STATE OF WISCONSIN CIRCUIT COURT DANE COUNTY

In the Matter of the Rehabilitation of:

Segregated Account of Ambac Assurance Corporation

Case No. 10 CV 1576

REHABILITATOR'S SUPPLEMENTAL BRIEF IN SUPPORT OF MOTION TO ENFORCE INJUNCTION AGAINST ASSURED GUARANTY CORP. AND ASSURED GUARANTY RE LTD.

The Rehabilitator files this supplemental brief in support of his motion to enforce this Court's Injunction against Assured Guaranty Corp. ("Assured-US") and Assured Guaranty Re Ltd. ("Assured-Bermuda") (collectively, "Assured").

The factual background is set forth in detail in the accompanying May 27, 2011 Affidavit of Michael B. Van Sicklen ("Van Sicklen Aff."), and is discussed in summary form below.

ARGUMENT

At the May 25, 2011 motion hearing, the centerpiece of Assured's argument was an assertion that it previously made in its May 9 opposition brief and in supporting affidavits: that the Rehabilitator's counsel's representations in a June 15, 2010 e-mail to Assured's counsel "***induced*** the Assured Reinsurers' ***reasonable reliance in deciding not to object to the Injunction or the Plan***," and that "the Assured Reinsurers[] ***relied to their detriment*** on these statements since they . . . could have used those objections to clarify their rights, avoiding this motion." (Assured Opp'n at 27 (emphasis added).)

However, Assured's position, and its affiants' description of the facts, is inaccurate. Specifically, on June 21, 2010—six days *after* the June 15 e-mail from Rehabilitator's counsel that Assured purportedly relied upon—Assured's counsel sent the Rehabilitator's counsel a set of

objections to the Injunction that Assured planned to file, captioned "Motion and Limited Objection By Assured Guaranty Corp. [Assured-US] and Assured Guaranty Re Ltd. [Assured-Bermuda] To Order For Temporary Injunctive Relief" (hereinafter, the "Objections"). (*See* Van Sicklen Aff., Exs. A (June 21, 2010 email) & B (Objections)).)

In its Objections, Assured-US and Assured-Bermuda explained the basis for its challenge to paragraph 1 of the Injunction as follows:

> The Assured Guaranty Entities act as reinsurers under a number of reinsurance agreements with Ambac Assurance Corporation ("Ambac"). The Assured Guaranty Entities understand that these reinsurance contracts are not currently part of the segregated account that is the subject of these proceedings (the "Segregated Account"). However, some of the policies that the Assured Guaranty Entities have reinsured have been assigned to the Segregated Account. Furthermore, the assets and liabilities of the Segregated Account apparently are subject to change. ***Since the Segregated Account includes some policies that are reinsured by the Assured Guaranty Entities, the Assured Guaranty Entities require confirmation that the exercise of their contractual rights under the reinsurance policies is not enjoined.*** To comply with the limited 90-day objection rights set forth in the Injunction, the Assured Guaranty Entities are ***required to raise these issues now***.

(*Id.*, Ex. B (Objections at 2 (emphasis added)).)

Assured's counsel told the Rehabilitator's counsel that it intended to file the Objections on June 22, 2010—the deadline for filing objections to the Injunction—unless the Rehabilitator agreed to extend the deadline for challenging the Injunction (or consent to holding the Objections once filed in abeyance). (*Id.* ¶¶ 7-8.) The Rehabilitator's counsel said that the Rehabilitator would not consent to extending the deadline for Assured to file the Objections pertaining to the two "ceded" reinsurance contracts (under which Assured-US and Assured-Bermuda are the reinsurers) at issue in the present dispute, but would consider a narrow extension of the deadline

MADI_2692142

as to the two "assumed" reinsurance contracts (under which Ambac is the reinsurer).[1] (Van Sicklen Aff. ¶ 8.) Assured agreed to drop its Objections to the Injunction in regard to the two ceded contracts (now at issue) if the Rehabilitator would execute a letter agreement that extended the deadline in regard to a narrow statutory offset issue pertaining to the two assumed contracts (that are not now at issue). (*Id.* ¶ 9.)

In a letter agreement reached later that day, June 22, 2010, the Rehabilitator agreed to extend the time for Assured to file objections regarding the statutory offset issue pertaining to the assumed reinsurance contracts, but the letter agreement does not permit Assured to file objections with respect to the scope of paragraph 1 of the Injunction or to the ceded reinsurance contracts. (*See id.*, Ex. C (June 22, 2010 letter agreement).) Assured thereafter filed no objections to the Injunction. (*Id.* ¶ 10.)

As discussed below, Assured's Objections highlight a number of inaccuracies in the position Assured argued to this Court.

I. ASSURED WAS NOT INDUCED TO FOREGO ITS OBJECTION TO PARAGRAPH 1 OF THE INJUNCTION BASED ON THE JUNE 15, 2010 EMAIL FROM THE REHABILITATOR'S COUNSEL

At the May 25, 2011 hearing, Assured told this Court that the June 15, 2010 email from the Rehabilitator's counsel—which Assured's counsel displayed on a large demonstrative exhibit at the hearing—was clear and, in reliance on that email, Assured did not object to or seek clarification with respect to the scope of the Injunction.

Assured's affiants told the same story. Alexander R. Cochran, an attorney for Assured at Debevoise & Plimpton LLP, stated in his affidavit that:

[1] As explained in the Van Sicklen Affidavit (at ¶ 6), the "ceded" and "assumed" reinsurance contracts are separate and distinct from each other, and the present dispute only relates to the two "ceded" contracts.

> After receiving the June 14 telephone conversation and Mr. Fitzgerald's June 15 email, advising the Assured Reinsurers that it was the Rehabilitator's position that their contractual rights would not be affected under the Injunction, the Assured Reinsurers ultimately decided not to object to the Injunction.

(Affidavit of Alexander R. Cochran Aff. ¶ 10.)[2]

Assured's story is not accurate. Specifically, on June 21, 2010, six days *after* the June 15 email from the Rehabilitator's counsel to Attorney Cochran, Assured sent the Rehabilitator's counsel the cover email (on which Attorney Cochran was copied) and the attached Objections that Assured intended to file. (*See* Van Sicklen Aff., Exs. A (June 21, 2010 email) & B (Objections).) Those Objections show that, even with the Rehabilitator's counsel's June 15 email in hand, Assured and its counsel believed that, with respect to underlying policies that were allocated to the Segregated Account, and for which Assured provided reinsurance, Assured "***require[d] confirmation*** [from this Court] ***that the exercise of their contractual rights under the reinsurance policies is not enjoined***." (Van Sicklen Aff., Ex. B (Assured Objections at 2 (emphasis added)).)

There are two takeaways from the timing and content of Assured's Objections. *First*, on June 21 and 22, 2010, Assured and its counsel did not attribute the significance or meaning to the June 15 email that they now claim. If they had, then there would have been no reason for Assured to include the above objection to paragraph 1 of the Injunction in its Objections.[3]

---

[2] *See also* Affidavit of James M. Michener ¶¶ 10-11 (incorrectly describing sequence of events and omitting any discussion of written and oral communications between Assured's counsel and the Rehabilitator's counsel on June 21 and 22, 2010).

[3] Assured's Objections contain no reference to the June 15, 2010 email from the Rehabilitator's counsel to Assured's counsel. (*See generally* Van Sicklen Aff., Ex. B.) Nor was the June 15 email mentioned by Assured's counsel in the multiple communications with the Rehabilitator's counsel on June 22, 2010. (*Id.* ¶ 10.)

Second, the reason Assured did not file its Objections was not because it relied on the June 15 email, as its affiants and counsel now suggest. Instead, as reflected in the June 22, 2010 letter agreement, Assured agreed to drop its objection to the Injunction in regard to the two ceded reinsurance contracts (which now are the subject of the present dispute), if the Rehabilitator would execute a letter agreement, which extended the deadline in regard to a narrow statutory offset issue pertaining to the two assumed reinsurance contracts (which are not now at issue). (*See* Van Sicklen Aff. ¶¶ 8-10 & Ex. C (June 22, 2010 letter agreement).)

II. ASSURED'S OBJECTIONS ALSO CONTRADICT A NUMBER OF ITS OTHER ARGUMENTS

Although Assured's Objections were not filed, they were sufficiently final that Assured's counsel sent them to the Rehabilitator's counsel the night before the June 22, 2010 deadline for objecting to the Injunction. Those Objections highlight a number of inconsistencies in Assured's position.

For example, the Objections show that Assured understood that the proper forum in which to seek clarification with respect to the scope of paragraph 1 of the Injunction was this Court, and that the time to do so was within the 90-day period permitted under the Injunction. In the words of Assured's Objections: "To comply with the limited 90-day objection rights set forth in the Injunction, the Assured Guaranty Entities ***are required to raise these issues now***." (Van Sicklen Aff., Ex. B (Objections at 2 (emphasis added)).)

In its Objections, Assured also acknowledged the broad remedial purpose and scope of the Injunction:

> Section 645.05(1) of the Wisconsin Statutes provides that this Court may issue injunctions and restraining orders to suspend the conduct of further business and the transfer of assets, to stay the continued prosecution of pending actions, and otherwise to prevent interference with the rehabilitator's work. The purpose of any such injunction (***like the purpose of the automatic stay in a***

MADI_2692142

> ***bankruptcy case***) is to ***centralize, with this Court, the control over the assets of the entity that is the subject of a rehabilitation proceeding, and to centralize the filing and prosecution of claims "to maintain the integrity of the proceeding."*** *See* Laws of Wis. (1967), ch. 89, p. 235.

(*Id.*, Ex. B (Objections at 3 (emphasis added)).)

The above-quoted statement by Assured contradicts a number of the arguments it made to this Court. *First*, this statement conflicts with the position that Assured's counsel took at the May 25 hearing, when he asserted that the Injunction entered in this action was not analogous to the automatic stay entered in bankruptcy cases.

Second, the above-quoted statement also contradicts Assured's counsel's argument at the May 25 hearing that there was no statutory basis under Wisconsin law to reverse-preempt the Federal Arbitration Act under the McCarran-Ferguson Act analysis. As Assured itself noted in its Objections, WIS. STAT. § 645.05(1) provides the broad statutory basis for the Injunction.

Third, the above-quoted statement shows that Assured—having failed to timely object to paragraph 1 of the Injunction, and having acknowledged in its Objections the importance of centralizing any challenges to the Injunction before this Court—had no legitimate basis to ignore paragraph 1 of the Injunction and to file a collateral lawsuit in New York state court to force arbitration.

Finally, with respect to Assured's argument that this Court lacks personal jurisdiction over Assured-Bermuda, Assured's Objections were prepared with the intent that they would be filed on behalf of both Assured-US ***and*** Assured-Bermuda. (*See* Van Sicklen Aff., Ex. B (Objections at 1).) The Objections contain no reference to any alleged lack of personal jurisdiction over Assured-Bermuda (or any reservation of rights). Thus, but for the discussions between Assured's counsel and the Rehabilitator's counsel on June 22, 2010, the Objections presumably would have been filed on behalf of Assured-Bermuda in this proceeding.

CONCLUSION

For the reasons stated, the Rehabilitator's motion should be granted, and an order should be entered, declaring that Assured has violated paragraphs 1 and 7 of the Injunction, declaring that Assured has breached the reinsurance agreements with Ambac, and requiring Assured to satisfy all unpaid obligations under the reinsurance agreements, including but not limited to payments related to the issuance of surplus notes.

Dated this 27th day of May, 2011

FOLEY & LARDNER LLP

By: ______________________

Michael B. Van Sicklen, SBN 1017827
Naikang Tsao, SBN 1036747
Matthew R. Lynch, SBN 1066370

150 East Gilman Street
Post Office Box 1497
Madison, Wisconsin 53701
Telephone: (608) 257-5035
Facsimile: (608) 258-4258

Attorneys for Commissioner of Insurance of the State of Wisconsin, as Rehabilitator of the Segregated Account of Ambac Assurance Corporation

STATE OF WISCONSIN CIRCUIT COURT DANE COUNTY

In the Matter of the Rehabilitation of:

Segregated Account of Ambac Assurance Corporation

Case No. 10 CV 1576

AFFIDAVIT OF MICHAEL B. VAN SICKLEN

STATE OF WISCONSIN)
) ss.
COUNTY OF DANE)

Michael B. Van Sicklen, being first duly sworn on oath deposes and states as follows:

1. I am a partner in Foley & Lardner LLP and am one of the lawyers representing the Rehabilitator in the above-captioned proceeding. This affidavit is based on personal knowledge and information.

2. Attached as **Exhibit A** is a true and correct copy of an email dated June 21, 2010 sent at 7:55 p.m. to my partner Kevin Fitzgerald by an attorney for Assured Guaranty Corp. and Assured Guaranty Re Ltd. (collectively "Assured") at Debevoise & Plimpton LLC, with an attached "Motion and Limited Objection By Assured Guaranty Corp. and Assured Guaranty Re Ltd. To Order For Temporary Injunctive Relief" (hereinafter, the "Objections"). The June 21 email and attached Objections were copied to other lawyers for Assured at the Debevoise law firm and its local counsel at Quarles & Brady, as well as two of my other colleagues at Foley & Lardner LLP.

3. Attached as **Exhibit B** is a true and correct copy of Assured's Objections to the Injunction that was attached to the June 21, 2010 email (Exhibit A hereto). My colleagues promptly forwarded the June 21 email and the Objections to my attention because I was handling

all proceedings in this Court pertaining to objections by parties-in-interest to the Injunction entered by this Court on March 24, 2010.

4. On the morning of June 22, 2010, my partner Kevin Fitzgerald and I called Assured's local counsel on this matter, Don Schott. June 22, 2010 was the expiration of the 90-day deadline specified in the March 24, 2010 Injunction for any party to file objections to the Injunction. There might have been other attorneys for Assured on the call, but I do not recall anyone else being a vocal participant.

5. In our telephone call with Mr. Schott on the morning of June 22, 2010, Mr. Fitzgerald and I discussed Assured's Objections (attached hereto as Exhibit B).

6. Assured has two different types of reinsurance contracts with Ambac:

> First, Assured is a party to two "ceded" reinsurance contracts with Ambac. Those two "ceded" contracts, which were not allocated to the Segregated Account, are the subject of the present court dispute. Under these "ceded" contracts, Ambac ceded responsibility for certain liabilities in the Segregated Account for which Assured Guaranty Corp. and Assured Guaranty Re Ltd. (referred to at the court hearing as "Assured-US" and "Assured-Bermuda") assumed liability as the reinsurers.
>
> Second, Assured-US also is a party to two "assumed" reinsurance contracts that were allocated to the Segregated Account as referenced at Exhibit F(1) and (2) of the March 24, 2010 Plan of Operation for the Segregated Account filed with this Court. (Assured-Bermuda is not a party to the "assumed" contracts.) Under these "assumed" contracts, Ambac assumed liability as reinsurer.

These two groups of reinsurance contracts are separate and distinct from each other and unrelated.

7. We informed Mr. Schott that the Rehabilitator disagreed with the Objections and was disappointed that Assured said it intended to file such an objection given that the Rehabilitator was scheduled to go to court the very next day, June 23, 2010, in support of his

motion to commute the Weinstein Company policy which, if granted, would result in a substantial payment of cash and surplus notes to be split by Assured and another counterparty.

8. Mr. Schott inquired on behalf of Assured as to whether the Rehabilitator would extend the deadline for filing the Objections or whether the Objections could be filed and then court proceedings on it held in abeyance. We indicated that the Rehabilitator would not consent to extending the deadline for Assured to file the Objections pertaining to the two ceded reinsurance contracts (which now are the subject of the present dispute), but would consider a narrow extension of the deadline for challenging the Injunction until September 3, 2010 as to the two "assumed" reinsurance agreements in the Segregated Account (which are not now at issue) in regard to the exercise of certain statutory offset rights. We also indicated that the Rehabilitator would not consent to holding the Objections in abeyance.

9. Assured agreed to drop its Objection to the Injunction in regard to the two "ceded" contracts presently at issue if the Rehabilitator would execute a letter agreement that extended the deadline in regard to a narrow statutory offset issue pertaining to the two "assumed" contracts in the Segregated Account.

10. Attached as **Exhibit C** is a true and correct copy of the June 22, 2010 letter agreement, which the Rehabilitator entered into with the Deputy General Counsel for Assured as indicated above. Assured never filed an objection after the letter agreement extension expired on September 3, 2010 in regard to the assumed contracts, and never filed an objection to the injunction in regard to the two "ceded" contracts now at issue. In the multiple email and phone communications I had with Assured's counsel on June 22, 2010, there was no mention by Assured about my partner's June 15 email the prior week.

11. In reliance on Assured agreeing to drop its Objection to the Injunction as it related to the two ceded reinsurance contracts now at issue, I went to Darlington the next day to seek this Court's approval of the commutation of the Weinstein Company policy. Through a different lawyer, James Bartzen of the Boardman Suhr law firm, Assured Guaranty Corp. appeared at that hearing and supported the Rehabilitator's motion, which was granted.

Dated this 27th day of May, 2011.

Michael B. Van Sicklen

Subscribed and sworn to before me
this 27 day of May, 2011.

Patricia M Wright
Notary Public, State of Wisconsin.
My Commission: 7/14/13

MADI_2693054.1

EXHIBIT A

Van Sicklen, Michael B.

Subject: FW: Ambac / Assured Guaranty

Attachments: dpny-23216370-v5-Motion and Limited Objection to Ambac Injunction.DOC

-----Original Message-----
From: Dunham, Wolcott B. [wbdunham@debevoise.com]
Sent: Monday, June 21, 2010 7:55 PM
To: Fitzgerald, Kevin G.
Cc: Wiles, Michael E.; Kaas, Brian S.; Oberdeck, Andrew A.; Cochran, Alexander R.; Toman, William J.; Schott, Donald K.
Subject: Ambac / Assured Guaranty

<<dpny-23216370-v5-Motion and Limited Objection to Ambac Injunction.DOC>> Kevin,

Thank you. For our short call tomorrow (Tuesday) morning at 9 am Central, 10 am Eastern, please use the dial-in number that appears below. The call will include Assured's Wisconsin counsel, Quarles & Brady.

As background for the call, I am attaching the Motion and Limited Objection that Assured plans to file.

Dick

Wolcott B. Dunham, Jr.
Debevoise & Plimpton LLP

Please dial:
1 888 684 9991 (North American toll free)
+1 719 785-4910 (International)
Passcode: 212 909 6595

EXHIBIT B

STATE OF WISCONSIN | CIRCUIT COURT | DANE COUNTY

In the Matter of the Rehabilitation of:

Segregated Account of Ambac Assurance Corporation

Case No. 10 CV 1576

MOTION AND LIMITED OBJECTION BY ASSURED GUARANTY CORP. AND ASSURED GUARANTY RE LTD. TO ORDER FOR TEMPORARY INJUNCTIVE RELIEF

Assured Guaranty Corp. and Assured Guaranty Re Ltd. (collectively, the "**Assured Guaranty Entities**") hereby submit this motion to modify and limited objection to the terms of the "Order for Temporary Injunctive Relief," dated March 24, 2010 (the "**Injunction**").

Nature of the Objection

The Assured Guaranty Entities express no opinion as to the authority for the establishment of the segregated account that is the subject of these proceedings or the other issues that have been the focus of most (if not all) of the objections that have been filed. Instead, the Assured Guaranty Entities submit this objection to address certain provisions of the Injunction that are overly broad in scope and that are improper. Those provisions are:

(a) The 90-day limit on the ability of interested parties to object to any provision of the Injunction or to seek relief from its terms (which is set forth in paragraph 12 of the Injunction);

(b) The prohibition on the exercise of statutory offset rights (which is set forth in paragraph 7 of the Injunction), which is contrary to the terms of Section 645.56(1) of the Wisconsin Statutes; and

(c) Limitations on the assertion of contractual rights (set forth in paragraph 4 of the Injunction), which go far beyond the stated purpose of preventing "ipso facto" terminations of existing contracts.

The grounds for the Assured Guaranty Entities' objections to each of these provisions are explained more fully below.

Nature of the Assured Guaranty Entities' Interests

The Assured Guaranty Entities act as reinsurers under a number of reinsurance agreements with Ambac Assurance Corporation ("**Ambac**"). The Assured Guaranty Entities understand that these reinsurance contracts are not currently part of the segregated account that is the subject of these proceedings (the "**Segregated Account**"). However, some of the policies that the Assured Guaranty Entities have reinsured have been assigned to the Segregated Account. Furthermore, the assets and liabilities of the Segregated Account apparently are subject to change. Since the Segregated Account includes some policies that are reinsured by the Assured Guaranty Entities, the Assured Guaranty Entities require confirmation that the exercise of their contractual rights under the reinsurance policies is not enjoined. To comply with the limited 90-day objection rights set forth in the Injunction, the Assured Guaranty Entities are required to raise these issues now.

In addition, the Assured Guaranty Entities have ceded business to Ambac under reinsurance agreements. The Assured Guaranty Entities understand that all such reinsurance (under which Ambac is reinsurer) has been assigned to the Segregated Account. To the extent that the Assured Guaranty Entities have ceded business to Ambac, the terms of the Injunction directly affect the Assured Guaranty Entities.

The Objections

I. The 90-Day Limit On Interested Parties' Rights to Object And To Seek Relief From The Injunction Is Improper

Section 645.05(1) of the Wisconsin Statutes provides that this Court may issue injunctions and restraining orders to suspend the conduct of further business and the transfer of assets, to stay the continued prosecution of pending actions, and otherwise to prevent interference with the rehabilitator's work. The purpose of any such injunction (like the purpose of the automatic stay in a bankruptcy case) is to centralize, with this Court, the control over the assets of the entity that is the subject of a rehabilitation proceeding, and to centralize the filing and prosecution of claims "to maintain the integrity of the proceedings." *See* Laws of Wis. (1967), ch. 89, p. 235. The statute makes clear that any injunction or restraining order is to be an interim one to preserve the status quo to the extent appropriate, and the issuance of any such order is subject to the provisions of Chapter 813 of the Wisconsin Civil Procedure Code.

In this case, however, the Injunction requested by the Rehabilitator includes a time limit on parties' rights to seek relief from the Injunction. Paragraph 12 of the Injunction provides, in relevant part:

> This Order shall remain effective until further order of the Court. If any interested parties believe any portion of this Order is unwarranted by the facts or the law, such parties may seek modification or dissolution of part or all of this Order by filing a written motion with this Court ***no later than 90 days following the issuance of this Order***.

See Injunction, ¶ 12 (emphasis added). Prior to filing this objection, the Assured Guaranty Entities sought confirmation from the Rehabilitator as to whether this provision of the Injunction really is intended to bar future requests by individual parties for relief from the stays and other restraints that are imposed by the Injunction. However, the Assured Guaranty Entities were told that no clarification or further information could be provided.

There exists no provision of the Wisconsin Statutes or the Wisconsin Civil Procedure Code that justifies the imposition of the time limit set forth in the Injunction, which effectively bars enjoined parties from petitioning this Court for relief from the Injunction (or modification of the terms of the Injunction) to the extent that future circumstances warrant that relief. The Assured Guaranty Entities believe that the time limit is contrary to common sense, to due process, and to the terms of the Wisconsin Statutes.

First, if any party is to be subjected to a continuing restraint – particularly one issued on a "preliminary" basis, that does not itself represent a rehabilitation plan or a final order having substantive effect – it is common sense that the party who is restrained should have a continuing right to petition the court for relief from that restraint based on circumstances that warrant such relief. Guidance may be found in Section 362 of the Bankruptcy Code, in which this concept is certainly embedded, as it provides for relief from the automatic stay at any time based on a showing of "cause" for such relief. *See* 11 U.S.C. § 362(d)(1).

Second, the issuance of a preliminary restraint, without permitting applications for modification or relief from its terms, would violate due process. Any continuing injunction is subject to modification as circumstances warrant. *See United States v. Swift & Co.*, 286 U.S. 106, 114-15 (1932) (confirming the inherent power of courts to modify injunctions, even when injunctions have been entered on a permanent basis); *see also Dombrowski v. Pfister*, 380 U.S. 479, 492 (1965) ("[D]istrict courts retain power to modify injunctions in light of changed circumstances"); *Ass'n For Retarded Citizens of North Dakota v. Sinner*, 942 F.2d 1235, 1239 (8th Cir. 1991) ("It is well settled that a district court retains authority under Rule 60(b)(5) to modify or terminate a continuing, permanent injunction if the injunction has become illegal or changed circumstances have caused it to operate unjustly"). An order which bars parties from

seeking such relief would deprive parties of their due process rights to petition the court for the exercise of modification powers that the court inherently must retain.

Third, the proposed time limit is not consistent with the Wisconsin Statutes or the Wisconsin Civil Procedure Code, each of which contemplate the issuance of temporary or preliminary restraints. The purpose of a temporary restraint or preliminary injunction, of the kind authorized by the statute, is "merely to preserve the relative positions of the parties until a trial on the merits can be held." *See Univ. of Tex. v. Camenish*, 451 U.S. 390, 396 (1981); *see also Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Grall*, 836 F. Supp. 428, 431 (W.D. Mich. 1993) (same). If parties cannot even seek relief from the Injunction, then the Injunction would not merely be a preliminary restraint at all. Instead, it would be the equivalent of a permanent order that alters substantive rights.

Certainly there can be no harm in permitting parties to make application to this Court for modification of the terms of the Injunction, or for relief from the Injunction to the extent it relates to such parties, based on any circumstances that warrant such modification or relief. Nor should there be any artificial restriction on the nature of the circumstances that warrant such relief. *See Board of Education of Oklahoma City Public Schools v. Dowell*, 498 U.S. 237, 247-49 (1991) (rejecting the argument that special circumstances or grievous harm needed to be shown to obtain modification of injunction, and approving the modification of an injunction based on a finding that the injunction was no longer needed); *Little Rock Sch. Dist. v. Pulaski County Special Sch. Dist. No. 1*, 949 F.2d 253, 258 (8th Cir. 1991) (same). The Assured Guaranty Entities therefore request that the Injunction be modified by the addition of the following paragraph and the use of the same general "cause" standard employed in the federal Bankruptcy Code:

Notwithstanding any other provision of this Order, any interested party shall have the right to seek relief from the provisions of this Order, or modification of the terms of this Order insofar as they relate to such interested party, upon a showing of cause.

II. The Proposed Limitation Of Offset Rights Would Violate Wisconsin Law

Section 645.56 of the Wisconsin Statutes provides as follows:

> (1) Setoffs allowed in general. Mutual debts or mutual credits between the insurer and another person in connection with any action or proceeding under this chapter shall be set off and the balance only shall be allowed or paid, except as provided in sub. (2).

The exceptions set forth in Section 645.56(2) are limited:

> (2) Exceptions. No setoff or counterclaim may be allowed in favor of any person where:
>
> (a) The obligation of the insurer to the person would not at the date of the filing of a petition for liquidation entitle the person to share as a claimant in the assets of the insurer;
>
> (b) The obligation of the insurer to the person was purchased by or transferred to the person with a view to its being used as a setoff;
>
> (c) The obligation of the person is to pay an assessment levied against the members or subscribers of the insurer, or is to pay a balance upon a subscription to the capital stock of the insurer, or is in any other way in the nature of a capital contribution; or
>
> (d) The obligation of the person is to pay premiums, whether earned or unearned, to the insurer.

See Wis. Stat. § 645.56.

Although the statute says clearly that virtually all offsets "shall" be made and that only "the balance" after offset shall be "paid or allowed," the Injunction nevertheless purports to bar offsets. Paragraph 7 of the Injunction provides:

> All persons and entities are enjoined and restrained from withholding or failing to pay or setting-off premiums ***or other payments (including without limitation recoveries, reimbursements, interest, deferred interest, and default interest)*** owed (or that would have been owed but for the occurrence

> of the Events or the financial condition of the Segregated Account, the Allocated Subsidiaries, or the Ambac General Account) to the Segregated Account, any Allocated Subsidiary or the Ambac General Account under or in connection with policies ***or contracts*** allocated to the Segregated Account, ***or contracts with an Allocated Subsidiary or any Transaction Documents associated therewith or related thereto***. . . . A party's withholding or set-off of premiums ***or payments owed under or in connection with any of the aforementioned documents*** may result in the future disallowance or decrease of such party's claims.

See Injunction, ¶ 7 (emphasis added).

The prohibition on offsets in paragraph 7 is directly contrary to the terms of Section 645.56 and is improper. This Court has authority under Section 645.05(1) to enjoin actions that could "prejudice" the Segregated Account, but by definition the assertion of offset rights that are explicitly granted and confirmed by Section 645.56 cannot be "prejudicial." The Assured Guaranty Entities therefore request that the Injunction be modified by the addition of the following language at the end of paragraph 7:

> Notwithstanding the provisions of this paragraph 7, nothing in this Order shall be construed to interfere with the exercise of statutory offset rights in accordance with Wis. Stat. § 645.56(1).

III. <u>The Limitations On The Assertion Of Contract Rights Is Overly Broad</u>

Paragraph 4 of the Injunction enjoins certain assertions of rights by policyholders and by counterparties to transactions or contracts. The motion in support of the Injunction explained that the purpose of this restriction is to mirror the provisions of the Bankruptcy Code that prohibit the enforcement of so-called "ipso facto" clauses: *i.e.*, provisions that purport to terminate or modify contract rights based solely on the fact that an insolvency proceeding has been commenced or based solely on the financial condition of the Segregated Account. *See* the "Brief in Support of Motion for Temporary Injunctive Relief" at 2, 9-11. However, the language

included in the Injunction goes far beyond the assertion of rights under "ipso facto" clauses.

Paragraph 4 provides:

> All policyholders and/or counterparties whose policies or contracts have been allocated to the Segregated Account, or who are counterparties to contracts with an Allocated Subsidiary (including without limitation, in each case noteholders and any other persons claiming by or through such policyholders and/or counterparties), are enjoined and restrained from terminating, ***collecting on, or claiming against*** -- or attempting to terminate, ***collect on, or claim against*** – such policies or contracts, or the transaction documents executed in connection with the issuance of such policies or contracts or related to such policies or contracts, on the basis of the Events (as defined below), or the financial condition of the Segregated Account, the Allocated Subsidiaries, or the Ambac General Account, regardless of the existence of any language in those policies, contracts or any other agreements that would otherwise require early termination. . . . As used herein, the term "Events" refers to the Proceedings ***and any acts taken or not taken or authorized to be taken pursuant thereto, including without limitation the failure of the Segregated Account, the Allocated Subsidiaries, or Ambac to pay amounts due under any policies, contracts, or other obligations that have been allocated to the Segregated Account or to which any of the Allocated Subsidiaries is a party.***

See Injunction, ¶ 4. By its terms, the foregoing language would permit the Rehabilitator to breach outstanding contracts with impunity. So long as the Rehabilitator's acts were "taken pursuant to" these Proceedings (as would be the case for any "act" by the Rehabilitator), policyholders and other contracting parties could do nothing.

The Assured Guaranty Entities do not object to temporary limits on the enforcement of true "ipso facto" clauses – though any such restraint should be temporary and, as noted above, should be subject to motions by affected parties seeking relief from the restraint, particularly since the Wisconsin Statutes do not bar such provisions. However, there is no justification for restraining the exercise of other contractual rights that parties may have. The Assured Guaranty Entities respectfully submit that paragraph 4 should be re-worded to delete all of the language that is highlighted in the foregoing excerpt.

Conclusion

The Assured Guaranty Entities respectfully request that the terms of the Injunction be modified in each of the ways set forth above, and that this Court grant such other and further relief as may be just and proper.

Dated: June __, 2010

QUARLES & BRADY LLP

____

Donald K. Schott, SBN 1010075
Matthew J. Splitek, SBN 1045592
33 East Main Street, Suite 900
P.O. Box 2113
Madison, Wisconsin 53703
(608) 251-5000

Michael E. Wiles
DEBEVOISE & PLIMPTON LLP
919 Third Ave
New York, New York 10022
(212) 909-6000
Attorneys for the Assured Guaranty Entities

EXHIBIT C

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, Governor
Sean Dilweg, Commissioner

Wisconsin.gov

125 South Webster Street • P.O. Box 7873
Madison, Wisconsin 53707-7873
Phone: (608) 266-3585 • Fax: (608) 266-9935
E-Mail: ociinformation@wisconsin.gov
Web Address: oci.wi.gov

Kimberly A. Shaul, Special Deputy Commissioner
Segregated Account of Ambac Assurance Corporation

June 22, 2010

Via E-Mail (RKastellec@assuredguaranty.com) and U.S. Mail

Richard Kastellec, Deputy General Counsel
Assured Guaranty Corp.
31 West 52nd Street - 28th Floor
New York, NY 10019

Re: *Segregated Account of Ambac Assurance Corporation (the "Segregated Account")*, Dane County, Wisconsin Circuit Court Case No. 10-CV-1576

Dear Mr. Kastellec:

I am writing to you in regard to the Order for Temporary Injunctive Relief which the Dane County, Wisconsin Circuit Court entered in regard to the Segregated Account on March 24, 2010 (the "Injunction Order"). June 22, 2010 is the present deadline for any policyholder or other party-in-interest to file any motion objecting to the Injunction Order becoming permanent.

Under Paragraph 15 of the Injunction Order, "the Rehabilitator may consent to actions or failure to act which would otherwise be enjoined or restrained by [the] Order." See also, Paragraph 13 which provides that the Injunction Order may be modified by "the consent of the Rehabilitator." Because the Injunction Order was entered at the request of the Commissioner for the benefit of the Rehabilitator's rehabilitation of the Segregated Account, the Rehabilitator and the office of the Wisconsin Commissioner of Insurance have taken, and shall continue to take, the position that the Rehabilitator may grant unilateral extensions or other adjustments to the deadline for filing objections with respect to the Injunction Order on such terms as the Rehabilitator deems just and appropriate under the circumstances, and may do so without seeking approval or leave of the Court.

You[1] have requested that the Rehabilitator grant you an extension of the deadline for filing a motion in regard to the Injunction Order from Tuesday, June 22, 2010 until the

[1] References to "you" and "your" shall mean the entity identified above as the addressee and below in the "Understood and Agreed" signature block, including all subsidiaries and affiliates of that entity.

close of business (Central Time) on Friday, September 3, in regard to the reinsurance agreements between you and Ambac Assurance Corporation and its affiliates which were allocated to the Segregated Account (the "Assured Reinsurance Agreements"). The purpose of the extension is to permit time for you and the Rehabilitator to discuss their present differences of opinion regarding the prohibition on the exercise of statutory offset rights (which is set forth in paragraph 7 of the Injunction), which you contend is contrary to the terms of Wis. Stat. § 645.56(1) with respect to the Reinsurance Agreements (the "Disagreement").

The Rehabilitator hereby agrees to your requested extension on the following four conditions:

1. While you may file a motion objecting to the Injunction Order in regard to the Assured Reinsurance Agreements prior to the extended deadline herein of September 3, 2010, you shall not do so sooner than August 16, 2010 and, as a courtesy, you shall provide the Rehabilitator with at least three (3) business days advance written notice of your intent to file such a motion prior to the extended deadline of September 3, 2010;

2. Any objection you file in the future with respect to the Injunction—during or after the extension period herein—shall be limited to the above-described Disagreement with respect to the Assured Reinsurance Agreements allocated to the Segregated Account;

3. During the extension period provided for herein, you shall make good faith efforts to meet and confer with the Rehabilitator and his designated representatives in regard to trying to reach a negotiated, mutually acceptable, long-term resolution of the Disagreement with respect to the Assured Reinsurance Agreements in relation to the Injunction Order; and

4. The extension accommodation provided herein is personal to you and does not apply to any other party claiming an interest in respect of the Assured Reinsurance Agreements or with respect to any other agreements.

If you are in agreement with the terms and conditions of the extension specified in this letter agreement, please note that understanding by signing below and returning the signed agreement to my attention. If we receive your signed copy of this letter agreement by no later than the close of the Dane County, Wisconsin Circuit Court's business day on June 22, 2010, you shall have the extension to the objection deadline described above, and the Rehabilitator hereby covenants and agrees that the Rehabilitator shall take no position before the rehabilitation Court to the contrary.

This letter agreement shall be without prejudice to the rights and positions of the parties to this agreement as to the merits, scope or length of the injunction and shall not be admissible in evidence, given to third parties (including any other policyholders involved

in the above-referenced rehabilitation proceeding), or made public in any respect other than to the narrow extent it might become necessary in the future to prove to a court the terms of the extension agreed to herein.

Very truly yours,

Kimberly A. Shaul
The Court-Appointed Special Deputy Commissioner of the Segregated Account of Ambac Assurance Corporation

cc: Michael Freed

Understood and Agreed:

____
Assured Guaranty Corp.

By: ____________________________
Its authorized representative

Title: Deputy General Counsel

Name in type: Philip R. Kastellec