COURT OF APPEALS OF WISCONSIN
DISTRICT IV

In the Matter of the Rehabilitation of:

Segregated Account of
Ambac Assurance Corporation,

Appeal No. 2010-AP-1291,
2010-AP-2022

TED NICKEL and OFFICE OF THE
COMMISSIONER OF INSURANCE,

Plaintiffs-Respondents,

AMBAC ASSURANCE,

Interested Party-Respondent,

v.

WELLS FARGO BANK/Trustee of
Bondholders, BANK OF NEW YORK
MELLON and DEUTSCHE BANK
NATIONAL TRUST COMPANY,

Defendants,

FEDERAL HOME LOAN MORTGAGE
CORPORATION,

Defendant-Petitioner-Co-Appellant,

AURELIUS CAPITAL MANAGEMENT
LP, FIR TREE, INC., KING STREET
CAPITAL MASTER FUND, LTD.,
KING STREET CAPITAL, L.P.,
MONARCH ALTERNATIVE CAPITAL,
LP and STONEHILL CAPITAL
MANAGEMENT LLC,

Defendants-Petitioners-Appellants,

EATON VANCE MANAGEMENT,

NUVEEN ASSET MANAGEMENT, RESTORATION CAPITAL MANAGEMENT, LLC, STONE LION CAPITAL PARTNERS, LP,

Defendants-Co-Appellants-Petitioners.

RMBS POLICYHOLDERS' RESPONSE IN OPPOSITION TO OCI'S AUGUST 5, 2011 LETTER TO THIS COURT

Bryan K. Nowicki
WI State Bar ID No. 1029857
Jessica Hutson Polakowski
WI State Bar ID No. 1061368
R. Timothy Muth
WI State Bar ID No. 1010710
Reinhart Boerner Van Deuren s.c.
22 East Mifflin Street, Suite 600
Madison, Wisconsin 53703
Telephone: (608) 229-2200
Facsimile: (608) 229-2100

Attorneys for Aurelius Capital Management, LP, Fir Tree, Inc., King Street Capital, L.P., King Street Capital Master Fund, Ltd., Monarch Alternative Capital LP, and Stonehill Capital Management LLC

Of Counsel:

David M. Greenwald
Michael T. Brody
Andrew J. Olejnik
Jenner & Block LLP
353 N. Clark Street
Chicago, Illinois 60654
Telephone: (312) 222-9350
Facsimile: (312) 840-7774

Patrick J. Trostle
Jenner & Block LLP
919 Third Avenue, 37th Floor
New York, New York 10022
Telephone: (212) 891-1665

Aurelius Capital Management, LP, Fir Tree, Inc., King Street Capital, L.P., King Street Capital Master Fund, Ltd., Monarch Alternative Capital LP, and Stonehill Capital Management LLC (collectively, the "RMBS Policyholders"), in their capacity as owners of or managers of funds that own residential mortgage-backed securities and other indebtedness insured by Ambac Assurance Corporation ("AAC"), submit this response in opposition to the Office of the Wisconsin

Commissioner of Insurance's ("OCI") August 5, 2011 letter to this Court ("August 5 Letter").

On May 3, 2011, this Court specifically ordered that "[n]o supplemental briefing in 10AP1291 and 10AP2022 will be allowed without a specific showing from a party as to why it is necessary." (Order, *Dilweg v. Wells Fargo Bank*, Nos. 2010AP1291, 2010AP2022, 2010AP2835, 2011AP300, and 2011AP561, at 13 (Wis. Ct. App. May 3, 2011).) OCI's August 5 Letter is nothing short of an attempt to circumvent this Order. In the guise of a letter providing the Court with supplemental authority pursuant to Wis. Stat. § 809.19(10), OCI attempts to supplement its response brief with new arguments and facts. The August 5 Letter is not only improper under the Court's May 3 Order, but the decisions cited also are irrelevant to this appeal.[1]

1. The Decisions Cited By OCI Are Irrelevant For Purposes Of This Appeal.

OCI's August 5 letter cites two decisions to support its argument that the RMBS Policyholders lack standing because they are not, according to OCI, policyholders: (1) the Circuit Court's January 24, 2011 Order confirming OCI's proposed Plan of Rehabilitation (the "Confirmation Order"), and (2) an inapplicable decision from a Chapter 11 bankruptcy case pending in the Bankruptcy Court for the

[1] To the extent the Court agrees with the RMBS Policyholders that the OCI's August 5 Letter is improper under the Court's May 3 Order, the RMBS Policyholders invite the Court to strike the August 5 Letter.

Southern District of New York. Neither of these decisions are relevant to the standing issues raised in the current appeal.

OCI criticizes the RMBS Policyholders for not specifically objecting to certain findings of fact and conclusions of law contained in the Circuit Court's Confirmation Order relating to the RMBS Policyholders' standing to participate in the Circuit Court proceedings as policyholders. (Aug. 5 Ltr. at 3.) In doing so, OCI ignores several key facts. First, the Circuit Court's Confirmation Order does not find – as OCI would like this Court to believe – that the RMBS Policyholders lacked standing to challenge the CDS Settlement or the rehabilitation plan. Instead, the Circuit Court found that the RMBS Policyholders had a right to participate in the rehabilitation proceedings as "parties-in-interest, but not as policyholders." (R.556:58 (¶ 9).) Second, as part of this appeal the RMBS Policyholders appealed their right to intervene as parties in the Circuit Court proceedings. OCI has pointed to no authority (and the RMBS Policyholders are not aware of any such authority) requiring the RMBS Policyholders to later appeal – for a second time – their right to intervene as parties when the intervention question is already pending before this Court. Third, the RMBS Policyholders objected to and appealed the *entire* Confirmation Order in 2011AP561. Whether the RMBS Policyholders later appeal one particular paragraph in the Confirmation Order thus has no bearing on this appeal of the denial of the RMBS Policyholders' motion to intervene.

Similarly, OCI's reliance on *In re Innkeepers USA Trust*, 448 B.R. 131 (Bankr. S.D.N.Y. 2011), is misplaced. As outlined in Section I of the RMBS Policyholders'

opening brief, the issue of standing requires the application of Wisconsin law. The *Innkeepers* court applied a federal bankruptcy provision not at issue in this case. *See Inkeepers*, 448 B.R. at 141 (applying Section 1109(b) of the Bankruptcy Code). As such, the *Innkeepers* case is inapplicable. The *Innkeepers* case is further inapplicable because the creditors in that case did not have the same direct contractual relationship with the debtor company as the RMBS Policyholders do with the insurer here. Unlike the creditors in *Innkeepers*, whom the court described as an "investor in a creditor," *id.* at 143, the RMBS Policyholders and other holders are the beneficiaries of insurance policies issued by AAC. Thus, whether the RMBS Policyholders should be referred to as "policyholders" is a red herring. The RMBS Policyholders are not a "creditor of a creditor" because they hold the insured obligations for those policies. Notably, AAC does not dispute that the RMBS Policyholders own or control securities insured by AAC. (*See* Brief of Respondent Ambac Assurance Corporation, *Dilweg v. Wells Fargo Bank*, Nos. 2010AP1291, 2022, at 14 n.8 (Wis. Ct. App. Nov. 18, 2010).) The insurance policies provide a direct relationship between the certificate holders of the trusts with the insurer. This direct relationship was not present in the *Innkeepers* case.

2. It Is Undisputed That The RMBS Policyholders Had A Right To Participate In The Circuit Court Proceedings.

In any event, both decisions cited by OCI are irrelevant because it is undisputed that the Circuit Court recognized – and OCI agreed – that the RMBS Policyholders could participate in the proceedings before the Circuit Court, whether

or not they are called "policyholders" or "parties-in-interest." At the outset of the case, the Circuit Court expressly invited interested parties to "seek modification or dissolution of part or all of" the Injunction Order. (R.9:13 (¶ 12).) The RMBS Policyholders are clearly interested parties, owning in excess of $1 billion face amount of RMBS Policies in the Segregated Account which has been placed into rehabilitation. (R.38:1 n.1.) More recently, the Circuit Court's Confirmation Order explicitly held that the RMBS Policyholders had a right to participate in the proceedings: "They [the RMBS Policyholders] may be heard as parties-in-interest . . .." (R.556:58 (¶ 9).) In other words, the Circuit Court recognized the right of interested parties to participate in the rehabilitation plan proceedings, even if it determined they may not intervene as parties or does not consider them policyholders.[2] In fact, the terms of the Plan of Rehabilitation specifically apply to named beneficiaries of policies. (*See* R.567:9 (§1.29) (defining "Holder" as "Any Person holding a Claim against the Segregated Account, including, in the case of a Policy Claim, the named beneficiary of the related Policy").)

Further, OCI itself has acknowledged the RMBS Policyholders' right to participate in the proceedings on the plan of rehabilitation. In a filing before this Court, OCI distinguished the right of interested parties to intervene in the proceedings – which the OCI opposes – from the right of those parties to appear at

[2] As outlined in detail in their opening brief, the RMBS Policyholders respectfully submit they have a right to intervene as a party. Even accepting OCI's position on intervention, the RMBS Policyholders had the right to appear at the hearing on the plan of rehabilitation and to participate in this appeal.

the hearing on the plan of rehabilitation. OCI conceded that even those parties that may not intervene as parties have the right to appear at the hearing on the plan of rehabilitation. OCI asserted that "although Chapter 645 special proceedings give those affected no right to 'intervene' in the traditional sense of being recognized as formal parties to an adverse litigation, *all persons and entities with an interest have the opportunity to be heard before the rehabilitation court.*" (Response Brief of the Wisconsin Office of the Commissioner of Insurance and Sean Dilweg, Commissioner of Insurance of the State of Wisconsin, as Court-Appointed Rehabilitator of the Segregated Account of Ambac Assurance Corporation, to Petition for Permissive Appeal and Request for Stay by Access to Loans for Learning Student Loan Corporation and Lloyds TSB Bank PLC, *Dilweg v. Access to Loans for Learning Student Loan Corp.*, No. 2010-AP-2721, at 26 (Wis. Ct. App. Nov. 10, 2010) (emphasis supplied).) OCI gave examples of the parties whose interests were sufficient to permit them to participate in the hearing on the plan of rehabilitation. OCI advised the Court:

> *In light of the rehabilitation court's invitation for those claiming an interest to be heard*—an invitation that has been accepted by movants ranging from Kentucky inmates (Appeal No. 2010AP2164) to Wall Street hedge funds [meaning the RMBS Policyholders] (Appeal Nos. 2010AP1291 & 2022) to institutional trustees . . . —the court struck the proper balance that the Wisconsin legislature intended: because rehabilitation proceedings are meant to be streamlined, non-adversarial proceedings, *claimants have the ongoing right to be heard* . . . .

(*Id.* (emphasis supplied).)

Similarly, AAC agreed that

> "[The objectors] *will be heard in connection with the formal rehabilitation plan* and formal intervention will add nothing to their right to be heard. The best regime, we submit, is one in which no one is formally a party to this proceeding but *everyone has an equal opportunity to be heard*, and we submit *that's what's happened thus far and that's what will continue to happen.*"

(R.469:110 (emphasis supplied).)

OCI has consistently maintained, and the Circuit Court has agreed, that regardless of their right to intervene as a party, interested entities – including the RMBS Policyholders – have a right to participate in the Circuit Court proceedings.

3. OCI Improperly Seeks To Supplement The Appellate Court Record With Later Introduced Facts.

Finally, OCI cites to certain findings of facts contained in the Circuit Court's Confirmation Order to support OCI's argument that "the Bank Group held insurable interests that entitled them to the same priority status as policyholders." (Aug. 5 Ltr. at 1.) OCI's citation to those facts is impermissible under Wis. Stat. § 809.19(10), which applies to supplemental authority, not later introduced facts. *See Hirschhorn v. Auto-Owners Ins. Co.*, 2010 WI App 154, ¶ 15 n.5, 330 Wis. 2d 232, 792 N.W.2d 639 (striking a party's "additional authority" filing of non-pertinent articles and statutes). Through what it has termed a "new decision," OCI improperly attempts to add additional facts introduced in the Circuit Court *after* this appeal was taken and after the appellants' opening briefs were filed. Because these facts clearly post-date the Circuit Court's order challenged in this appeal, they cannot be used to evaluate the

appropriateness of the Circuit Court's order that was entered over six months before the evidentiary hearing referenced in OCI's August 5 Letter.

Moreover, even if later introduced facts were somehow relevant to this appeal, the Circuit Court never conducted the review necessary to determine if the CDS Counterparties were entitled to anything before policyholders were paid in full, and the Circuit Court refused to permit the discovery necessary to allow that analysis. As the RMBS Policyholders demonstrated in their briefs, rather than review the CDS Settlement as the law requires, or even to permit discovery so the parties could present their arguments to the court in a developed fashion, the Circuit Court incorrectly held it lacked authority to review and limit OCI's approval of the CDS Settlement. (Brief of RMBS Policyholders, *Dilweg v. Wells Fargo Bank*, No. 2010-AP-1291, 2022, at 44-52 (Wis. Ct. App. Sept. 13, 2010).)

Conclusion

For the reasons set forth herein the RMBS Policyholders respectfully submit that OCI's August 5 Letter is irrelevant and a violation of this Court's May 3 Order.

Dated this 16th day of August, 2011.

Reinhart Boerner Van Deuren s.c.
22 East Mifflin Street, Suite 600
Madison, Wisconsin 53703
Telephone: (608) 229-2200
Facsimile: (608) 229-2100

Mailing Address:
P.O. Box 2018
Madison, Wisconsin 53701-2018

Bryan K. Nowicki
WI State Bar ID No. 1029857
Jessica Hutson Polakowski
WI State Bar ID No. 1061368
R. Timothy Muth
WI State Bar ID No. 1010710

BY _____

Attorneys for Aurelius Capital Management, LP, Fir Tree, Inc., King Street Capital, L.P., King Street Capital Master Fund, Ltd., Monarch Alternative Capital LP, and Stonehill Capital Management LLC

Of Counsel

David M. Greenwald
Michael T. Brody
Andrew J. Olejnik
Jenner & Block LLP
353 N. Clark Street
Chicago, Illinois 60654
Telephone: (312) 222-9350
Facsimile: (312) 840-7774

Patrick J. Trostle
Jenner & Block LLP
919 Third Avenue, 37th Floor
New York, New York 10022
Telephone: (212) 891-1665
Facsimile: (212) 909-0835