **24** THE COURT: Make an offer. Go ahead.
06:25:48 **25** MR. BENTLEY: He gave some extensive testimony

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06:25:50 **1** about the reasons for his belief why the banks held
06:25:56 **2** the underlying securities. And what I'm trying to
06:25:58 **3** establish is if the deals, in fact, involved synthetic
06:26:02 **4** CDOs, then holding the underlying securities doesn't
06:26:06 **5** mean in any way they suffered losses. The losses
06:26:08 **6** issue is the issue that's relevant to the Plan.
06:26:12 **7** THE COURT: Why don't you go there and let's see
06:26:14 **8** if it is relevant.
06:26:14 **9 Q** Okay.
06:26:14 **10 A** **Just to be clear.**
06:26:16 **11 Q** Mm-hmm (Yes).
06:26:18 **12 A** **A transaction that may have some synthetic securities**
06:26:22 **13** **in it, the banks would still actually own a physical**
06:26:24 **14** **note on these transactions that you describe as**
06:26:30 **15** **partially synthetic.**
06:26:32 **16** MR. SIMMONS: Your Honor, we continue to object
06:26:34 **17** on relevance grounds.
06:26:36 **18** THE COURT: All right. I guess I ruled several
06:26:38 **19** times that it isn't relevant. It may be
06:26:40 **20** interesting -- interesting to the folks who are here,
06:26:44 **21** but it isn't really relevant to the Plan or the
06:26:46 **22** application. You said you were going to show some
06:26:50 **23** correlation there. Why don't you go there and let's
06:26:52 **24** talk about that area.
06:26:54 **25** MR. BENTLEY: Okay. You explained on direct

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06:27:00 **1** some reasons why you think the banks hold the
06:27:02 **2** underlying securities. Have you ever been told by any
06:27:06 **3** of the banks that they do hold the underlying
06:27:08 **4** securities?
06:27:10 **5** MR. SIMMONS: Your Honor, same objection. This
06:27:12 **6** is dealing --
06:27:12 **7** THE COURT: Sustained.
06:27:12 **8** MR. BENTLEY: Your Honor, this is -- If I may
06:27:14 **9** briefly. This is testimony they elicited and they're
06:27:18 **10** now saying I can't cross on the very testimony they
06:27:20 **11** chose to bring out. That's a little one-sided, Your
06:27:24 **12** Honor.
06:27:24 **13** THE COURT: Sustained. Let's move on. How does
06:27:28 **14** it relate to the Plan. Get to the point.
06:27:30 **15** MR. BENTLEY: Your Honor, it relates to the Plan
06:27:32 **16** because we established the other day that if the CDS
06:27:38 **17** settlement is reversed, we have potentially billions
06:27:40 **18** of dollars in bank claims.
06:27:42 **19** THE COURT: Is that what you're seeking
06:27:42 **20** verification of?
06:27:44 **21** MR. BENTLEY: That's where I'm going, Your
06:27:46 **22** Honor.
06:27:46 **23** THE COURT: All right. Well, then let's get
06:27:46 **24** there.
06:27:54 **25 Q** You were just saying that it may be that a number of

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06:27:58 **1** these deals were partially synthetic. Can you
06:28:02 **2** explain--
06:28:02 **3** MR. SIMMONS: Your Honor, same objection here.
06:28:04 **4** Mr. Bentley's explanation went directly to the appeal
06:28:10 **5** frankly. I mean this issue is on appeal right now.
06:28:12 **6** None of these people are policyholders. The deal
06:28:16 **7** settled. It's on appeal.
06:28:18 **8** MR. BENTLEY: Your Honor, we established the
06:28:18 **9** other day that if the appeal results in a reversal,
06:28:22 **10** than this Plan may give billions of dollars to these
06:28:28 **11** banks, and so the question arises have the banks
06:28:30 **12** established that they suffered actual losses such that
06:28:34 **13** they should be entitled to receive this money?
06:28:36 **14** THE COURT: Sustained the objection.
06:28:40 **15** MR. BENTLEY: Have you ever seen any documents
06:28:42 **16** showing that the banks hold any of the underlying
06:28:48 **17** securities?
06:28:48 **18** MR. SIMMONS: Your Honor, same objection.
06:28:50 **19** THE COURT: Same ruling. Sustained.
06:28:52 **20** MR. BENTLEY: Are you familiar with the CDS
06:29:00 **21** claims that have not been settled and that are being
06:29:02 **22** treated under the Plan?
06:29:04 **23** THE WITNESS: Can you clarify claims?
06:29:06 **24 Q** Okay. The Plan provide that the holder of any
06:29:12 **25** financial guarantee claim, including a claim relating

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06:29:16 **1** to a credit default swap gets a certain treatment.

06:29:22 **2** Are you aware that there are certain CDS

06:29:26 **3** counterparties who were not part of the March

06:29:28 **4** settlement?

06:29:28 **5 A Yes. Yes, I am aware that there were. We still have**

06:29:34 **6 a number of outstanding CDS contracts.**

06:29:36 **7 Q** So let me ask you about those. Those are being

06:29:40 **8** treated under the Plan, aren't they, as far as you

06:29:42 **9** know?

06:29:42 **10 A There are some CDS contracts in the Segregated**

06:29:46 **11 Account. There are some CDS contracts in the General**

06:29:50 **12 Account.**

06:29:50 **13 Q** So I'm glad you clarified that. What I mean to ask

06:29:54 **14** you about are the ones that are in the Segregated

06:29:56 **15** Account and are therefore being treated under the

06:29:58 **16** Plan.

06:29:58 **17 A Okay.**

06:29:58 **18 Q** Let's focus on those claims. How many deals do those

06:30:02 **19** arise out of?

06:30:04 **20 A Okay. I just want to be clear. I think of claim or**

06:30:08 **21 potential claim or reserve, I would -- I think about**

06:30:12 **22 an impairment on the security, and I would not**

06:30:16 **23 describe any of the CDS contracts that remain in the**

06:30:22 **24 Segregated Account as having a reserve or an**

06:30:24 **25 impairment on them. So I just want to be clear when**

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06:30:28 **1 you same claim and I say claim, I just want to -- I**

06:30:32 **2 want you to understand what I think when I think about**

06:30:36 **3 a claim.**

06:30:36 **4 Q** Okay. Understood. Are you aware that the Disclosure

06:30:40 **5** Statement contains certain projections of potential

06:30:42 **6** losses with respect to those policies?

06:30:44 **7 A I'm aware that there is a projection, I believe with**

06:30:48 **8 respect to mark-to-market -- potential mark-to-market**

06:30:54 **9 claims.**

06:30:54 **10 Q** What I'm referring to is that the Disclosure Statement

06:30:58 **11** projects a range of between \$5 million and \$20 million

06:31:02 **12** of potential losses with respect to the nonsettled CDS

06:31:06 **13** claims that are in the Segregated Account. Are you

06:31:10 **14** aware of that?

06:31:10 **15 A I am not.**

06:31:12 **16 Q** Okay. Regardless of your knowledge of that statement,

06:31:18 **17** let me ask you about those deals. The CDS deals that

06:31:22 **18** are in the Segregated Account and that have not

06:31:24 **19** settled.

06:31:26 **20 A Okay.**

06:31:26 **21 Q** Focusing on those deals, how many deals -- how many

06:31:30 **22** policies are there?

06:31:32 **23 A I am not sure of the exact number of policies but**

06:31:36 **24 my -- I recollect there is roughly \$2.5 billion of**

06:31:42 **25 par outstanding of CDS contracts in the Segregated**

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06:31:46 **1 Account.**

06:31:48 **2 Q** Do you know how many underlying deals --

06:31:52 **3 A I don't.**

06:31:54 **4 Q** -- that reflect?

06:31:54 **5 A I would only be guessing and I would -- the number**

06:31:58 **6 would be under 30.**

06:32:00 **7 Q** And do you know if some of those deals are

06:32:06 **8** synthetic -- strike that. Are those all CDOs to your

06:32:10 **9** knowledge?

06:32:10 **10 A They are not all CDOs.**

06:32:14 **11 Q** How many are CDOs?

06:32:16 **12 A I'm not sure of the exact number.**

06:32:18 **13 Q** Are some of those deals synthetic CDOs?

06:32:22 **14 A Not to my knowledge.**

06:32:24 **15 Q** Do you know one way or the other or do you simply not

06:32:26 **16** know?

06:32:28 **17 A I am not aware of any of those transactions, CDS**

06:32:38 **18 contracts residing in Segregated Account as being**

06:32:40 **19 synthetic transactions as -- as synthetic as you**

06:32:44 **20 described before.**

06:32:46 **21 Q** Okay. And with respect to those deals, has anybody

06:32:50 **22** ever -- have any of the banks that are the

06:32:54 **23** counterparties in those deals ever told you that they

06:32:56 **24** do hold the underlying securities?

06:32:58 **25 A Have they told me specifically that they hold the**

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06:33:02 **1 underlying securities?**

06:33:02 **2 Q** Correct?

06:33:04 **3 A No. But would say the same with -- again with all of**

06:33:10 **4 our CDS contracts the key contractual elements is is**

06:33:14 **5 our control right and is there -- actually is our**

06:33:18 **6 ability to direct them to do certain things, and in**

06:33:22 **7 addition to ABS CDOs, which are written on CDS**

06:33:26 **8 contracts, we've also with respect to CLOs and other**

06:33:30 **9 deals we've also instructed people to do different**

06:33:32 **10 things, move collateral managers and what have you.**

06:33:36 **11 So my expectation would be similar to what it was for**

06:33:40 **12 the ABS CDOs.**

06:33:44 **13 Q** If these were synthetic CDOs they would be able to

06:33:48 **14** take direction, wouldn't they?

06:33:50 **15** THE COURT: He's already said they're not.

06:33:52 **16 Q** He said he doesn't know for sure.

06:33:54 **17 A Can you ask that question again?**

06:33:56 **18 Q** Okay. If a CDS counterparty had a claim that arose

06:34:06 **19** out a synthetic CDO could that counterparty

06:34:12 **20** effectively take direction from Ambac?

06:34:14 **21 A I guess I'm not really following. I mean, the way I**

06:34:20 **22 would understand it to work, and again this is like**

06:34:22 **23 controlling creditor type of issues, so we have a CDS**

06:34:26 **24 again a senior bond in a particular trust, that senior**

06:34:32 **25 bond has certain control rights, because they're the**

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06:34:36 **1** senior bond. As part of our CDS contract they have
06:34:40 **2** agreed to let us direct them with respect to any sort
06:34:42 **3** of control rights in those bonds -- in those
06:34:44 **4** particular bonds. And so the things that we would do,
06:34:48 **5** you know, by and large, these transactions that are
06:34:52 **6** left over in the Segregated Account in the General
06:34:54 **7** Account as CDSs are performing pretty well but to the
06:34:58 **8** extent there was a trigger trip where we could switch
06:35:04 **9** a collateral manager or something like, that we would
06:35:06 **10** exercise that right and have done so. So I guess I'm
06:35:12 **11** not understanding fully the synthetic analogy in terms
06:35:14 **12** of not following our direction as a -- which, you
06:35:20 **13** know, which the counterparty has given to us.
06:35:22 **14** Q All right, what I'm asking is, does the fact that the
06:35:24 **15** counterparty is capable of exercising, acting upon the
06:35:30 **16** direction that Ambac gives, that doesn't tell you
06:35:32 **17** whether the deal is a synthetic CDO or not, does it?
06:35:38 **18** A Does it tell -- No. We would know -- As we underwrote
06:35:44 **19** a transactions we would know whether a transaction was
06:35:48 **20** a synthetic CDO or not.
06:35:50 **21** Q You weren't involved in the underwriting of these
06:35:52 **22** transactions?
06:35:54 **23** A I have responsibility for a lot of those transactions
06:35:58 **24** particularly the CLOs that remain and I would be
06:36:00 **25** generally familiar with those transactions.

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06:36:04 **1** Q But we're not speaking now about the deals that you
06:36:08 **2** underwrote, are we?
06:36:08 **3** A I don't believe there are any CLOs in the Segregated
06:36:14 **4** Account that I underwrote.
06:36:16 **5** MR. BENTLEY: Okay. Thank you, Mr. Barranco. I
06:36:18 **6** have no further questions.
06:36:20 **7** THE COURT: All right. Any other --
06:36:20 **8** CROSS-EXAMINATION
06:36:20 **9** BY MR. BLOOMGARDEN:
06:36:46 **10** Q Good afternoon, Mr. Barranco. Craig Bloomgarden on
06:36:48 **11** behalf of Freddie Mac. I just want to follow-up on
06:36:52 **12** one thing that Mr. Bentley was just questioning you
06:36:56 **13** about. I believe he asked you if you knew whether any
06:37:08 **14** of the CDS contracts that are in the Segregated
06:37:14 **15** Account were synthetic CDOs, and I believe you said
06:37:20 **16** not to your knowledge. Mr. Bentley also asked you I
06:37:30 **17** believe whether you knew one way or another -- and I
06:37:34 **18** don't believe you answered that question -- if you had
06:37:34 **19** personal knowledge one way or another as to whether
06:37:38 **20** any of those transactions were synthetic CDOs?
06:37:44 **21** A To be clear my knowledge in terms of synthetic CLOs,
06:37:50 **22** Ambac had very, very limited exposure to synthetic --
06:37:54 **23** purely synthetic CDOs. I think there is a discontinue
06:37:58 **24** that Mr. Bentley made about if a note structure note
06:38:02 **25** is issued and in the underlying assets of that

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06:38:06 **1** securitization there are some cash note -- there are
06:38:08 **2** some cash assets and some synthetic assets that is not
06:38:12 **3** the same thing as saying this is a synthetic note,
06:38:16 **4** that we were facing just a synthetic contract. That's
06:38:20 **5** the distinction, and to the best of my knowledge that
06:38:24 **6** are no synthetic CDOs as Mr. Bentley described in the
06:38:30 **7** Segregated Account.
06:38:32 **8** Q Okay. And -- And again you've indicated to the --
06:38:38 **9** to the best of your knowledge and I'm asking you, do
06:38:40 **10** you know one way or the other or are you just saying
06:38:42 **11** you're not aware of any but have you done an
06:38:46 **12** examination of each and every one of those
06:38:48 **13** transactions to be able to render testimony on that
06:38:52 **14** subject as to each and every one of them?
06:38:56 **15** MR. SIMMONS: Objection, asked and answered,
06:38:58 **16** Your Honor. He's given testimony on this.
06:38:58 **17** THE COURT: Sustained.
06:39:04 **18** Mr. BLOOMGARDEN: Nothing further, Your Honor.
06:39:04 **19** THE COURT: All right. Who is next? Cross?
06:39:14 **20** Any redirect. Just a moment. Anyone on the phone
06:39:16 **21** wish to cross this witness?
06:39:22 **22** UNIDENTIFIED SPEAKER (Speaking via telephone):
06:39:22 **23** No, thank you, Your Honor.
06:39:24 **24** THE COURT: All right.
06:39:24 **25** MR. SIMMONS: Just two quick questions, Your

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06:39:26 **1** Honor, on redirect, Your Honor.
06:39:26 **2** REDIRECT EXAMINATION
06:39:26 **3** BY MR. SIMMONS:
06:39:28 **4** Q Mr. Barranco, some of the cross-examination went to
06:39:30 **5** your comments regarding commutations and maximizing
06:39:36 **6** returns on capital through commutations; do you recall
06:39:40 **7** that questioning?
06:39:40 **8** A I do.
06:39:40 **9** Q By Ambac maximizing return to capital through
06:39:44 **10** commutations, what effect does that have on the
06:39:48 **11** claims-paying resources of Ambac?
06:39:48 **12** A It increases it.
06:39:50 **13** Q And then with -- Changing subjects, with regard to the
06:39:54 **14** student loan allocation process that you were involved
06:39:56 **15** in, who ultimately decided which policies got
06:40:02 **16** allocated to the Segregated Account?
06:40:02 **17** A OCI can.
06:40:04 **18** MR. SIMMONS: No further questions, Your Honor.
06:40:06 **19** THE COURT: All right. That will complete the
06:40:08 **20** examination. You may step down.
06:40:16 **21** THE COURT: Call your next witness.
06:40:16 **22** MR. SIMMONS: We call Cathleen Matanle, Your
06:40:20 **23** Honor.
06:40:20 **24** THE COURT: Will you come up, Ms. Matanle up
06:40:22 **25** here to the witness chair. Watch your step as you go

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06:40:26 **1** through the well there. And raise your right and
06:40:30 **2** receive the witness oath, please.
06:40:38 **3** **CATHLEEN MATANLE**
06:40:38 **4** was duly sworn by the Clerk and was examined and
06:40:38 **5** testified as follows:
06:40:38 **6** THE COURT: Be seated. As has been pointed out,
06:40:46 **7** watch your chair so you don't go over the edge of the
06:40:48 **8** platform. All right. Start please by stating your
06:40:52 **9** name.
06:40:52 **10** THE WITNESS: My name is Cathleen Matanle.
06:40:54 **11** THE COURT: Do you have the spelling of that?
06:40:54 **12** COURT REPORTER: Yes.
06:40:56 **13** THE COURT: And do you understand the procedure
06:40:58 **14** we like to follow here in terms of you answer
06:41:00 **15** questions after they've been fully asked, and while
06:41:04 **16** you're answering counsel will not start to ask you new
06:41:10 **17** questions until you're done answering the question
06:41:12 **18** asked.
06:41:12 **19** THE WITNESS: Yes. I understand.
06:41:14 **20** THE COURT: All right. You may proceed.
06:41:14 **21** **DIRECT EXAMINATION**
06:41:14 **22** **BY MR. SIMMONS:**
06:41:16 **23** **Q** You may want to admonish her in advance, Your Honor,
06:41:18 **24** to slow down. Have you ever testified in court
06:41:24 **25** before, Ms. Matanle?

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06:41:26 **1** **A** **No.**
06:41:26 **2** **Q** Can you tell the Court who your employer is?
06:41:28 **3** **A** **Yes. I work for Ambac Assurance Company.**
06:41:30 **4** **Q** Okay. And what's your position at Ambac Assurance
06:41:30 **5** Corporation?
06:41:34 **6** **A** **I'm a senior credit officer and managing director. I**
06:41:36 **7** **run a large portion of the risk management function of**
06:41:40 **8** **the organization, and that comprises the surveillance**
06:41:44 **9** **activity for the exposures in the General Account, and**
06:41:46 **10** **it also -- it also covers many of the risk related**
06:41:52 **11** **services that are necessary to conduct surveillance**
06:41:54 **12** **and remediation across both the General Account and**
06:41:58 **13** **the Segregated Account.**
06:41:58 **14** **Q** Okay. And how long have you had those
06:42:00 **15** responsibilities?
06:42:02 **16** **A** **I joined the company in 2001, and I've had various**
06:42:06 **17** **management responsibilities from the time that I**
06:42:10 **18** **joined, they've moved around a fair amount. These**
06:42:12 **19** **specific responsibilities I've had as structured for**
06:42:18 **20** **the last six months or so.**
06:42:20 **21** **Q** What did you do before you came to Ambac?
06:42:24 **22** **A** **I was in banking for 20 -- 20 plus years with JP**
06:42:28 **23** **Morgan.**
06:42:28 **24** **Q** And what were you doing in banking?
06:42:30 **25** **A** **I did a variety of credit and fixed income**

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06:42:34 **1** **underwriting activities.**
06:42:36 **2** **Q** And then when you came to Ambac in 2001 what were your
06:42:40 **3** initial responsibilities?
06:42:42 **4** **A** **I was brought over to Ambac because I have a**
06:42:44 **5** **background -- a very deep background in credit**
06:42:46 **6** **analysis and management and they were choosing at that**
06:42:52 **7** **time to expand their oversight of structured-finance**
06:42:56 **8** **exposures because the exposures were becoming**
06:43:00 **9** **increasingly complicated.**
06:43:02 **10** **Q** Can you just briefly describe the progression of your
06:43:06 **11** responsibilities at Ambac?
06:43:08 **12** **A** **Sure. I was brought in to run the surveillance**
06:43:10 **13** **activity for about a third of the company. It**
06:43:14 **14** **comprised the commercial an ABS, the consumer ABS and**
06:43:18 **15** **the CDO areas. I did that for a couple of years and**
06:43:24 **16** **then we collapsed down and reduced -- split the**
06:43:28 **17** **company between two people and I was one of those two**
06:43:30 **18** **people. At that time I took over the surveillance of**
06:43:32 **19** **the public finance business. And we reorganized, you**
06:43:38 **20** **know -- I think the mortgage-backed business was then**
06:43:40 **21** **handed over to someone else at that point in time.**
06:43:44 **22** **Q** And so now currently you run the surveillance effort
06:43:46 **23** at Ambac; is that right?
06:43:48 **24** **A** **I run the surveillance effort. During the summer we**
06:43:52 **25** **specifically carved out the surveillance activity for**

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06:43:54 **1** **the exposures in the Segregated Account, specifically**
06:43:58 **2** **the mortgage-backed exposures and the student loan**
06:44:02 **3** **exposures. We did that because we wanted to have more**
06:44:08 **4** **direct accountability for the owners of those credits**
06:44:10 **5** **to the OCI.**
06:44:12 **6** **Q** Okay. And what's your relationship with the
06:44:14 **7** surveillance that's done for the exposures in the
06:44:16 **8** Segregated Account?
06:44:18 **9** **A** **I run the basically the office of the senior credit --**
06:44:24 **10** **senior credit manager. I'm a senior credit officer**
06:44:26 **11** **and I have three senior credit officers who work for**
06:44:30 **12** **me in that department, and we take recommendations**
06:44:34 **13** **that come to us from the surveillance managers across**
06:44:40 **14** **both the General Account and the Segregated Account.**
06:44:44 **15** **Q** Maybe we should back up for a second, we're using the
06:44:48 **16** term surveillance which I'm not sure is clear in this
06:44:50 **17** context. What does surveillance mean in the Ambac
06:44:54 **18** context?
06:44:54 **19** **A** **Surveillance has kind of a passive connotation to it.**
06:44:58 **20** **It's actually more than that. Surveillance means that**
06:45:00 **21** **you take on the ownership of credit once it's been**
06:45:04 **22** **underwritten and booked into the company's -- into**
06:45:08 **23** **the company's portfolio and that -- the surveillance**
06:45:12 **24** **analyst or the surveillance manager then owns that**
06:45:16 **25** **credit for purposes of determining how to follow the**

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06:45:18 **1 credit to look for difficulties with the credit so**
06:45:22 **2 that they can then proactively work with the credits**
06:45:26 **3 so as to avoid loss or to mitigate loss.**
06:45:30 **4 Q** Okay. And let's define another term, you were using
06:45:32 **5** the term credit. What is credit, a policy? What's a
06:45:36 **6** credit at Ambac?
06:45:36 **7 A** **Our insurance policies are basically a forum in which**
06:45:40 **8** **Ambac then takes credit exposure to the particular**
06:45:44 **9** **underlying bond or note that its insuring.**
06:45:48 **10 Q** Okay. So when you're talking credits you're generally
06:45:52 **11** talking about the policies; is that right?
06:45:52 **12 A** **I'm absolutely speaking about the policy in our**
06:45:56 **13** **insurance portfolio.**
06:45:58 **14 Q** Okay. So when you -- Well, first of all how many
06:46:00 **15** people do you have working under you conducting
06:46:02 **16** surveillance?
06:46:02 **17 A** **I have about 55 people in my part of the risk**
06:46:06 **18** **management effort.**
06:46:08 **19 Q** And when Ambac is conducting surveillance, what types
06:46:10 **20** of activities does it do?
06:46:12 **21 A** **A good example, when a transaction closes, the**
06:46:18 **22** **transaction is handed over to the surveillance**
06:46:20 **23** **department. At that point they set it up so that they**
06:46:24 **24** **basically understand the underlying criteria that got**
06:46:30 **25** **the deal into our portfolio so that they can set up a**

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06:46:32 **1** **proper monitoring system for that credit. The credits**
06:46:36 **2** **are largely boarded with someone in the surveillance**
06:46:42 **3** **department or different books of business who is**
06:46:46 **4** **skilled in the particular type of asset that it is so**
06:46:48 **5** **that it fits into, you know, what hopefully is a**
06:46:52 **6** **pretty customary way of setting up a deal to monitor,**
06:46:54 **7** **to be able to look for performance that's -- that's**
06:47:00 **8** **deviating from the underwriting expectations.**
06:47:02 **9 Q** Is surveillance important?
06:47:04 **10 A** **Yes.**
06:47:04 **11 Q** Why?
06:47:06 **12 A** **Because if you conduct good surveillance you can fix**
06:47:10 **13** **deals before they break.**
06:47:10 **14 Q** Is there any difference between the surveillance that
06:47:14 **15** Ambac performs for the General Account versus the
06:47:16 **16** surveillance that it performs for the Segregated
06:47:18 **17** Account?
06:47:18 **18 A** **No.**
06:47:18 **19 Q** I think you mentioned control rights in your
06:47:22 **20** discussion. Can you tell the Court what control
06:47:26 **21** rights are?
06:47:26 **22 A** **Control rights are the rights that are built into the**
06:47:32 **23** **contract at the time that we underwrite it that gives**
06:47:36 **24** **us the ability to then act to either instruct things**
06:47:42 **25** **to happen or prevent things from happening. Like, for**

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06:47:46 **1** **example, exercising forbearances. We generally ensure**
06:47:50 **2** **the senior most tranche in our transactions which**
06:47:54 **3** **means we are the controlling party and can instruct**
06:47:58 **4** **the trustees to take action according to whatever**
06:48:02 **5** **contractual rights we have.**
06:48:02 **6 Q** Okay. Can you give some more examples of the types of
06:48:08 **7** control rights Ambac might exercise?
06:48:10 **8 A** **Yes. For example, in an RMBS transaction there are**
06:48:14 **9** **embedded triggers that will allow us to transfer**
06:48:18 **10** **service.**
06:48:18 **11 Q** Any other examples of control rights you can exercise?
06:48:22 **12 A** **Again in an RMBS transaction we have the right to**
06:48:26 **13** **request information which we -- which we use then to**
06:48:28 **14** **get under -- underlying loan files on the home loans**
06:48:32 **15** **in the mortgage-backed securities.**
06:48:34 **16 Q** Why is it important to exercise control rights?
06:48:38 **17 A** **Because you can mitigate loss when you exercise**
06:48:40 **18** **control rights by, for example, moving the servicing.**
06:48:44 **19** **Frequently leading up to this crisis most common**
06:48:48 **20** **reason and RMBS transaction would not perform would be**
06:48:52 **21** **because it is poor servicing, so by proactively moving**
06:48:56 **22** **the servicing you could prevented or certainly**
06:49:00 **23** **mitigate loss.**
06:49:00 **24 Q** What's the servicing for an RMBS transaction?
06:49:04 **25 A** **Excuse me.**

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06:49:06 **1 Q** That's okay.
06:49:06 **2 A** **The servicing is the entity that takes over the**
06:49:10 **3** **administration of the home loans -- the underlying**
06:49:14 **4** **home loans that are in the securitization pool. So if**
06:49:16 **5** **the home loan -- if the borrower in the home loan**
06:49:20 **6** **doesn't make a payment, they get a call from a**
06:49:22 **7** **servicer.**
06:49:24 **8 Q** What's Ambac's general view towards when it should
06:49:32 **9** exercise its control rights?
06:49:32 **10 A** **Did you say willingness?**
06:49:34 **11 Q** What's its general view towards when it should
06:49:38 **12** exercise its control rights?
06:49:40 **13 A** **As early as it makes sense to do so. The way one**
06:49:44 **14** **conducts surveillance is to very quickly, when there**
06:49:46 **15** **is any stress whatsoever understand what your control**
06:49:50 **16** **rights are, and usually come up with multiple plans of**
06:49:54 **17** **how you might go about exercising controlling rights**
06:49:58 **18** **in different -- in different scenarios.**
06:50:00 **19 Q** I'd like to change topics now and just talk about your
06:50:04 **20** interactions with OCI leading up to the
06:50:10 **21** Rehabilitation. When was your first interaction with
06:50:12 **22** OCI or any of its advisors to your knowledge?
06:50:14 **23 A** **Early 2008.**
06:50:16 **24 Q** And can you just describe, you know, the circumstances
06:50:18 **25** of that interaction?

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06:50:22 **1 A Yes. In early 2008 when OCI chose to increase its**
06:50:26 **2 oversights of us because we were weakening they**
06:50:28 **3 appointed a financial advisor who then moved into a**
06:50:34 **4 conference room at our office in order to bring in**
06:50:36 **5 some equipment and live on-site for a period of time**
06:50:40 **6 while they conducted a very extensive analysis of our**
06:50:44 **7 business and got to know our people.**
06:50:46 **8 Q** And you said a financial advisor. You're referring to
06:50:48 **9** one person or a group of people?
06:50:50 **10 A A group. A group. It was a combination of the**
06:51:02 **11 Gordian Group Jeffries.**
06:51:02 **12 Q** And how long was the Gordian Group and Jeffries camped
06:51:06 **13** out in that office space at Ambac?
06:51:08 **14 A I don't remember precisely. I think it was, you know,**
06:51:12 **15 weeks, maybe a few months. When they left it wasn't**
06:51:14 **16 because they had stopped their work, it was because a**
06:51:18 **17 rhythm had developed in the conduct of their work and**
06:51:20 **18 we then worked by phone or, you know, meetings on an**
06:51:24 **19 ad hoc basis.**
06:51:26 **20 Q** So did you have any meetings with the Gordian Group or
06:51:30 **21** Jeffries while they were at Ambac's office in during
06:51:32 **22** that time in early 2008?
06:51:34 **23 A Yes, I had some, but there were also meetings more**
06:51:38 **24 increasingly so with people who work on my staff that**
06:51:40 **25 were the actual owners of the credits because they had**

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06:51:44 **1 a preference for digging in and not hearing about**
06:51:48 **2 things at a high level but rather understanding from**
06:51:52 **3 the analysts who actually owned the exposures what**
06:51:54 **4 was -- what was -- what the exposures were all**
06:51:58 **5 about, what the Plan was, if it was a stressed asset,**
06:52:00 **6 if we had projected losses, the basis on which our**
06:52:04 **7 losses were projected.**
06:52:06 **8 Q** And how many people in your group would you say had
06:52:08 **9** contact with OCI and its advisors during that time?
06:52:12 **10 A I think it fanned out, we started initially with the**
06:52:16 **11 people that were associated with at the MBSs and ABS**
06:52:22 **12 CDOs and the people that modeled those transaction so**
06:52:24 **13 it probably started with 20 people and then fanned out**
06:52:26 **14 so that over the course of the next two years I would**
06:52:32 **15 say virtually every officer in the credit function in**
06:52:34 **16 the risk management organization has had regular**
06:52:40 **17 contact with the OCI's advisors.**
06:52:42 **18 Q** Okay. And do they provide documents to OCI as part of
06:52:46 **19** that process?
06:52:46 **20 A Yes.**
06:52:46 **21 Q** Okay. And other information as well?
06:52:48 **22 A Yes.**
06:52:50 **23 Q** Are there any confidentiality concerns when Ambac has
06:53:00 **24** to provide information to outside parties?
06:53:04 **25 A Generally yes there are.**

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06:53:06 **1 Q** And why is that?
06:53:08 **2 A Well, many of our transactions are private**
06:53:10 **3 transactions and in many cases it's not clear what the**
06:53:14 **4 motivation and the roles are with the people that we**
06:53:18 **5 conduct due diligence are all about. In other words,**
06:53:22 **6 a party may be interested in getting information from**
06:53:24 **7 us in one particular instance and a person who**
06:53:28 **8 otherwise works at their firm may be adversarial to us**
06:53:34 **9 and in one of our exposures or work outs.**
06:53:36 **10 Q** Does that in any way limit the information you can
06:53:38 **11** provide to an individual third party?
06:53:40 **12 A It makes it very sensitive, it makes the negotiation**
06:53:44 **13 of a confidentiality agreement and the safeguards**
06:53:48 **14 very, very important.**
06:53:50 **15 Q** Does it result in limiting of the information that you
06:53:54 **16** provide to the third party?
06:53:56 **17 A Yes.**
06:53:56 **18 Q** And with respect to providing information to OCI were
06:53:58 **19** the same confidentiality concerns present?
06:54:00 **20 A No. They're our regulator so they have unfettered**
06:54:04 **21 rights to access information.**
06:54:04 **22 Q** If Ambac's Segregated Account policyholders access to
06:54:12 **23** just the documents and data that it gave to OCI in
06:54:18 **24** your view would the policyholders be able to replicate
06:54:22 **25** the work that OCI has done in developing the Plan of

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06:54:26 **1** Rehabilitation?
06:54:26 **2 A It would be very difficult because they've been on**
06:54:28 **3 site now for so long and they've seen the information**
06:54:32 **4 quarter after quarter after quarter, so the depth of**
06:54:34 **5 understanding has grown over that period of time.**
06:54:38 **6 Q** Would just providing the policyholders with the
06:54:40 **7** documents and data be sufficient to conduct the same
06:54:44 **8** analysis?
06:54:46 **9 A No. Because the information that one would make**
06:54:52 **10 available, in addition to the information that we**
06:54:54 **11 already make available in our SEC published on GAAP**
06:55:02 **12 10K and 10Q is very much spreadsheet based, so it's**
06:55:06 **13 prepared for our personal use, not for outsiders so it**
06:55:10 **14 rarely makes a lot of sense on its face, you know, you**
06:55:14 **15 really need to spend a fair amount of time with the**
06:55:16 **16 principals who prepare the information to understand**
06:55:18 **17 the assumptions and --**
06:55:20 **18 Q** You have meet with the employees at Ambac and have
06:55:22 **19** them explain it to you in other words?
06:55:24 **20 A Yes.**
06:55:24 **21 Q** And if -- So if you gave Segregated Account
06:55:28 **22** policyholders access to the same documents data and
06:55:30 **23** the employees necessary to explain that data, what
06:55:34 **24** kind of impact would that have on Ambac's operations?
06:55:36 **25 A Very significant impact. And we're a small company,**

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06:55:40 **1** you know there are only 80 of us in the risk
06:55:42 **2** organization, and we're working very proactively to
06:55:46 **3** work off the exposures it our portfolio. Similarly
06:55:50 **4** our finance department is small and tries to get its
06:55:54 **5** work done as a run-off company.
06:55:56 **6** Q I'd like to change topics here and talk about claims
06:56:00 **7** processing. Are you involved in claims processing at
06:56:04 **8** Ambac at all?
06:56:04 **9** A One of the departments that works for me is a
06:56:06 **10** department we call risk operations and it -- it's the
06:56:10 **11** department that's responsible for getting the inbound
06:56:16 **12** request for claims payments from the trustees, and
06:56:18 **13** then queuing them up in order to then be paid.
06:56:24 **14** Q Okay. And so describe that process of queuing them up
06:56:26 **15** to be paid a little more -- in a little more detail?
06:56:30 **16** A Sure. The request for payment comes in and it needs
06:56:34 **17** to order worded into our system so that someone can
06:56:40 **18** verify that it's a legitimate claim that's on the
06:56:42 **19** proper paperwork that's required under the contract,
06:56:44 **20** and that it has the proper signing authorities
06:56:48 **21** internally, so as to authorize the dispersement of the
06:56:52 **22** payment.
06:56:54 **23** Q How many employees at Ambac are involved in that claim
06:56:58 **24** processing function?
06:57:00 **25** A In the past we had a limited number of people that

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06:57:04 **1** were responsible, engaged in this process because we
06:57:08 **2** had been paying a large amount of claims over a
06:57:10 **3** two-year period and it had become pretty routine so
06:57:14 **4** there was maybe two people in that operations
06:57:18 **5** department that could handle the flow of payment of
06:57:22 **6** claims. In addition to the risk operations staffing
06:57:28 **7** we'd line up against an operations area in our
06:57:30 **8** treasury department, and that's where they then
06:57:32 **9** disperse the money by wire transfer.
06:57:36 **10** Q So today how many people do you have involved that are
06:57:38 **11** actually locking at the claims and deciding whether or
06:57:42 **12** not they should be paid?
06:57:42 **13** A We're not paying claims in the Segregated Account as a
06:57:46 **14** result of the moratorium but we are mapping out the
06:57:50 **15** process to reinstate the claims payment process when
06:57:54 **16** we're given instruction to do so.
06:57:58 **17** Q What about in the General Account, how many people do
06:58:00 **18** you have devoted to claims payment there?
06:58:02 **19** A No one's devoted because we very rarely pay claims out
06:58:06 **20** of the General Account.
06:58:06 **21** Q How about with respect prior to March 24th how many
06:58:10 **22** people did you have involved in claim processing?
06:58:12 **23** A As I said we probably had two across the company work
06:58:16 **24** in the risk operation area setting these up to be paid
06:58:18 **25** and checking them.

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06:58:20 **1** Q And how experienced are those people?
06:58:22 **2** A They're very experienced. I mean, it's a -- it's
06:58:26 **3** a -- it's a pretty routine administrative function.
06:58:30 **4** In the new world where, you know, paying sustained
06:58:34 **5** attention to the effort, it's going to be -- you know,
06:58:36 **6** it's going to be more challenging. We're using the
06:58:40 **7** time -- have been using the time and will continue to
06:58:42 **8** out use the time to get it mapped out properly.
06:58:44 **9** Q Do you think you have the resources to handle the new
06:58:48 **10** claims processing function?
-08:-58:-31 **11** A Yes.
-08:-58:-31 **12** Q Why do you think that?
-08:-58:-31 **13** A We really have had no turnover in the risk operations
-08:-58:-31 **14** area. And I believe we haven't had turnover in
-08:-58:-31 **15** treasury operations either. People in those
-08:-58:-31 **16** departments know that they have a fair amount of job
-08:-58:-31 **17** security.
-08:-58:-31 **18** THE COURT: Just a moment. Did you want to make
19 that switch?
20 COURT REPORTER: Yes.
21 MS. SIMMONS: That's actually my last question
22 for her, Your Honor.
23 (The following proceedings reported
24 by Reporter Albert.)
25 (4:00 p.m.)

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07:02:22 **1** THE COURT: All right. Proceed, Mr. Greenwald.
07:02:26 **2** MR. GREENWALD: Yes, your Honor.
07:02:26 **3** CROSS EXAMINATION
07:02:26 **4** BY MR. GREENWALD:
07:02:28 **5** Q Now, Ms. Matanle, you're an employee of AAC; is that
07:02:33 **6** correct?
07:02:33 **7** A Yes.
07:02:33 **8** Q And who do you report to?
07:02:35 **9** A I report to David Wallace.
07:02:36 **10** Q Okay. I'd like to ask you a series of questions, I
07:02:42 **11** think, although we're not going to look at it
07:02:44 **12** immediately. Why don't I get Mr. Wallace's affidavit
07:02:46 **13** in front of you. I believe it's Exhibit 48.
07:02:49 **14** THE COURT: Can you pull your mic up, please.
07:02:51 **15** MR. GREENWALD: Yes, I'm sorry.
07:02:53 **16** Q Exhibit 38.
07:02:58 **17** Ms. Matanle, you're undoubtedly aware that the
07:03:09 **18** holding company for AAC, AFG filed for bankruptcy last
07:03:13 **19** Monday?
07:03:13 **20** A Yes.
07:03:13 **21** Q And were you aware that Mr. Wallace had filed an
07:03:17 **22** affidavit in the first day of proceedings in the
07:03:20 **23** bankruptcy?
07:03:20 **24** A Yes. Not until I saw it posted on our internal
07:03:24 **25** website.

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07:03:25 **1 Q** And have you reviewed Mr. Wallace's affidavit?

07:03:27 **2 A** **I read it briefly.**

07:03:28 **3 Q** I want to draw your attention to one aspect -- well,

07:03:34 **4** first let me ask a couple of other questions.

07:03:37 **5** Can we also get Ms. Matanle's affidavit in front

07:03:41 **6** of her from this case which -- there's two of them, so

07:03:47 **7** I'll refer you to the first one. It's the affidavit

07:03:50 **8** dated -- it's dated May 20, 2010. I had that number

07:04:05 **9** written down.

07:04:06 **10** Do you have the exhibit number? Number 10. I'm

07:04:06 **11** sorry.

07:04:11 **12** So I'm showing you what's actually been marked as

07:04:17 **13** Objector's Exhibit Number 10. And maybe it makes

07:04:21 **14** sense to move one of those notebooks. Would that make

07:04:25 **15** it easier for you?

07:04:25 **16 A** **Which one do you want me to move?**

07:04:27 **17 Q** Well, I'll have KaIja move the one underneath. We

07:04:31 **18** don't want chairs to fall off and notebooks to fall

07:04:34 **19** off.

07:04:35 **20** Great. Thank you.

07:04:35 **21** If you could look at Exhibit Number 10 and tell me

07:04:37 **22** if you recognize at that document?

07:04:38 **23 A** **Yes, I do.**

07:04:39 **24 Q** Is this an affidavit that you've submitted in this

07:04:41 **25** proceeding?

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07:04:42 **1 A** **Yes.**

07:04:43 **2 Q** I want to turn your attention to page 4 of the

07:04:47 **3** affidavit, paragraph 13. And if you'll take a moment

07:04:52 **4** to review that, I'll have just a couple of questions.

07:05:12 **5 A** **Okay.**

07:05:12 **6 Q** All right. Paragraph 13 deals with the CDS bank

07:05:20 **7** settlement; is that correct?

07:05:22 **8 A** **Yes.**

07:05:22 **9 Q** And did you have a role in the CDS bank settlement?

07:05:26 **10 A** **Yes. I had a limited role.**

07:05:28 **11 Q** What was your role?

07:05:29 **12 A** **I was involved in the -- in dealing with the banks in**

07:05:36 **13** **more of a one-off capacity in the period of time**

07:05:40 **14** **leading up to the most active negotiations of the bank**

07:05:45 **15** **settlement, at which time I pretty much was no longer**

07:05:49 **16** **involved.**

07:05:49 **17 Q** Okay. There's been some -- have you been here all

07:05:52 **18** week --

07:05:52 **19 A** **Uh-huh (affirmative).**

07:05:53 **20 Q** -- Ms. Matanle?

07:05:54 **21 A** **Yes.**

07:05:54 **22 Q** All right there's been some testimony about an earlier

07:05:57 **23** period during which AAC pursued what has been referred

07:06:01 **24** to as one-off commutations with banks on CDS

07:06:04 **25** transactions; correct?

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07:06:05 **1 A** **Yes.**

07:06:06 **2 Q** And then later sometime late in 2009, a group of banks

07:06:12 **3** collectively negotiated with AAC for a global

07:06:16 **4** commutation?

07:06:18 **5 A** **Yes.**

07:06:18 **6 Q** And so dealing with those two periods of time, in the

07:06:22 **7** first period of time, during the one, we'll call it

07:06:25 **8** the one-off commutation era, is that when you were

07:06:30 **9** involved with dealings with the banks?

07:06:31 **10 A** **Yes.**

07:06:32 **11 Q** And in the global commutation era, were you involved

07:06:37 **12** with the banks at that time?

07:06:38 **13 A** **Substantially less so.**

07:06:41 **14 Q** I want to draw your attention to the fourth sentence

07:06:47 **15** of your paragraph 13. It says, "In exchange for

07:06:50 **16** commuting approximately \$16.7 billion of net par

07:06:56 **17** exposure." I just want to look at that part. What is

07:07:00 **18** the basis for a -- strike that.

07:07:02 **19** Can you explain what the \$16.7 billion in par

07:07:08 **20** exposure relates to?

07:07:10 **21** MR. SIMMONS: Your Honor, object on relevance

07:07:12 **22** grounds. This topic has been plowed over and over

07:07:15 **23** again.

07:07:15 **24** THE COURT: What is the relevance as to this

07:07:17 **25** witness?

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07:07:17 **1** MR. GREENWALD: I'm trying to tie out numbers in

07:07:19 **2** the liquidity analysis that was provided last Friday.

07:07:23 **3** I'm trying to -- you'll see, your Honor, that there's

07:07:25 **4** some discrepancies in the par value that I want to get

07:07:28 **5** clarity on, and this is --

07:07:30 **6** THE COURT: How is that relevant?

07:07:32 **7** MR. GREENWALD: Well, the liquidity analysis is

07:07:34 **8** driven off of CDS -- pre-CDS settlement figures. And

07:07:41 **9** I'm trying to -- we haven't been given an opportunity

07:07:45 **10** to get any discovery on the Liquidation Analysis.

07:07:48 **11** THE COURT: Sustained. Sustain the objection.

07:07:51 **12** BY MR. GREENWALD:

07:07:51 **13 Q** Ms. Matanle, do you understand that Mr. Wallace

07:07:54 **14** submitted a sworn statement in the bankruptcy

07:07:56 **15** proceeding last Monday?

07:07:58 **16 A** **Could you repeat the question?**

07:07:59 **17 Q** Do you understand that Mr. Wallace provided a sworn

07:08:03 **18** statement to the bankruptcy court last Monday, an

07:08:06 **19** affidavit?

07:08:06 **20 A** **Yes.**

07:08:06 **21 Q** And in that affidavit, he cited a par value that was

07:08:11 **22** different than the figure that is in this affidavit?

07:08:14 **23** MR. SIMMONS: Your Honor, objection.

07:08:16 **24** Misleading. He needs to direct her to a part of the

07:08:18 **25** affidavit.

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07:08:19 **1** MR. GREENWALD: I've been trying to do that,
07:08:21 **2** your Honor.
07:08:22 **3** THE COURT: Just a second. Just a second.
07:08:25 **4** Somebody is shuffling papers. It may be on the
07:08:25 **5** telephone. Or I don't think it's Mr. Bentley. He's
07:08:28 **6** busy writing.
07:08:29 **7** Let me hear your objection again. I didn't hear
07:08:33 **8** it with the shuffle going on.
07:08:36 **9** MR. SIMMONS: Your Honor, the way the question
07:08:37 **10** was phrased, it doesn't give her any direction as to
07:08:40 **11** what part of Mr. Wallace's affidavit it's referring
07:08:43 **12** to. It's misleading in the way that it's phrased
07:08:45 **13** right now.
07:08:46 **14** Also I object on relevance grounds. I don't see
07:08:48 **15** where this is going.
07:08:48 **16** THE COURT: How would the bankruptcy be relevant
07:08:50 **17** here as it relates to the Plan?
07:08:52 **18** MR. GREENWALD: There's a discrepancy in a CDS
07:08:56 **19** figure that I believe is being plugged into the
07:08:58 **20** Liquidation Analysis. I'm just trying to tie the two
07:09:01 **21** numbers out and then move on. And to do that the
07:09:03 **22** proper way, as OCI has just suggested, is to show the
07:09:07 **23** witness the affidavit. I've done that. That was
07:09:09 **24** objected to. I'd now like to ask the question
07:09:12 **25** generally. And that was objected to. I just want to

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07:09:15 **1** tie out numbers so that -- I mean --
07:09:17 **2** THE COURT: Make an offer.
07:09:19 **3** MR. GREENWALD: Okay. The offer is that Ms.
07:09:20 **4** Matanle has stated in her affidavit in May that the
07:09:24 **5** par value was \$16.7 billion. Mr. Wallace stated that
07:09:27 **6** it was \$16.3 billion on Monday.
07:09:30 **7** Now, \$400 million in the scheme of things in my
07:09:34 **8** life is material. It may or may not be here. But it
07:09:38 **9** would help me in closing argument to be able to tie
07:09:41 **10** those numbers out.
07:09:43 **11** MR. SIMMONS: Your Honor, she has no foundation
07:09:44 **12** for commenting on Mr. Wallace's affidavit.
07:09:48 **13** THE COURT: I guess --
07:09:50 **14** MR. GREENWALD: I would love to ask the
07:09:51 **15** foundation questions and just not have them objected
07:09:54 **16** so your Honor would see where we're going quickly and
07:09:56 **17** we could be done with it.
07:09:58 **18** MR. SIMMONS: Moreover, your Honor, the numbers
07:10:00 **19** are wrong. Somebody just pointed out to me the number
07:10:03 **20** is \$16.5 billion in Mr. Wallace's affidavit.
07:10:07 **21** MR. GREENWALD: If your Honor would let me show
07:10:09 **22** Ms. Matanle the affidavit, we would get that. That's
07:10:11 **23** \$200 million.
07:10:13 **24** In order for me to do closing arguments, I'd
07:10:14 **25** like to have precise numbers that I can presents to

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07:10:17 **1** your Honor. And I am asking the witness who has
07:10:20 **2** knowledge and presented it to you in May so that I
07:10:24 **3** make sure I use the correct number.
07:10:26 **4** I'm willing to bet that Ms. Matanle provided the
07:10:29 **5** \$16.5 billion number to Mr. Wallace. I ascribe no
07:10:33 **6** necessarily even error. I'm trying to clarify those
07:10:37 **7** numbers.
07:10:37 **8** THE COURT: I guess I'm still having trouble
07:10:40 **9** seeing how they're relevant to the operation of the
07:10:43 **10** Plan. I'll give you some latitude on this and see if
07:10:47 **11** it is relevant.
07:10:48 **12** BY MR. GREENWALD:
07:10:48 **13** **Q** All right. Ms. Matanle, as you're sitting here now,
07:10:51 **14** do you know what the par value was of the CDS
07:10:56 **15** contracts that were commuted as part of the bank
07:11:00 **16** settlement?
07:11:01 **17** **A** **My recollection is it was between 16 and 17. And I'm**
07:11:06 **18** **sure that when I did this that we tied the number to**
07:11:10 **19** **the facts at the time.**
07:11:12 **20** **Q** Okay. And when you made the statement in May, I'm
07:11:17 **21** sure that you believed that that was accurate;
07:11:19 **22** correct?
07:11:19 **23** **A** **Yes.**
07:11:20 **24** **Q** And I'm willing to bet that Mr. Wallace believed that
07:11:23 **25** 16.5 was accurate as well. I'm not suggesting that he

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07:11:26 **1** didn't.
07:11:27 **2** THE COURT: Isn't that hearsay?
07:11:30 **3** MR. GREENWALD: I'm sorry?
07:11:31 **4** THE COURT: You're the one who's raising the
07:11:33 **5** hearsay objection. But what Mr. Wallace said in a
07:11:36 **6** statement not before the Court apparently of some
07:11:40 **7** other New York proceeding. Wouldn't that be hearsay?
07:11:44 **8** MR. GREENWALD: Here's the next question.
07:11:45 **9** **Q** Do you know if Mr. Wallace got the CDS par value
07:11:48 **10** figure from you for use in his affidavit last Monday?
07:11:51 **11** **A** **I know he did not.**
07:11:52 **12** **Q** Okay. And do you know who he got it from?
07:11:54 **13** **A** **No.**
07:11:55 **14** **Q** Okay. The par value figure is different than the
07:12:02 **15** BlackRock mark-to-market estimate that was provided to
07:12:08 **16** AAC sometime in the first quarter of 2010; is that
07:12:12 **17** correct?
07:12:12 **18** **A** **It's different from what number?**
07:12:17 **19** **Q** The par value.
07:12:18 **20** **A** **The par value is different from the par value in the**
07:12:21 **21** **BlackRock?**
07:12:22 **22** **Q** I'm sorry. Strike that.
07:12:23 **23** You understand that AAC engaged BlackRock in 2010;
07:12:29 **24** correct?
07:12:30 **25** **A** **Yes.**

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07:12:30 **1 Q** And what did BlackRock do with regard to the CDS
07:12:35 **2** settlement?
07:12:37 **3** MR. SIMMONS: Your Honor, foundation.
07:12:40 **4** THE COURT: Well, I'll overrule that. Let me
07:12:43 **5** see where this is going.
07:12:45 **6** MR. GREENWALD: So I'll ask leading questions
07:12:48 **7** and see if we can get there, and if you've got a
07:12:50 **8** problem with the question, let me know.
07:12:52 **9 Q** BlackRock was retained in order to do an independent
07:12:56 **10** estimate of the exposure from the CDS transactions;
07:13:01 **11** correct?
07:13:01 **12 A** **Exposure to loss?**
07:13:03 **13 Q** Exposure to loss, correct?
07:13:05 **14 A** **Yes.**
07:13:05 **15 Q** And one of the things that they calculated was what
07:13:10 **16** the mark-to-market loss could be; is that correct?
07:13:12 **17 A** **Yes.**
07:13:13 **18 Q** And do you recall that that was approximately \$12.9
07:13:17 **19** billion?
07:13:18 **20 A** **Yes.**
07:13:18 **21 Q** How does the mark-to-market loss compare to the par
07:13:24 **22** exposure on the CDS contracts?
07:13:26 **23 A** **The par amount is simply the face amount of the**
07:13:29 **24** **contract. So there was -- if you were gonna lose**
07:13:36 **25** **everything, the mark-to-market loss would have been**

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07:13:38 **1** **\$16.7 billion.**
07:13:40 **2** MR. GREENWALD: And if your Honor --
07:13:41 **3** MR. SIMMONS: Your Honor, can I object to this
07:13:43 **4** line of testimony on relevance grounds? If this is
07:13:44 **5** going to the Liquidation Analysis, the Liquidation
07:13:47 **6** Analysis isn't even based on that par value. It's
07:13:50 **7** based on estimated loss. So if all these questions
07:13:53 **8** are going to par value, I have no idea why they're
07:13:57 **9** relevant.
07:13:58 **10** THE COURT: What is the relevance?
07:13:59 **11** MR. GREENWALD: No, no. I just want to make
07:14:00 **12** sure, is OCI representing that the Liquidation
07:14:03 **13** Analysis is based on loss projection, not on
07:14:05 **14** mark-to-market.
07:14:06 **15** MR. SIMMONS: Well, what --
07:14:08 **16** MR. GREENWALD: I'm asking.
07:14:09 **17** MR. SIMMONS: Ms. Matanle has no foundation to
07:14:11 **18** answer that question.
07:14:12 **19** MR. GREENWALD: I want to go back to the
07:14:13 **20** representation that was just made to find out if we
07:14:15 **21** can rely on it.
07:14:18 **22** MR. SIMMONS: What's -- yeah, this is argument.
07:14:22 **23** THE COURT: Of course it's argument.
07:14:24 **24** MR. SIMMONS: What's the question again?
07:14:27 **25** MR. GREENWALD: Please, could you, the court

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07:14:28 **1** reporter -- your Honor, I'd ask the court reporter to
07:14:30 **2** read OCI's statement back into the record or read it
07:14:33 **3** out loud so that we can hear it. I'm sorry. What's
07:14:43 **4** your name?
07:14:43 **5** MR. SIMMONS: Mr. Simmons.
07:14:44 **6** MR. GREENWALD: Yeah. Could you read
07:14:45 **7** Mr. Simmons' statement regarding the Liquidation
07:14:50 **8** Analysis being based on projected loss, not on
07:14:53 **9** mark-to-market?
07:14:57 **10** Again, I would still say, your Honor, that the
07:14:58 **11** question is -- is he representing that it's based on
07:15:01 **12** estimated loss as opposed to mark-to-market damages?
07:15:05 **13** MR. SIMMONS: No. That's not what I said. You
07:15:07 **14** can read back my statement.
07:15:09 **15** MR. GREENWALD: That's fine.
07:15:09 **16** THE COURT REPORTER: I'm not sure what statement
07:15:16 **17** you're referring to.
07:15:16 **18** MR. SIMMONS: Well, I can just restate it.
07:15:16 **19** This whole line of questioning is going to net
07:15:18 **20** par value, and that's not what the Liquidation
07:15:21 **21** Analysis is based on. It's based on estimated losses.
07:15:24 **22** THE COURT: All right. Sustain the objection.
07:15:39 **23** BY MR. GREENWALD:
07:15:39 **24 Q** Ms. Matanle, when did you first learn that AFG was
07:15:42 **25** gonna be filing for bankruptcy?

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07:15:45 **1 A** **They've been speaking about filing for bankruptcy for**
07:15:50 **2** **several quarters, so I'm certainly aware of that.**
07:15:54 **3 Q** Are you aware that and ad hoc committee of creditors
07:16:00 **4** was negotiating with OCI and with AFG? Is that
07:16:04 **5** something that's within your area of knowledge?
07:16:06 **6 A** **No. Not really. There were rumors, and it's a small**
07:16:09 **7** **company. But it was nothing that I knew of firsthand.**
07:16:11 **8 Q** Okay. Are you familiar with, um, Net Operating Losses
07:16:18 **9** that are -- strike that.
07:16:20 **10** In general, do your job responsibilities involve
07:16:24 **11** dealing with Net Operating Losses?
07:16:26 **12 A** **No.**
07:16:26 **13 Q** You've testified that your job responsibilities do
07:16:42 **14** involve remediation?
07:16:44 **15 A** **Yes.**
07:16:44 **16 Q** And can you describe -- and this is different than
07:16:50 **17** your job of risk surveillance?
07:16:54 **18 A** **Remediation is one aspect of surveillance. It's**
07:16:58 **19** **really when surveillance moves beyond routinely**
07:17:02 **20** **looking after a performing credit and starts to then**
07:17:05 **21** **take action on a credit that's not performing.**
07:17:08 **22 Q** And with regard to taking action, what is your role in
07:17:14 **23** getting AAC to take action with regard to remediation?
07:17:18 **24 A** **I'm a senior credit officer, so, for example, the**
07:17:23 **25** **surveillance manager for the public finance book of**

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07:17:25 **1** **business reports to me. So if he has a troubled**
07:17:29 **2** **credit, he will come to me to, we'll discuss what his**
07:17:33 **3** **plans are, and in fact he'll then bring it to our**
07:17:36 **4** **commit -- standing committee to take credit decisions**
07:17:40 **5** **to approve his remediation plan for that particular**
07:17:43 **6** **credit.**
07:17:43 **7** **Q** Okay.
07:17:44 **8** **A** **And so on.**
07:17:45 **9** **Q** And without -- without talking about -- because in
07:17:47 **10** this case, remediation is part of the value of the
07:17:51 **11** Plan. I want to ask without -- and I want to be
07:17:55 **12** clear. I'm not asking you about any individual trust
07:17:58 **13** or individual remediation decision. I'm just going to
07:18:04 **14** ask you global questions both to anticipate an
07:18:08 **15** objection and because I understand that that's
07:18:09 **16** sensitive information.
07:18:11 **17** So in general, if one of the people who report to
07:18:15 **18** you report a problem at an action plan, what types of
07:18:19 **19** action can be taken to pursue remediation?
07:18:22 **20** **A** **You can forbear, for example. I mean, I think that's**
07:18:30 **21** **a frequently used method of remediating a credit.**
07:18:34 **22** **Because many of the transactions are set up so that**
07:18:37 **23** **they have embedded triggers and covenants, and if a**
07:18:41 **24** **transaction is deteriorating, it will automatically**
07:18:44 **25** **hit one of those trigger points. And that will cause**

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07:18:50 **1** **events to occur that were built into the transaction**
07:18:52 **2** **as a protective measure that probably we would want to**
07:18:57 **3** **think about before we'll allow them to have to happen**
07:19:00 **4** **automatically.**
07:19:01 **5** **Q** What other kinds of steps?
07:19:05 **6** **A** **In a health care credit, for example, we can go and**
07:19:10 **7** **meet with a not-for-profit hospital and meet up with**
07:19:14 **8** **its management, meet up with its board, try to bring**
07:19:17 **9** **in a financial consultant and ask the board to retain**
07:19:20 **10** **a financial consultant so as to come up with a plan**
07:19:23 **11** **for the hospital.**
07:19:24 **12** **Q** Okay. And, um, let's, if we could -- and I respect
07:19:29 **13** that because I asked an open-ended question. I don't
07:19:33 **14** think there are health care exposures involved in the
07:19:38 **15** Segregated Account; are there?
07:19:39 **16** **A** **I don't think there are.**
07:19:39 **17** **Q** Okay. So let's stay with the RMBS if we could.
07:19:47 **18** So with regard to the residential mortgage back
07:19:50 **19** exposure, someone comes to you with a problem on the
07:19:54 **20** underlying credit and says we need to take steps to
07:19:57 **21** remediate.
07:19:58 **22** Other than forbearance, are there other steps?
07:20:01 **23** And would it include, for example, litigation?
07:20:03 **24** **A** **Yes, it would.**
07:20:04 **25** **Q** Could you explain what those other alternatives are

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07:20:06 **1** and explain the type -- what's involved in litigation?
07:20:09 **2** **A** **Sure.**
07:20:11 **3** MR. SIMMONS: Object; compound.
07:20:13 **4** THE COURT: What?
07:20:14 **5** MR. SIMMONS: Object; compound, your Honor.
07:20:16 **6** MR. GREENWALD: Well, I will strike it then. I
07:20:18 **7** was trying to hurry up. I'm sorry. I'll slow it
07:20:21 **8** down. The best way to do it is step by step.
07:20:23 **9** Could you explain the other steps that you would
07:20:26 **10** do on an RMBS remediation other than forbearance and
07:20:31 **11** other than litigation? I'll leave that for later.
07:20:33 **12** **A** **Sure. You -- transferring servicing. How many**
07:20:37 **13** **examples do you want? Transferring servicing;**
07:20:39 **14** **requesting loan files; checking the, um -- checking**
07:20:44 **15** **the cash flows to make sure that the cash flows have**
07:20:48 **16** **been properly allocated.**
07:20:52 **17** **Q** Okay. And then perhaps seeing the loan files is part
07:20:58 **18** of an auditing activity?
07:21:01 **19** **A** **Yes.**
07:21:01 **20** **Q** And following the auditing activity, you might then
07:21:04 **21** evaluate whether or not to bring litigation?
07:21:07 **22** **A** **Yes. Long before you would litigate, there is plenty**
07:21:12 **23** **of opportunity to work with the servicer in order to**
07:21:16 **24** **put back loans.**
07:21:17 **25** **Q** And that's what I wanted to ask about. There's been a

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07:21:20 **1** distinction here in this proceeding between put-backs
07:21:25 **2** and cash recoveries. Could you explain what a
07:21:28 **3** put-back is and how that generates value in
07:21:32 **4** remediation?
07:21:33 **5** **A** **Sure. "Put-back" means that you, through the effort**
07:21:39 **6** **of getting loan files on the underlying home loans, if**
07:21:42 **7** **you find that some of the home loans were not properly**
07:21:47 **8** **put into the securitization to begin with because they**
07:21:51 **9** **failed to meet the underwriting criteria for the pool,**
07:21:55 **10** **the -- that home loan is then put back to whoever it**
07:21:59 **11** **was that put it into the deal. They have an**
07:22:02 **12** **obligation to either replace it with another home loan**
07:22:05 **13** **that does qualify or pay off the entire par amount of**
07:22:10 **14** **that underlying home loan so as to put cash back into**
07:22:14 **15** **the transaction.**
07:22:16 **16** **Q** And we've all recently read about foreclosure
07:22:21 **17** moratoriums and problems with robo-signing. Are those
07:22:25 **18** issues that relate to put-back activity?
07:22:30 **19** **A** **There are a lot of mortgage back articles. Are you**
07:22:35 **20** **talking about the foreclosure freeze? Is that what**
07:22:37 **21** **you mean?**
07:22:37 **22** **Q** The freeze. And I'm now asking someone who's actually
07:22:43 **23** in this industry. I read about it in the paper. I
07:22:45 **24** have read that the likelihood is that put-backs will
07:22:51 **25** likely increase as a result of the issues related to

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07:22:55 **1** documentation loans. And I'm wondering if that has
07:22:59 **2** increased the possibility of put-backs by Ambac to
07:23:04 **3** recover value for the Segregated Account?
07:23:07 **4 A We put back as many as we can get our hands on. I**
07:23:12 **5 mean, it's, you know, critical to our job.**
07:23:14 **6 Q** Now, let me -- and we'll tie this down now
07:23:17 **7** specifically to the Disclosure Statement.
07:23:19 **8** If we could show Ms. Matanle Exhibit 27, I'm gonna
07:23:23 **9** draw your attention to some things directly to
07:23:26 **10** remediation.
07:23:33 **11** Do you have Exhibit 27?
07:23:45 **12 A Yes.**
07:23:46 **13 Q** Okay. I'm gonna draw your attention to page 61. But
07:23:59 **14** when I asked Commissioner Dilweg about this, I was
07:24:01 **15** told this was AAC's number and not the OCI's and I
07:24:05 **16** should ask someone from AAC, which is why I'm doing it
07:24:08 **17** now, your Honor.
07:24:09 **18** I want to draw your attention to the first full
07:24:12 **19** paragraph under Loss Reserves. Do you see -- do you
07:24:17 **20** see that?
07:24:17 **21 A Uh-huh (affirmative).**
07:24:18 **22 Q** The first sentence states, "As of June 30, 2010, total
07:24:23 **23** statutory loss reserves associated with defaulted
07:24:27 **24** Segregated Account policies were approximately \$1.7
07:24:32 **25** billion, net of \$2 billion of benefits related to

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07:24:36 **1** projected R and W remediation recoveries relating to
07:24:40 **2** ongoing representation and warranty breaches in
07:24:44 **3** certain RMBS transactions implying total policy claims
07:24:48 **4** associated with such policies of \$3.8 billion."
07:24:53 **5** Did I read that correctly?
07:24:55 **6 A Yes.**
07:24:55 **7 Q** So my question is, do you agree that as of June 30,
07:25:01 **8** 2010, AAC was projecting \$2 billion in benefits that
07:25:08 **9** would be recovered from reps and warranties
07:25:12 **10** remediation efforts by AAC?
07:25:15 **11 A That's correct.**
07:25:15 **12 Q** All right. That of that \$2 billion, is that a
07:25:20 **13** projection of cash recoveries -- or let me just ask
07:25:25 **14** that. Is that a projection of cash recoveries in the
07:25:28 **15** future?
07:25:28 **16 A Yes.**
07:25:28 **17 Q** So the put-back value that would be obtained would be
07:25:35 **18** over and above the \$2 billion?
07:25:36 **19 A No. Whether we pay fewer claims or get cash back, I**
07:25:41 **20 mean, I view cash as fungible, so the put-back**
07:25:44 **21 activities that we conduct roll to the \$2 billion of**
07:25:50 **22 recoveries that you see here.**
07:25:51 **23 Q** Okay. I'm trying to -- because a distinction has been
07:25:54 **24** made between the two, I'm wondering if the \$2 billion
07:25:57 **25** was the total of put-back plus cash or if it was only

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07:26:01 **1** one or the other.
07:26:02 **2** Is it your testimony that \$2 billion was as of
07:26:05 **3** June 30th the estimate of the total value of put-back
07:26:08 **4** plus cash recoveries?
07:26:09 **5 A Yes.**
07:26:10 **6 Q** And as you're sitting here today, I assume that you
07:26:13 **7** can't estimate what the ratio is of put-back to cash
07:26:18 **8** recovery?
07:26:19 **9 A No.**
07:26:19 **10 Q** You haven't yet resolved some of those open issues.
07:26:28 **11** I want to show you Exhibit -- well, before I do
07:26:32 **12** this, one question. And let me see if I can find the
07:26:36 **13** reference.
07:26:37 **14** Yes. It says in that same sentence that the
07:26:42 **15** statutory loss reserves reflect -- let's see. I want
07:26:50 **16** to make sure I get this right.
07:26:51 **17** So the statutory loss reserves associated with the
07:26:56 **18** defaulted Segregated Account policies were
07:26:58 **19** approximately 1.7 billion. Do you see that?
07:27:01 **20 A In the first sentence?**
07:27:02 **21 Q** Right.
07:27:02 **22 A Yes.**
07:27:03 **23 Q** And then its net of \$2 billion in projected
07:27:08 **24** remediation?
07:27:09 **25 A Yes.**

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07:27:09 **1 Q** Does that mean that the statutory reserve takes into
07:27:14 **2** account the full value of the estimated remediation
07:27:18 **3** recoveries?
07:27:20 **4** MR. SIMMONS: Your Honor, objection; foundation.
07:27:21 **5** It's not clear that -- while Ms. Matanle is from
07:27:24 **6** Ambac, it's not clear that she had input in coming up
07:27:27 **7** with these numbers.
07:27:28 **8** THE COURT: Lay the foundation, counsel.
07:27:30 **9 Q** Yeah. Let me just ask a question.
07:27:32 **10** Do you understand statutory reserving?
07:27:34 **11 A Very little. I'm much more knowledgeable with GAAP**
07:27:37 **12 reserving.**
07:27:37 **13 Q** Okay. Well, in a GAAP reserve, do you take into
07:27:40 **14** account estimated recoveries on the R and W
07:27:44 **15** remediation?
07:27:45 **16 A Yes, we do.**
07:27:46 **17 Q** And if you know, how does statutory loss reserving
07:27:52 **18** differ with regard to this issue?
07:27:57 **19** MR. SIMMONS: Your Honor, I think we just
07:27:58 **20** established it doesn't.
07:28:00 **21** MR. GREENWALD: If the answer is "I don't know,"
07:28:02 **22** the answer is "I don't know."
07:28:02 **23 A I don't know.**
07:28:03 **24** THE COURT: Sustain the objection.
07:28:04 **25 Q** Let me give you one additional document, which is

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07:28:07 **1** Exhibit 60 -- I believe 48. It's Ambac's 3Q.
 07:28:26 **2** For the record, what has previously been marked as
 07:28:45 **3** Objectors' Exhibit 48 is the Q3 Financial Highlights
 07:28:50 **4** 2010 Quarterly Operating Supplement. Ms. Matanle,
 07:28:56 **5** have you seen this document before?
 07:28:57 **6 A Yes.**
 07:28:58 **7 Q** Okay. And in what context did you see it?
 07:29:03 **8 A I usually go and print it off as soon as it's posted**
 07:29:07 **9 and take a look at it. And people that work for me**
 07:29:10 **10 are involved in some of the numbers that are in here.**
 07:29:12 **11 Q** So your group is responsible for some of the inputs
 07:29:16 **12** into that document?
 07:29:17 **13 A We -- Finance prepares this document. But we check**
 07:29:22 **14 some of the information for correctness.**
 07:29:25 **15 Q** Okay. Particularly because it's a publicly-traded
 07:29:29 **16** company?
 07:29:30 **17 A Yeah. Exactly.**
 07:29:31 **18 Q** People have to sign. You have to trust people to
 07:29:36 **19** check the numbers?
 07:29:36 **20 A Yes.**
 07:29:36 **21 Q** Let me draw your attention to page 2 to begin with.
 07:29:45 **22** There are a series of bullet points there. I want to
 07:29:47 **23** draw your attention to the last bullet point on page
 07:29:50 **24** 2.
 07:29:50 **25** It says that, "Statutory surplus of Ambac

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07:29:54 **1** Assurance Corporation, AAC, decreased to approximately
 07:29:58 **2** \$912 million at September 30, 2010, from \$1.5 billion
 07:30:05 **3** at June 30, 2010, driven primarily by statutory loss
 07:30:10 **4** and loss expenses." Do you see that?
 07:30:11 **5 A Yes.**
 07:30:12 **6 Q** Do you have any understanding of the cause of the
 07:30:16 **7** decrease in the statutory surplus during that quarter?
 07:30:21 **8** MR. SIMMONS: Your Honor, objection. She just
 07:30:24 **9** testified she's not familiar.
 07:30:26 **10** MR. GREENWALD: I think she can testify herself
 07:30:27 **11** whether she knows. That was the question.
 07:30:28 **12** THE COURT: I think I can hear whether she
 07:30:30 **13** knows.
 07:30:31 **14 Q** So Ms. Matanle, my question is do you understand what
 07:30:35 **15** the cause was for the decrease in the statutory
 07:30:40 **16** surplus?
 07:30:43 **17 A I haven't looked at the numbers behind this. I know**
 07:30:46 **18 what might cause a reduction associated with statutory**
 07:30:50 **19 loss reserves.**
 07:30:50 **20 Q** Okay. Could you testify to that, please?
 07:30:53 **21** MR. SIMMONS: Wait. Objection, your Honor.
 07:30:54 **22** That's asking for speculation.
 07:30:55 **23** THE COURT: That's a lack of foundation. She
 07:30:57 **24** hasn't looked at the numbers. This whole thing
 07:31:01 **25** becomes speculation.

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07:31:01 **1 Q** Did the company have negative events between June 30th
 07:31:05 **2** and September 30th that might have caused a decrease
 07:31:09 **3** in reported statutory reserves? I just want to --
 07:31:17 **4 A What I know about statutory loss reserves that differs**
 07:31:20 **5 from GAAP loss reserves is that losses for statutory**
 07:31:25 **6 purposes will only appear when the underlying**
 07:31:29 **7 transaction first defaults. So our GAAP reserve will**
 07:31:35 **8 include reserves for all of our reserve transactions,**
 07:31:38 **9 whether or not they've yet defaulted.**
 07:31:40 **10 Q** So for GAAP accounting, if you have internally
 07:31:44 **11** determined that a loss is reasonably possible in the
 07:31:49 **12** future, you have to take that into account in your
 07:31:52 **13** reserving?
 07:31:53 **14 A Yes.**
 07:31:53 **15 Q** But under statutory reserving, you don't until the
 07:31:57 **16** loss actually occurs?
 07:32:01 **17 A Until the first default occurs, at which point you**
 07:32:02 **18 move your entire future expected loss into the -- onto**
 07:32:07 **19 the statutory reserve.**
 07:32:08 **20 Q** So under GAAP accounting, you look at FAS 5 to
 07:32:18 **21** determine whether to report that as a reserve?
 07:32:23 **22 A Financial guarantors use FAS 163.**
 07:32:27 **23 Q** Is it similar to FAS 5?
 07:32:30 **24 A I don't know.**
 07:32:31 **25** MR. SIMMONS: Objection; relevance, your Honor.

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07:32:32 **1** THE COURT: Sustained.
 07:32:33 **2 Q** Let me turn your attention to page 4.
 07:32:36 **3** If you look at the second full paragraph that
 07:32:43 **4** starts "Loss and loss expense reserves," and this
 07:32:48 **5** doesn't say statutory, and I want to ask you if you
 07:32:50 **6** know about it. But let me read it into the record,
 07:32:53 **7** and then I'll have a couple of questions.
 07:32:54 **8** It states that, "Loss and loss expense reserves
 07:32:57 **9** for all RMBS insurance exposures as of September 30,
 07:33:02 **10** 2010, were \$2.746 billion." And I'm gonna stop here.
 07:33:12 **11** Can I read that as \$2.746 billion as opposed to \$2,746
 07:33:19 **12** million? How would you prefer that I read that?
 07:33:21 **13 A Me?**
 07:33:22 **14 Q** Yeah. Well, I don't want to be objectionable.
 07:33:24 **15** Let me start over, and I'll read it exactly as
 07:33:27 **16** it's written.
 07:33:28 **17** "Loss and loss expense reserves for all RMBS
 07:33:32 **18** insurance exposures as of September 30, 2010, were
 07:33:38 **19** \$2,746 million, including \$1,074.2 million
 07:33:45 **20** representing claims presented but not paid since March
 07:33:49 **21** 24, 2010, due to the claims moratorium. RMBS reserves
 07:33:55 **22** as of September 30, 2010, are net of \$2,395.5 million
 07:34:03 **23** of estimated net remediation recoveries."
 07:34:06 **24** Do you see that?
 07:34:06 **25 A Yes.**

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07:34:06 **1 Q** Okay. Here is the simple question.

07:34:09 **2** It appears to me that the \$2.3955 billion of

07:34:19 **3** estimated net remediation is larger than the \$2

07:34:22 **4** billion that I showed you from the Disclosure

07:34:26 **5** Statement.

07:34:26 **6 A** **That's correct.**

07:34:27 **7 Q** Okay. Can you explain why the number is larger in the

07:34:32 **8** 3Q report provided by Ambac?

07:34:37 **9 A** **A couple of reasons. This will include all of the**

07:34:41 **10** **remediation recoveries, whether or not the deal has**

07:34:44 **11** **defaulted. And I don't know. And in addition, there**

07:34:50 **12** **are different discount rates that are used, I believe.**

07:34:52 **13 Q** Okay. Can you explain that?

07:34:54 **14 A** **For GAAP purposes, we're required to discount future**

07:34:58 **15** **cash flows at the risk-free rate, and for statutory**

07:35:02 **16** **purposes we're required to use a 5.1 percent discount**

07:35:06 **17** **rate.**

07:35:06 **18 Q** All right. And I will not ask you the question about

07:35:24 **19** statutory surplus, which appears later.

07:35:26 **20** Could you turn to page 9 of this exhibit.

07:35:38 **21** And if you don't know, just tell me, but if you go

07:35:45 **22** down to Variable Interest Entity Liabilities, the

07:35:50 **23** second line down is Long-Term Debt. And if you look

07:35:54 **24** over at December 31, 2009, and compare it to September

07:35:58 **25** 30, 2010, it's grown by more than \$14 billion. And

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07:36:05 **1** I'm wondering if that's something that's within your

07:36:07 **2** area of knowledge?

07:36:08 **3 A** **Not specifically, no.**

07:36:10 **4 Q** Okay. Do you have any firsthand information that

07:36:13 **5** would be relevant to that change to explain how that

07:36:17 **6** occurred?

07:36:18 **7 A** **I don't -- no. I may know more about what VIEs are**

07:36:23 **8** **than I would about why it changed.**

07:36:25 **9 Q** Okay. And because I don't think that the Court's

07:36:29 **10** indulgence would go as far as me to ask the scholarly

07:36:34 **11** question -- or my asking your scholarly information

07:36:36 **12** about what that means, I'm not going to do it. But

07:36:39 **13** thank you.

07:36:39 **14** All right. We can put that document aside.

07:36:43 **15** Ms. Matanle, you testified that the information

07:36:50 **16** that you provided to OCI was very sensitive in nature;

07:36:54 **17** correct?

07:36:54 **18 A** **Yes.**

07:36:55 **19 Q** And that it would be difficult to disclose some or all

07:37:01 **20** of that information to policyholders because of the

07:37:05 **21** nature of how sensitive it was; correct?

07:37:08 **22 A** **Yes.**

07:37:08 **23 Q** Now, in the CDS bank deal, it's true, isn't it, that

07:37:14 **24** the CDS counterparty banks entered into

07:37:18 **25** confidentiality agreements with AAC?

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07:37:21 **1 A** **Yes.**

07:37:21 **2 Q** And were those in the nature of professional-eyes-only

07:37:26 **3** confidentiality agreements?

07:37:28 **4** MR. SIMMONS: Object. That calls for a legal

07:37:30 **5** conclusion, your Honor.

07:37:30 **6** THE COURT: That would. And have you seen 'em,

07:37:32 **7** or do you know anything about 'em?

07:37:33 **8 A** **Not very much.**

07:37:35 **9 Q** Well, here's the question. AAC did enter into

07:37:38 **10** confidentiality agreements to negotiate a commutation

07:37:42 **11** with the 14 CDS counterparty banks; correct?

07:37:45 **12 A** **Yes.**

07:37:46 **13 Q** Now, the information was just as sensitive to disclose

07:37:49 **14** to the banks as it would be to other financial

07:37:51 **15** institutions, I assume.

07:37:56 **16** THE COURT: Do you know?

07:37:57 **17 A** **I -- I don't really -- I don't recall the extent of**

07:38:02 **18** **what was even shared with the banks.**

07:38:04 **19 Q** Okay. Have you ever personally been involved in

07:38:09 **20** entering into a confidentiality agreement in order to

07:38:12 **21** negotiate with a party?

07:38:13 **22 A** **Yes. In my years of --**

07:38:17 **23 Q** Right. Of course.

07:38:17 **24 A** **Yeah.**

07:38:19 **25 Q** Well, the question here is, is there any reason why

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07:38:23 **1** AAC couldn't have entered into professional-eyes-only

07:38:27 **2** confidentiality agreements so that just financial

07:38:31 **3** advisors and lawyers would have access to some small

07:38:35 **4** portion of the sensitive information in order to

07:38:36 **5** facilitate negotiating a resolution of the short-tail

07:38:43 **6** claims that were presented to Ambac?

07:38:47 **7** MR. SIMMONS: Object; vague and calls for

07:38:49 **8** speculation.

07:38:51 **9** THE COURT: Sustained. And lack of foundation.

07:38:57 **10** MR. GREENWALD: Your Honor, if I could have one

07:39:06 **11** second, I think I may very well be done. And last

07:39:08 **12** time I made good on my promise, so let me see if I can

07:39:11 **13** do it again.

07:39:24 **14** (Pause)

07:39:24 **15** MR. GREENWALD: And your Honor, I made good one

07:39:25 **16** more time. I have no further questions.

07:39:27 **17** THE COURT: All right. The clerk will tally

07:39:29 **18** that as a point for Mr. Greenwald.

07:39:32 **19** All right. It's about 4:40. Um, perhaps it

07:39:44 **20** would be better if we start with Mr. Bentley tomorrow

07:39:47 **21** morning.

07:39:48 **22** MR. BENTLEY: Whichever way your Honor prefers.

07:39:50 **23** THE COURT: Well, are you -- yours are usually

07:39:52 **24** long and detailed.

07:39:55 **25** MR. BENTLEY: And tedious.

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07:40:02 **1** UNIDENTIFIED ATTORNEY: Can't we get it over
07:40:04 **2** with, your Honor, please.
07:40:05 **3** MR. BENTLEY: I can tell your Honor that while
07:40:06 **4** my cross may not be any more entertaining than my
07:40:09 **5** prior crosses were, it will be shorter.
07:40:13 **6** MR. SIMMONS: We have no objection, your Honor.
07:40:18 **7** THE COURT: All right. And again, as was the
07:40:20 **8** case with Mr. Greenwald, you'll be held to that.
07:40:26 **9** MR. BENTLEY: That's fair, your Honor.
07:40:26 **10** **CROSS EXAMINATION**
07:40:27 **11** **BY MR. BENTLEY:**
07:40:27 **12** **Q** Good afternoon, Ms. Matanle. For the record, I'm
07:40:31 **13** Philip Bentley, and I represent the LVM Bondholders.
07:40:34 **14** I'm going to ask you a relatively short number of
07:40:38 **15** questions all relating to one aspect of your
07:40:41 **16** testimony, and that is you testified that it would be
07:40:46 **17** very difficult -- and I'm paraphrasing -- very
07:40:50 **18** difficult for policyholders or other parties to
07:40:55 **19** acquire the same sort of detailed understanding that
07:41:00 **20** Ambac and OCI have as to the potential losses under
07:41:06 **21** Ambac's various policies. Correct?
07:41:08 **22** **A Yes.**
07:41:12 **23** **Q** That in order to acquire that sort -- that same sort
07:41:15 **24** of policy-by-policy understanding of potential losses,
07:41:21 **25** that would require reviewing very detailed claim files

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07:41:26 **1** and other documents and extensive discussions with
07:41:30 **2** employees, among other things. Is that a fair
07:41:34 **3** summary?
07:41:35 **4** **A Yes.**
07:41:35 **5** **Q** Isn't it true, though, that short of that sort of
07:41:44 **6** comprehensive examination, um, there are a lot of
07:41:48 **7** things that could be turned over to policyholders that
07:41:53 **8** wouldn't involve anything like the sort of burden you
07:41:57 **9** were describing. True?
07:41:59 **10** MR. SIMMONS: Object. Vague, your Honor.
07:42:01 **11** THE COURT: Yes, I agree. Sustain the
07:42:04 **12** objection.
07:42:05 **13** **Q** Um, well, this is -- this was simply a prelude to a
07:42:09 **14** few examples.
07:42:10 **15** The Plan rests on a lot of projections and a lot
07:42:15 **16** of estimates of loss potential, claims-paying
07:42:19 **17** resources, and so forth; correct?
07:42:20 **18** **A Yes.**
07:42:21 **19** **Q** And those estimates were developed by OCI working very
07:42:26 **20** closely with Ambac; correct?
07:42:31 **21** MR. SIMMONS: Object; foundation.
07:42:33 **22** THE COURT: Do you know?
07:42:34 **23** **A What was the lead-in?**
07:42:37 **24** **Q** The projections on which the Plan is based were
07:42:45 **25** involved by OCI working in conjunction with Ambac.

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07:42:48 **1** Fair?
07:42:48 **2** THE COURT: Do you know?
07:42:52 **3** **A We develop projections of loss, and then we hand over**
07:42:56 **4** **our view of loss to the OCI, and then they take it**
07:43:00 **5** **where they want to take it. And it's -- I wouldn't**
07:43:03 **6** **say we collaborate in the preparation of the loss**
07:43:06 **7** **projections.**
07:43:08 **8** **Q** I think, like you said, you're roommates, but not
07:43:12 **9** partners.
07:43:13 **10** **A Exactly.**
07:43:13 **11** **Q** Now, you were here during Mr. Peterson's testimony
07:43:16 **12** earlier this week?
07:43:18 **13** **A Yes.**
07:43:18 **14** **Q** Including during his cross-examination by myself and
07:43:22 **15** many other parties?
07:43:23 **16** **A Yes.**
07:43:23 **17** **Q** And do you recall he gave quite a bit of testimony
07:43:29 **18** about the various different sorts of data that he
07:43:32 **19** reviewed in order to form his own judgment as to loss
07:43:36 **20** potential, claims-paying resources, and so on?
07:43:40 **21** **A Yes.**
07:43:40 **22** **Q** Let me ask you first about what he reviewed to form a
07:43:47 **23** judgment with respect to Ambac RMBS loss exposures.
07:43:53 **24** MR. SIMMONS: Object to foundation, your Honor.
07:43:57 **25** MR. BENTLEY: It's just a preamble, your Honor.

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07:43:59 **1** THE COURT: Well, of course, it's always a
07:44:00 **2** preamble. But it still has to have a foundation.
07:44:03 **3** MR. BENTLEY: I'm happy to withdraw it and
07:44:05 **4** proceed with another question.
07:44:06 **5** THE COURT: All right. Accepted. Proceed.
07:44:08 **6** BY MR. BENTLEY:
07:44:08 **7** **Q** Do you recall Mr. Peterson's testimony that in
07:44:12 **8** developing his own view of Ambac's RMBS loss exposures
07:44:17 **9** he reviewed cash flow estimates for each deal?
07:44:22 **10** **A If you say he said that, yes, I was here.**
07:44:27 **11** THE COURT: Do you remember him saying that?
07:44:29 **12** MS. MATANLE: Not specifically.
07:44:30 **13** THE COURT: There you go. She doesn't remember
07:44:32 **14** it.
07:44:33 **15** MR. BENTLEY: All right. Fair enough.
07:44:35 **16** **Q** Did Ambac make available to Mr. Peterson and his
07:44:38 **17** colleagues at OCI cash flow estimates for each deal?
07:44:42 **18** **A Yes.**
07:44:43 **19** **Q** And in what form can those estimates be found?
07:44:48 **20** **A Spreadsheets, gigantic spreadsheets.**
07:44:51 **21** **Q** Spreadsheets. Okay.
07:44:53 **22** Now, let me ask you for a moment to look at
07:44:58 **23** Exhibit 41. Do you have that available?
07:45:27 **24** If you have the document, let me ask you to turn
07:45:29 **25** to page 24 and look at -- and look at the first

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07:45:34 **1** paragraph under the heading "First Lien RMBS." Tell
07:45:39 **2** me if you have that --
07:45:45 **3 A I do.**
07:45:45 **4 Q** -- in front of you.
07:45:45 **5** Do you see in the first sentence, it refers to a
07:45:47 **6** "regression-based loan level model?"
07:45:50 **7 A Yes.**
07:45:50 **8 Q** Are you familiar with that model?
07:45:52 **9 A At a very high level.**
07:45:55 **10 Q** Was that developed by Ambac?
07:46:01 **11** MR. SIMMONS: Object; foundation, your Honor.
07:46:02 **12** She didn't prepare this document. This document is
07:46:04 **13** from OCI.
07:46:05 **14** THE COURT: Well, let's find out whether she's
07:46:07 **15** familiar with it. If she didn't prepare it, she
07:46:10 **16** didn't prepare it.
07:46:11 **17** MR. SIMMONS: This -- your Honor, I'm sorry, but
07:46:13 **18** this document, this exhibit, doesn't refer to where
07:46:15 **19** this document comes from. There's no way from looking
07:46:17 **20** at this exhibit to determine whether or not it was a
07:46:20 **21** document she would have been involved in.
07:46:21 **22** THE COURT: Well --
07:46:23 **23** MR. BENTLEY: If I may, your Honor.
07:46:24 **24** THE COURT: No. Just a moment. Let's let her
07:46:26 **25** answer.

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07:46:27 **1** MS. MATANLE: Could you repeat the question?
07:46:28 **2 Q** Sure. You testified a moment ago that on a very high
07:46:32 **3** level, you're familiar with a regression-based loan
07:46:35 **4** level model?
07:46:36 **5 A Yes.**
07:46:36 **6 Q** With respect to RMBS exposures?
07:46:39 **7 A Yes.**
07:46:40 **8 Q** Who developed that model?
07:46:41 **9 A The model was developed by, um, an independent vendor**
07:46:47 **10 who we owned for a short time.**
07:46:57 **11 Q** What's the name of that vendor?
07:46:59 **12 A Rangemark.**
07:47:02 **13 Q** And did Ambac work with that vendor in developing this
07:47:06 **14** model?
07:47:06 **15 A No.**
07:47:06 **16 Q** Did the vendor use Ambac data in developing the model?
07:47:13 **17 A They had the model. It was a model that they used in**
07:47:16 **18 the normal course of their business.**
07:47:18 **19 Q** Did they input Ambac data into the model?
07:47:22 **20 A Yes.**
07:47:23 **21 Q** And in fact, did they input into the model
07:47:28 **22** approximately two million -- data concerning
07:47:32 **23** approximately two million mortgage loans?
07:47:34 **24 A I don't know.**
07:47:37 **25 Q** Now, you see this document says -- this document is

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07:47:41 **1** speaking to the projections that OCI developed, not to
07:47:46 **2** Ambac's projections; correct? That's the point that
07:47:49 **3** counsel just made.
07:47:50 **4 A Yes.**
07:47:50 **5 Q** So you understand that this is a model that OCI used
07:47:58 **6** in connection with developing the estimates on which
07:48:01 **7** the Plan is based?
07:48:02 **8 A Yes.**
07:48:03 **9 Q** Okay. Now, would you agree that if you were -- let me
07:48:10 **10** start again.
07:48:11 **11** Imagine for a moment that you're not employed by
07:48:15 **12** Ambac, but instead, you're a consultant and you're
07:48:18 **13** hired by one of the policyholders in this case who
07:48:20 **14** says we'd like you to come in and help us understand
07:48:23 **15** Ambac's loss exposures. Can you imagine that for a
07:48:26 **16** moment?
07:48:26 **17 A Uh-huh (affirmative).**
07:48:27 **18 Q** I know that may be hard.
07:48:29 **19 A Yes.**
07:48:29 **20 Q** Now, would you want to see that model?
07:48:36 **21 A Yes.**
07:48:36 **22 Q** You'd think the model would be helpful to assist your
07:48:42 **23** understanding of Ambac's RMBS loss exposures; correct?
07:48:47 **24** MR. SIMMONS: Your Honor, foundation. Calls for
07:48:49 **25** speculation.

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07:48:49 **1** THE COURT: It does. Sustain the objection.
07:48:51 **2 Q** Well, you have worked -- you have worked on the
07:48:56 **3** development of estimates of loss exposures within
07:49:01 **4** Ambac; have you?
07:49:02 **5 A Yes.**
07:49:03 **6 Q** And have you found useful in doing that reliance on
07:49:11 **7** models?
07:49:12 **8 A Yes.**
07:49:12 **9 Q** Models roughly similar to the model that's described
07:49:16 **10** here?
07:49:17 **11 A And others, yes.**
07:49:18 **12 Q** Among other things, models that would incorporate, um,
07:49:25 **13** cash flow estimates for each RMBS deal?
07:49:29 **14 A Yes.**
07:49:29 **15 Q** And if you were, again, hypothetically, employed by a
07:49:34 **16** policyholder as a consultant and asked to assess
07:49:37 **17** Ambac's potential loss exposures, you would find it
07:49:40 **18** helpful to have access to that model; correct?
07:49:43 **19 A Helpful, yes.**
07:49:46 **20 Q** Okay. Please turn to page 25 of Exhibit 41. You see
07:50:00 **21** at the top of the page there's a discussion of how
07:50:05 **22** loss exposures with respect to second-lien RMBS were
07:50:11 **23** developed?
07:50:11 **24 A Yes.**
07:50:11 **25 Q** Was a model used in the development of those loss

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07:50:16 **1** exposures?

07:50:17 **2 A Yes.**

07:50:18 **3** MR. SIMMONS: Your Honor, just for a second. We

07:50:20 **4** need to establish a foundation of whether she knows or

07:50:22 **5** not. It's not clear from her answer that she actually

07:50:25 **6** knows whether it was used.

07:50:26 **7** THE COURT: Do you know if it was used?

07:50:28 **8** MS. MATANLE: Yes, it was used.

07:50:28 **9** THE COURT: All right. Overruled.

07:50:30 **10 Q** And do you know something about the nature of that

07:50:32 **11** model?

07:50:33 **12 A Yes, at a high level.**

07:50:35 **13 Q** Tell us what you know at a high level.

07:50:37 **14 A It's what we call a roll-rate model, which means that**

07:50:41 **15 it deals with, um, a particular deal and looks at the**

07:50:47 **16 aging of the different home loans in that pool and**

07:50:52 **17 makes a judgment about how many of those delinquent**

07:50:56 **18 loans will stay delinquent as opposed to getting**

07:51:00 **19 prepaid or returning to be paid on a current basis.**

07:51:05 **20 So it rolls forward the future performance of all of**

07:51:09 **21 the different categories of the home loan borrowers.**

07:51:14 **22 Q** And does that model incorporate historical data from

07:51:18 **23** Ambac's files?

07:51:21 **24** THE COURT: Do you know?

07:51:22 **25 Q** Among other things?

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07:51:24 **1** THE COURT: Do you know?

07:51:28 **2 Q** Let me try it a different way.

07:51:30 **3 A No.**

07:51:30 **4 Q** Let me try it a different way.

07:51:33 **5** Does it incorporate data from Ambac's files?

07:51:35 **6 A Of course. Yes.**

07:51:36 **7 Q** What sorts of data?

07:51:37 **8 A Well, it takes the -- it takes the loan that we have,**

07:51:41 **9 knows our exposure in the loan. It takes information**

07:51:47 **10 from third-party vendors that we import in order to**

07:51:48 **11 then know the characteristics of the loan in question**

07:51:51 **12 to be able to model it.**

07:51:52 **13 Q** Now, let me again ask -- put you in a difficult

07:51:56 **14** position of imagining you're a consultant for one of

07:51:59 **15** the policyholders. If you were asked to assess

07:52:03 **16** Ambac's potential second-lien RMBS loss exposures,

07:52:08 **17** would you find it helpful to have access to that

07:52:11 **18** model?

07:52:12 **19** MR. SIMMONS: Your Honor, calls for speculation.

07:52:13 **20** Also, relevance. They want documents. We know they

07:52:16 **21** want documents. That's all this is designed to

07:52:18 **22** obtain. There's no point in having this testimony.

07:52:20 **23** THE COURT: It's speculation, and I will sustain

07:52:23 **24** that objection. And to ask her to place herself as a

07:52:29 **25** consultant when she has this information from Ambac I

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07:52:35 **1** think inherently skews your question.

07:52:41 **2** MR. BENTLEY: Let me ask a different question

07:52:42 **3** then, your Honor.

07:52:43 **4 Q** Ms. Matanle, did I hear you correctly a moment ago

07:52:46 **5** that you have from time to time worked on the

07:52:49 **6** development of estimates of loss exposures in Ambac's

07:52:55 **7** different books?

07:52:55 **8 A Yes.**

07:52:56 **9 Q** And in doing that, you've used models; correct?

07:53:01 **10 A Yes. My staff has used models.**

07:53:04 **11 Q** And those models incorporate a lot of data from

07:53:07 **12** Ambac's files; correct?

07:53:09 **13 A Yes.**

07:53:09 **14 Q** And you find it helpful to be able to consult those

07:53:14 **15** models and work with them?

07:53:15 **16 A We do our best to use models that we think are the**

07:53:19 **17 right models. But people can differ on what the right**

07:53:23 **18 models are to model our exposures.**

07:53:26 **19 Q** Sure. You do your best?

07:53:27 **20 A Yeah.**

07:53:28 **21 Q** And if somebody wanted to understand these exposures,

07:53:31 **22** it would be helpful for them to see the model;

07:53:34 **23** correct?

07:53:34 **24 A There are many RMBS models available to model loss.**

07:53:38 **25 Q** But a model that incorporates data in Ambac's

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07:53:45 **1** possession would be very helpful; wouldn't it?

07:53:48 **2** THE COURT: Again, that's speculation. You're

07:53:50 **3** asking her -- I'm not sure where you're placing her in

07:53:55 **4** terms of making that evaluation. There's so many

07:53:59 **5** unknowns in the person who is looking. What are they

07:54:04 **6** looking for? What are their backgrounds?

07:54:09 **7** That's an objection I think that's been

07:54:11 **8** continuing, and I'll sustain it. It's highly

07:54:14 **9** speculative.

07:54:15 **10** BY MR. BENTLEY:

07:54:15 **11 Q** Let me ask you to turn to another document.

07:54:18 **12** And Judge, we're actually getting close to the end

07:54:21 **13** here. This is the last document I'll be using.

07:54:24 **14** Exhibit 27, the Disclosure Statement.

07:54:27 **15** Do you have it, or are you waiting?

07:54:47 **16 A I do.**

07:54:47 **17 Q** Can you please turn to Exhibit C. And I'd like you to

07:54:52 **18** look at not the cover page, but the first page that

07:54:54 **19** has several paragraphs on it.

07:54:56 **20 A Where are you?**

07:54:57 **21 Q** Exhibit C. And not the cover page, but the page that

07:55:03 **22** follows the cover page. And specifically, look at the

07:55:09 **23** second paragraph under the heading "Statement of

07:55:12 **24** Operations." Do you see this paragraph which relates

07:55:15 **25** to the reinvestment rate?

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07:55:17 **1 A Yes.**
 07:55:17 **2 Q** Now, this reinvestment rate relates to Ambac's
 07:55:27 **3** investment portfolio; correct?
 07:55:30 **4 A I don't know.**
 07:55:32 **5 Q** Well, take a moment and read the preceding paragraph.
 07:55:35 **6** And I think it's pretty clear from the context.
 07:55:41 **7** (Pause)
 07:55:54 **8** MR. SIMMONS: Your Honor, there's a still a
 07:55:55 **9** foundation objection here. And this is OCI's
 07:55:57 **10** document. This wasn't prepared by Ambac.
 07:56:00 **11** MR. BENTLEY: I'm still at the level of preamble
 07:56:03 **12** questions, so you might want to wait until I ask a
 07:56:05 **13** more substantive question.
 07:56:12 **14 Q** Do you see that the first paragraph following the
 07:56:13 **15** heading "Statement of Operations" refers to investment
 07:56:17 **16** income on AAC's existing investment portfolio?
 07:56:21 **17 A You're on the second paragraph?**
 07:56:23 **18 Q** Second paragraph on the page, yeah.
 07:56:26 **19 A The one that starts, "The reinvestment rate is assumed**
 07:56:29 **20 to be 3.6 percent."**
 07:56:31 **21 Q** I'm sorry. I was referring to the second paragraph on
 07:56:33 **22** the page. It's the one that precedes the one you were
 07:56:37 **23** just --
 07:56:37 **24 A Oh. The first paragraph in section 1?**
 07:56:39 **25 Q** Exactly.

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07:56:39 **1 A Okay. I'm there.**
 07:56:40 **2 Q** Okay. You see it refers to investment income on AAC's
 07:56:45 **3** existing investment portfolio?
 07:56:48 **4 A Yes.**
 07:56:49 **5** THE COURT: Can you get close to the mic,
 07:56:51 **6** please.
 07:56:52 **7** MR. BENTLEY: Yes. Sorry, your Honor.
 07:56:55 **8 Q** And do you see it then goes on to discuss in the next
 07:56:58 **9** paragraph different assumed reinvestment rates?
 07:57:03 **10 A Yes.**
 07:57:03 **11 Q** Now, are you familiar on a high level with the nature
 07:57:09 **12** of Ambac's investment portfolio?
 07:57:12 **13 A Yes.**
 07:57:13 **14 Q** You're aware that it consists of a number of different
 07:57:15 **15** types of securities, including municipal bonds, RMBS
 07:57:20 **16** investments, and others?
 07:57:21 **17 A Yes.**
 07:57:21 **18 Q** And do you recall Mr. Peterson's testimony on that
 07:57:24 **19** general topic over the past day or two?
 07:57:29 **20 A Yes.**
 07:57:29 **21 Q** And do you recall his testimony that the reinvestment
 07:57:34 **22** rate referred to in this paragraph is what one might
 07:57:37 **23** call a roll-up of reinvestment rates from the
 07:57:41 **24** different categories of investment in Ambac's overall
 07:57:47 **25** investment portfolio?

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07:57:50 **1 A Yes.**
 07:57:51 **2 Q** Now, to your knowledge, the numbers that were used,
 07:57:57 **3** the calculations used to derive these blended
 07:58:00 **4** reinvestment rates have not been produced to
 07:58:04 **5** policyholders; have they?
 07:58:06 **6** THE COURT: Do you know?
 07:58:07 **7 A I don't know.**
 07:58:08 **8 Q** Okay. And in order to -- in order for policyholders
 07:58:12 **9** to form an independent judgment as to whether these
 07:58:16 **10** projections of reinvestment rates are reliable, it
 07:58:20 **11** would be helpful for them to see the backup underlying
 07:58:24 **12** this data; wouldn't it?
 07:58:26 **13** MR. SIMMONS: Your Honor, calls for speculation.
 07:58:27 **14** THE COURT: Sustained.
 07:58:30 **15** MR. BENTLEY: That's all I have, your Honor.
 07:58:31 **16** THE COURT: All right. That will complete the
 07:58:33 **17** proceedings for today. We'll resume tomorrow morning
 07:58:36 **18** at 9:00. And I guess you'll be with us and on the
 07:58:42 **19** stand first tomorrow.
 07:58:43 **20** MR. BLOOMGARDEN: Your Honor, just a scheduling
 07:58:45 **21** issue before we adjourn today that I just want --
 07:58:47 **22** THE COURT: All right. You can step down.
 07:58:51 **23** MR. BLOOMGARDEN: Craig Bloomgarden. I just
 07:58:51 **24** want to -- it's my understanding that we have Mr.
 07:58:58 **25** -- we have a witness to present tomorrow after we

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07:59:00 **1** finish the current witness, Mr. Schacht, and then that
 07:59:07 **2** we are then looking to close evidence tomorrow and
 07:59:10 **3** that we will be back here on the 29th for closing
 07:59:13 **4** arguments before your Honor.
 07:59:14 **5** THE COURT: That's what the schedule is, yes.
 07:59:17 **6** MR. BLOOMGARDEN: Yes. Okay. Thank you.
 07:59:34 **7** (Proceedings adjourned at 5:00 p.m.)
8
9 STATE OF WISCONSIN)
) ss:
10 COUNTY OF DANE)
11
12 We, LINDA M. FLAKNE and ANN M. ALBERT, Court
13 Reporters for Dane County Circuit Court, do hereby
14 certify that we took in machine shorthand the
15 above-entitled proceedings held on the 18th day of
16 November, 2010; we reduced the same to a written
17 transcript and that it is a true and correct
18 transcript of our notes and the whole thereof.
19 Dated this 18th day of November, 2010.
20
21
22
23 _____
 Linda M. Flakne, RMR
 Court Reporter
24
25 _____
 Ann. M. Albert, RMR, CRR
 Court Reporter

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