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

CARVAL HOLDERS' OPPOSITION TO REHABILITATOR'S MOTION TO QUASH DEPOSITION NOTICE

On February 26, 2016, the CarVal Holders[1] noticed the deposition of Ambac Assurance Corporation ("Ambac"). *See* February 26, 2016 Notice of Deposition (the "Notice," a copy of which previously was filed with this Court as Exhibit A to the Affidavit of Jeffery A. Simmons). They sought no discovery from the Office of the Commissioner of Insurance ("OCI"), nor from the designee of that office who serves as Rehabilitator under Ambac's Rehabilitation Plan, issued by this Court in 2011, amended in 2014, over which this Court retains jurisdiction today (the "Plan").

Oddly, it was the Rehabilitator, not the prospective deponent, who objected to the Notice. He filed a motion to quash on March 2, 2016. The deponent -- Ambac -- merely filed a perfunctory joinder.[2] These motions should be denied. They do not show that the requested discovery is in any way unreasonable or oppressive, Wis. Stat. § 805.07(3), nor that it is barred by Chapter 645, Wis. Stats.

[1] CVI GVF (Lux) Master S.a.r.l., CVF Lux Securities Trading S.a.r.l., CVI CVF II Lux Securities Trading S.a.r.l., CVI CVF III Lux Securities S.a.r.l., CVIC Lux Securities Trading S.a.r.l., CVIC II Lux Securities Trading S.a.r.l., CVI AA Lux Securities S.a.r.l., CVI CHVF Lux Securities S.a.r.l., CarVal GCF Lux Securities S.a.r.l., and CVI HH Investments LP are collectively referred to herein as the "CarVal Holders."

[2] The Rehabilitator's Notice of Motion and Motion to Quash (dated March 2, 2016), was joined by Ambac by its Notice of Motion (dated March 3, 2016).

This discovery dispute arises from the CarVal Holders' Motion for Order to Show Cause, filed February 11, 2016, and scheduled for hearing on March 29, 2016. Relying on the Rehabilitator's own statements and disclosures concerning Ambac's financial condition, the Motion argues that the Rehabilitator should make to Segregated Account policyholders the distributions contemplated by this Court's landmark 2011 Rehabilitation Plan. *See generally*, Brief in Support of Motion of Carval Holders' for Order to Show Cause ("OSC Brief"). The Rehabilitator has now abandoned the Plan's purpose, endorsing a course of action by Ambac's management that harms the CarVal Holders and all policyholders. *Id.* As shown below, Ambac's own recent disclosures show that Ambac is not simply refusing to distribute a mountain of cash, but is now launching a program to divert that cash to risky speculation, including, of all things, speculation in distressed real estate.

To block inquiry into the facts, the Rehabilitator invokes statutes and precedents that may apply to the emergency-room environment of a recently-commenced insurance insolvency: i.e., what the Ambac proceeding *was* before the Plan was approved in 2011. But the Rehabilitator's attempt to block discovery is not appropriate today. Ambac's emergency is long past. Its current cash-rich position has encouraged it to engage in risky equity speculation that dangerously undermines this Court's directives in the Plan. The tailored discovery sought by the Notice is warranted, imposes no unfair burden, puts no party at risk, and does not negatively impact the Plan.

BACKGROUND FACTS AND CIRCUMSTANCES

The Court's Continuing Jurisdiction. The Plan is the only vehicle by which long-delayed allowed claims of creditors like the CarVal Holders can be paid. This Court continues to have

jurisdiction of the Plan. The creditor claims at issue in this proceeding arose many years ago from the financial guaranty insurance policies discussed below.

Ambac's Financial Guaranty Insurance and the CarVal Holders' Interests. Ambac issued financial guaranty insurance policies that supported -- or in insurance jargon, "wrapped" -- residential mortgage-backed securities ("RMBS"). During the boom years of the last decade, Wall Street issuers formed trusts, which raised cash by selling RMBS, and used that cash to acquire pools of residential mortgage loans. Bondholders like the CarVal holders purchased the RMBS. These securities (called "certificates" in some transactions) depended on the trusts for payment, and that payment in turn depended on collections on the pooled mortgages, related revenue (such as mortgage payments, proceeds of foreclosures and mortgage insurance), and (at issue here) proceeds from Ambac's financial guaranties. Those financial guaranties were triggered, payable, and represented the only real source of the bondholders' recovery, until the Plan took away the bondholders' contractual rights, and left them to depend on the mechanics of the Plan.

In the structure outlined above, the trust is a pass-through. Its functions are to issue securities to bondholders, acquire and hold the pooled mortgages and related assets, and pay the former with the proceeds of the latter. The trustee has no economic interest in the mortgages or other mortgage-related income, as any and all income derived from the trust assets flows directly to bondholders. RMBS trustees serve as the agents for collection of payments under the financial guaranties. This arrangement is also a pass-through to the bondholders, who are the insureds. The various trustees of the Ambac-wrapped RMBS that the CarVal Holders own did not receive any portion of previous Plan payments for their own account, but passed them through to the CarVal Holders and other similarly-situated creditors.

The Pooling and Service Agreement ("2005 PSA") for Asset-Backed Certificates dated December 1, 2005 for which Bank of New York ("BoNY") serves as Trustee[3] is one example that illustrates these relationships. Under this arrangement, the relevant RMBS are the "Class AF Certificates," payable by BoNY as trustee from the trusts' assets, which include (i) the underlying mortgages and all payments thereon (principal and interest); (ii) various accounts funded with the proceeds of underlying mortgage payments; (iii) proceeds from other agreements and contracts; (iv) mortgage collateral upon foreclosure; (v) rights under mortgage insurance; and (vi) *the rights of the Trustee for the benefit of the Class AF Certificateholders under the Class AF Policy.* The latter refers to the financial guaranty provided by Ambac. *See* Third Kersten Aff. at ¶ 2, Ex. A at 65 (emphasis added).

All insurance proceeds under this Ambac insurance policy must pass, in their entirety, *directly* to certificate holders like CarVal:

> *The Trustee shall deposit any amount paid under the Class AF Policy* into the Class AF Policy Payments Account and distribute such amount only for the purposes of making the payments to Holders of the Class AF Certificates . . . . Funds received by the Trustee as a result of any claim under the Class AF Policy *shall be used solely for payment to the Holders* of the Class AF Certificates and *may not be applied for any other purpose*, including, without limitation, satisfaction of any costs, expenses or liabilities of the Trustee, the Master Servicer or the Trust Fund."

Id. at 144 (emphasis added).[4]

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[3] *See* Third Affidavit of Daniel Kersten ("Third Kersten Aff.") at ¶ 2, Ex. A. Because the 2005 PSA is a massive document, only the relevant pages have been attached. The entire document may be found at http://www.sec.gov/Archives/edgar/data/1348343/000090514806000814/efc6-0316_ 5810059ex41.txt.

[4] Other RMBS trust arrangements also clearly make this point. For example, the SACO I Trust 2006-2 provides that the trustee holds the relevant financial guaranty policy "in trust as agent for the Holders of the Class I-A Certificates," and that policy proceeds shall not "constitute part of the Trust Fund by this Agreement." *See* Third Kersten Aff. at ¶ 3, Ex. B at Section 6.08(j).

The subrogation arrangement under the 2005 PSA also shows that the real parties in interest are the RMBS holders, such as CarVal, not the trustees. When an insurer pays an insured's claim, the insurer then "stands in the shoes" of the insured to pursue whatever valuable rights -- typically, the insured's rights against third parties -- that may have given rise to its claim. The insurer is said to subrogate to the rights of the insured. Subrogation points to where the real economic interests lie. Suppose a car accident, in which Driver A, who is at fault, injures Driver B. Driver B's automobile insurer pays Driver B's claim, and then subrogates to Driver B's rights against Driver A. Driver B's tort suit is a valuable asset that the insurer takes by subrogation. In the 2005 PSA, Ambac, as the insurer, subrogates to the rights of the Holders, not to the rights of the trustee. The Class AF policy provides:

> . . . Ambac Assurance Corporation (Ambac) . . . agrees unconditionally and irrevocably *to pay to the Trustee for the benefit of the Holders* of the Insured Obligations, that portion of the Insured Amounts which shall become Due for Payment but shall be unpaid by reason of Nonpayment. . . . *Ambac shall be subrogated to all the Holders' rights to payment* on the Insured Obligations to the extent of the insurance disbursements so made. . . .

See Third Kersten Aff. at ¶ 2, Ex. A at Ex. R, A-1 (emphasis added).[5] This shows that it is the bondholders like the CarVal Holders, not the trustee, who are the insureds under the Ambac financial guaranty insurance. They are the real parties in interest in this proceeding, who are injured upon the failure of the Rehabilitator to carry out the Plan.

The Plan. By 2010, Ambac's situation had become dire. Continued payment on its financial guaranties would have been ruinous to Ambac, so the OCI used Wisconsin's statutory insurance rehabilitation process to significantly alter the rights of one class of Ambac's financial guaranty insurance policyholders, in order to accomplish a more orderly run-off of Ambac's

[5] Similarly, the policy endorsement provides, "[t]he Class AF Certificate Insurer shall be subrogated to the rights of each Holder to the extent of any payment by the Class AF Certificate Insurer under the Policy." Third Kersten Aff. at ¶ 2, Ex. A at Ex. R, A-6 (emphasis added).

liabilities and pursuit of its litigation claims. The OCI ordered Ambac to place its riskiest liabilities (primarily its financial guaranties of RMBS and student loans) into a "Segregated Account," which was put into Rehabilitation. This Court entered a Rehabilitation Order on March 24, 2010, naming the Commissioner as Rehabilitator of the Ambac Segregated Account. The Court later confirmed the Plan, which effectively issued I.O.U.s for insurance policy claims, and made the I.O.U.'s payable as funds became available from the General Account. *See generally*, OSC Brief at 3.

The Plan allowed Ambac to proceed as though it had not defaulted on any of its insurance policy obligations. It retained the power (which financial guaranty insurers have before they default) to manage the pools of mortgage-backed loans and to prosecute securities fraud actions against issuers -- rights that, in default, would belong to the policyholders. *See Nickel v. Wells Fargo Bank*, 2013 WI App 129, ¶¶ 86-94, 351 Wis. 2d 539, 841 N.W.2d 482. In return, the Plan prohibited Ambac from issuing new policies, and made the assets in the General Account fully available to the Segregated Account for the payment of its obligations. The Plan allowed General Account creditors to be paid currently, while Segregated Account claims could be paid only as and when the Rehabilitator drew down available cash. In the intervening six years Segregated Account Deferred Policy Obligations rose to almost $3.5 billion. OSC Brief. at 3-4. CarVal, and the other bondholders, remain the real parties in interest in this proceeding.

Ambac's Current Financial Condition. Ambac's financial condition has improved dramatically since 2010. The Rehabilitator's own analysis has shown -- unequivocally -- that circumstances *do* now permit a substantial distribution. *See* February 9, 2016 Affidavit of Daniel Kersten ("First Kersten Aff.") at ¶ 23 and Schedule 2; OSC Brief at 9-11. Since then, Ambac's ability to pay has only improved. OSC Brief at 12. This cash was supposed to be distributed to

long-delayed creditors. *See* First Kersten Aff. at ¶ 4, Ex. A at 13 ("[t]he Secured Note together with the Reinsurance Agreement *effectively render all of the claims paying resources of the General Account available to pay liabilities of the Segregated Account.*") (emphasis added).

Ambac's Recent Disclosures and the Need for Discovery From Ambac. On February 19, 2016, Ambac stated publicly that instead of distributing the huge amount cash it has accumulated since the Plan was enacted, it is now converting that cash into risky and illiquid securities, including RMBS. *See* February 25, 2016 Affidavit of Daniel Kersten ("Second Kersten Aff.") at ¶¶ 9-11. Last October, Ambac ramped up purchases of the securities it insures. *Id.* at ¶ 15. Each time it does this, it converts cash available for distribution now under the Plan into a security that may or may not pay out in future.

Later disclosures were yet more alarming. Last month, Ambac stated that it has moved into *speculation in distressed real estate*. In its 2015 Annual Report (filed with the SEC on February 29, 2016), Ambac reports that beginning in October 2015 it "introduced a new program to invest in residential real estate owned properties sourced from Ambac Assurance insured transactions. . . . While this program was initiated in order to help remediate losses in the insured portfolio, it has the potential to evolve into a new business opportunity for Ambac." *See* Third Kersten Aff. at ¶ 4, Ex. C at 2 (Q4 2015 10-K).[6]

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[6] Ambac admits that

> We initiated a new program . . . to invest in real estate owned properties ["REOs"] . . . . The main component of the value creation of this project will be the result of *making repairs to the REO properties in order to bring them up to neighborhood standards.* Upon completion of necessary repairs, the properties will either be immediately resold or resold at a future date *after being rented for a period of time. . . . This program will be rolled out gradually in order to validate our internal investment thesis.*

See First Kersten Aff. at ¶ 44, Ex. I (Ambac 3d Quarter Earnings Call at 3) (emphasis added).

In plainer English, Ambac, a regulated insurance company, has apparently begun to dabble in buying, fixing up and renting the distressed properties that secure the failed mortgage pools that it insured, using for capital cash that this Court contemplated for distribution to Segregated Account holders. With either the blessing or the indifference of the Rehabilitator, Ambac now appears to be pursuing house-flipping as a long-term business plan. This is hedge-fund activity, not insurance run-off. This speculative activity will tie up and put at risk liquid resources that the Plan envisioned would be transferred to the Segregated Account to pay policy claims. This speculative activity cannot benefit the Segregated Account holders (where claims are fixed in amount), but only the equity. It amounts to a seizure of creditor cash in order to make an equity bet.[7]

These are the core issues upon which The Rehabilitator -- and Ambac itself -- seek to bar discovery.

ARGUMENT

A. Wisconsin Law Affords Broad Discovery Rights.

The Rehabilitator makes no argument that the discovery sought by the CarVal Holders is contrary to Wisconsin's ordinary discovery norms concerning relevance and burden. Nor could he. "Wisconsin discovery law reflects a principle of liberal and open pretrial discovery." *Ambrose v. General Cas. Co. of Wis.*, 156 Wis. 2d 306, 314, 456 N.W.2d 642 (Ct. App. 1990) (citations omitted). "The parameters of permissible discovery are broad by necessity . . . this breadth is essential because the purpose of discovery is identical to the purpose of our trial

[7] Ambac's use of resources for real estate speculation diverts assets from the only two permissible uses envisioned by the Plan: reserving for claims against the General Account, and paying obligations under the Segregated Account. "Specifically, the commissioner points out that under the rehabilitation plan, the segregated account and the general account have equal access to the same common pool of resources held in the general account. According to the commissioner, this structure protects Ambac's claims-paying resources and provides the necessary resources to satisfy the segregated account liabilities." *Nickel*, 2013 WI App 129 at ¶ 32.

system – the ascertainment of truth." *Sands v. Whitnall Sch. Dist.*, 2008 WI 89, ¶ 19, 312 Wis. 2d 1, 754 N.W.2d 439 (citations omitted). As recognized by the Wisconsin Supreme Court in *Sands*:

> The quest for truth in each case, in turn, demands that we allow litigants to build complete records, investigating and preparing their cases thoroughly before presenting their cases to fact-finders. As such, we are even more loath to impose limitations upon discovery than we are to limit public access to government records.

Id. at ¶ 20.

Here, the need for the discovery is manifest. Creditors of the Segregated Account -- the CarVal Holders among them -- now appear to be involuntary lenders to a hedge fund. The requested discovery would show the Court the detail behind Ambac's public descriptions of its plans to divert cash from distribution to risky investments, and thus highlight Ambac's contravention of the directives of this Court in the Plan. The Notice is tailored to seek information on these topics from Ambac's designee, not the Rehabilitator himself nor the OCI.

In the Motion, the Rehabilitator seeks to protect Ambac from discovery on two grounds. Relying on *Nickel v. Wells Fargo Bank*, he argues first that the CarVal Holders are not "policyholders," and therefore have no right to take discovery in this proceeding. Second, he contends that three topics listed for Ambac's deposition fall within statutory protections for certain communications between insurance companies and their regulators. As shown below, these arguments would avoid the very supervision -- in a rehabilitation proceeding involving billions in liabilities -- retained by the Court to effectuate "the purposes and intent of the Plan."[8]

[8] *See* First Kersten Aff. at ¶ 6, Ex. B at 14 ("Following the Effective Date [of the Plan], *the Court shall retain exclusive jurisdiction* over the Proceeding in accordance with the Act to *ensure that the purposes and intent of the Plan and these Payment Guidelines are carried out.*") (emphasis added).

B. CarVal is Not Barred from Discovery as a "Non-Party" or by *Nickel.*

The Nickel Case. The Rehabilitator makes no direct attack on the standing of the CarVal Holders to bring their OSC Motion, arguing hypertechnically that they are not "policyholders," but rather, "investors in securities insured by policies." Rehabilitator's Motion at ¶ 4. His reference is to the trustee structure discussed above, in which the trustee nominally holds the policies, but policy proceeds belong to creditors like the CarVal Holders. *See* discussion, *supra* at 3-7. The point of this distinction is unclear, for "[s]tanding in Wisconsin is not to be construed narrowly or restrictively, but rather should be construed liberally." *Foley-Ciccantelli v. Bishop's Grove Condo. Ass'n, Inc.*, 2011 WI 36, ¶ 38, 333 Wis. 2d 402, 797 N.W.2d 789. "[S]tanding is satisfied when a party has a personal stake in the outcome." *Krier v. Vilione*, 2009 WI 45, ¶ 20, 317 Wis. 2d 288, 766 N.W.2d 517 (citation omitted). The Wisconsin Supreme Court has "frequently held that the law of standing in Wisconsin should not be construed narrowly or restrictively." *Fox v. Wisconsin Dep't of Health and Soc. Servs.*, 112 Wis. 2d 514, 524, 334 N.W.2d 532 (1983) (citations omitted). "[E]ven a trifling interest may be sufficient to confer standing." *City of Madison v. Town of Fitchburg*, 112 Wis. 2d 224, 230, 332 N.W.2d 782 (1983). A party's injury need not already have occurred; its standing may result from a sequence of events set in motion by another's conduct. *See, e.g., Chenequa Land Conservancy, Inc. v. Village of Hartland*, 2004 WI App 144, ¶ 17, 275 Wis. 2d 533, 685 N.W.2d 573. The standard is above all a practical one. As the Wisconsin Supreme Court has explained:

> The only problems about standing should be what interests deserve protection against injury, and what should be enough to constitute an injury. Whether interests deserve legal protection depends upon whether they are sufficiently significant and whether good policy calls for protecting them or for denying them protection.

Wisconsin's Envtl. Decade, Inc. v. Pub. Serv. Comm'n of Wis., 69 Wis. 2d 1, 13, 230 N.W.2d 243 (1975) (citation omitted). The CarVal Holders and other Segregated Account creditors hold

all of the economic interest in payments due on Ambac's Segregated Account liabilities. *See* Third Kersten Aff. at ¶¶ 2-3, Exs. A, B and discussion *infra*. Since the scope of these interests is entirely dependent on the Plan confirmed by this Court, those interests certainly deserve legal protection by the Court as a matter of "good policy." *See Wisconsin's Envtl. Decade,* 69 Wis. 2d at 13.

The Rehabilitator relies on *Nickel* to argue that the CarVal Holders' technical status deprives them of discovery rights. This misreads the decision. In *Nickel*, the Court of Appeals upheld a discretionary bar on what otherwise would have been a discovery free-for-all during the trial court's consideration of whether to confirm the Plan in the first place. The Court of Appeals did not impose an absolute bar on discovery, and certainly not under the changed circumstances that exist now. *Nickel* involved, centrally, an appeal from this Court's approval of the Plan. The Plan was presented during a period of economic emergency. In the course of affirming this Court, the court of appeals reviewed and upheld various procedural orders. While the court held that creditors like CarVal were not, in the context of fashioning a plan, "parties" with an *absolute right* to discovery under Chapter 804, Wis. Stats., it did not foreclose rights arising under Chapter 645, Wis. Stats., to pursue discovery, noting with approval a general power of courts in such matters "in the proper exercise of their discretion, [to] allow interested parties to conduct discovery in rehabilitation proceedings." *See Nickel*, 2013 WI App 129 at ¶ 112.

Thus *Nickel* does not erect a general ban on discovery in this proceeding. It holds simply that the circuit court properly exercised its discretion in denying what would have been a flood of discovery to a mass of creditors, at a time when the question was what sort of plan should be approved. We are now in a post-Plan world. The question now is whether discovery should be denied to the very parties whose contract rights were stripped by the Plan, whose only recourse is

via that Plan, and who now say, to their direct injury, that the Plan is being undermined by those with a duty toward them.

In this very different context, the limited discovery sought by the CarVal Holders is well within this Court's discretion under *Nickel*. The CarVal holders make no request for discovery from OCI or the Rehabilitator. They seek only limited discovery from an Ambac designee, so that they can learn and present to the Court the facts behind Ambac management's stated intent to gamble with funds that the Plan intended for distribution. The Rehabilitator can have no reasonable basis to fear these facts. Common sense dictates that he, and the Court, will profit from learning them. This Court's review of this dispute will depend on such facts.

If, as the Rehabilitator contends, no discovery *ever* can be permitted in this rehabilitation proceeding – a *per se* rule not set forth in *Nickel* – then as a practical matter creditors who have now been delayed for six years will be left with little recourse. No one will be able effectively to contest the Rehabilitator's failure to cause a distribution. It is precisely because the Plan grants him discretion that discovery is necessary.

Section 645. Apparently recognizing that *Nickel* leaves open this Court's discretion under Wis. Chap. 645, the Rehabilitator cites Wis. Stat. § 645.05(1)(k). Rehabilitator's Motion at 2. He has not attempted to meet the standard that applies to that section. Wis. Stat. § 645.05 does not address discovery issues directly, but states only that the Rehabilitator, a court-appointed receiver:

> may . . . apply for and any court of general jurisdiction in this state may grant, *under the relevant sections of ch. 813*, such restraining orders, temporary and permanent injunctions, and other orders as are deemed necessary and proper to prevent:
>
> * * *
>
> (k) Any other threatened or contemplated action that might lessen the value of the insurer's assets or prejudice the rights of the policy holders, creditors or shareholders, or the administration of the proceeding.

See Wis. Stat. § 645.05(1)(k) (emphasis added). Thus, this section would provide authority for quashing discovery only where the movant meets the standard for an injunction under chapter Wis. Chap. 813.

Wis. Chap. 813, entitled "INJUNCTIONS, NO EXEAT AND RECEIVERS," does not address discovery motion practice either, but does provide for injunctive relief (which in theory could include a motion to quash). But this relief is available only where the movant meets a high burden, which the Rehabilitator neither meets, nor even discusses.[9] Injunctive relief cannot be granted in Wisconsin unless the movant shows a reasonable probability of success on the merits, an inadequate remedy at law and irreparable harm. *See Werner v. A.L. Grootemaat & Sons, Inc.*, 80 Wis. 2d 513, 520, 259 N.W.2d 310 (1977). Under well-established Wisconsin law:

1. Injunctions are not to be issued lightly;
2. The cause must be substantial;
3. The movant must show a reasonable probability of ultimate success on the merits;
4. Injunctions should issue only when necessary to preserve the status quo; and
5. Injunctions are not to be issued without a showing of lack of adequate remedy at law and a showing of irreparable harm.

Id. As explained by the Seventh Circuit, if a court finds any of these elements lacking, then the analysis "ends and the preliminary injunction should not be issued." *Adams v. City of Chicago,* 135 F.3d 1150, 1154 (7th Cir. 1998). "'A preliminary injunction is an extraordinary and drastic remedy, one that should not be granted unless the movant, *by a clear showing,* carries the burden of persuasion.'" *Goodman v. Illinois Dep't of Fin. & Prof'l Regulation,* 430 F.3d 432, 437 (7th Cir. 2005) (emphasis added).

[9] Nor does the Rehabilitator offer to post the necessary bond before injunctive relief can be issued, as required by Wis. Stat. § 813.06.

The Wisconsin Supreme Court repeatedly has cautioned trial courts that "[i]njunctions, whether temporary or permanent, are not to be issued lightly. The cause must be substantial." *A.L. Grootemaat,* 80 Wis. 2d at 520. "Injunctive relief is not ordered as a matter of course . . .." *Forest County v. Goode,* 219 Wis. 2d 654, 670, 579 N.W.2d 715 (1998) (citations omitted). As one court stated:

> A preliminary injunction is an extraordinary and drastic remedy, one that should not be granted unless the movant, by a clear showing, carries the burden of persuasion. Granting a preliminary injunction involves the exercise of a very far-reaching power and is never to be indulged except in a case clearly demanding it.

S&S Sales Corp. v. Marvin Lumber & Cedar Co., 435 F. Supp. 2d 879, 882 (E.D. Wis. 2006) (citations omitted). And as the Wisconsin Supreme Court has held:

> [I]n order to warrant an injunction, the injury must be real, serious, material, and permanent, or potentially permanent; the right to the injunction must be clear; and the reasons for granting it strong and weighty.

Kocken v. Wisconsin Council 40, *AFSCME, AFL-CIO,* 2007 WI 72, ¶ 27 n.12, 301 Wis. 2d 266, 732 N.W.2d 828. These same standards apply with respect to temporary restraining orders. *See, e.g., Flakes v. Cullen,* 683 F. Supp. 700 (E.D. Wis. 1988) (denying request for temporary restraining order). In granting preliminary injunctive relief, a court exercises "a very far-reaching power, never to be indulged in except in a case clearly demanding it." *Roland Mach. Co., v. Dresser Indus., Inc.,* 749 F.2d 380, 389 (7th Cir. 1984) (quotation omitted) (reversing grant of preliminary injunction). Because the Rehabilitator has not even tried to meet these standards, his motion cannot be sustained under Wis. Stat. § 645.05(1) and should be denied.[10]

[10] The putative deponent, Ambac, says almost nothing in its joinder, which consists of a single sentence. Usually it is the potential deponent that explains to a court why discovery is inappropriate, but here, Ambac's "motion" is devoid of any analysis or support.

C. The Deposition Request Is Narrowly Tailored To Core Facts Underlying The Motion For Order To Show Cause, and Does Not Seek Privileged Material.

The Notice presents nine topics for examination for an Ambac designee. Each one is directly related to Ambac's statements about its intention to divert liquid assets away from payment of Segregated Account creditors under the Plan, and toward hedge fund activities.

Every dollar of liquid assets that Ambac invests in its hedge fund strategy (including its newly announced property management strategy) is a dollar made unavailable to the Segregated Account and its creditors, in contravention of the Plan. At the same time the Rehabilitator is confirming that assets are available for distribution, Ambac management is announcing their diversion of these assets to a "longer-term vision for the company." Second Kersten Aff. at ¶ 4, Ex. 2 at 9. The Rehabilitator reports at least $3.847 billion in assets available for distribution. The fundamental question posed by discovery is to what extent Ambac may now lock them up in long-term, and risky new ventures.

The Rehabilitator objects to Items 7, 8 and 9 of the Notice, arguing that these requests seek information protected by a statutory privilege under Wis. Stat. § 601.465. Rehabilitator's Motion at 6-7. Items 7 and 8 request that a corporate designee testify as to communications by Ambac's management with the Rehabilitator regarding "the Rehabilitator's current plans with regard to distributions to Holders of Segregated Account obligations, and [Ambac] Management's understanding of those plans" and "alternatives including tender of Ambac-wrapped securities, recapitalizations, or offers to policy holders to exchange their claims for new securities." Notice at 2. Item 9 requests no communications with the Rehabilitator, but rather seeks testimony by an Ambac designee on "Management's long-term plan for the operation (including any contemplated acquisition strategy, liquidation, sale or other disposition of AAC [Ambac Assurance Corporation]." *Id.* at 3.

Evidentiary privileges are to be strictly construed: they are "the exception, not the rule." *Imposition of Sanctions in Alt v. Cline*, 224 Wis. 2d 72, 85, 589 N.W.2d 21 (1999). "'[E]videntiary privileges . . . interfere with the trial's search for the truth, and must be strictly construed, consistent with the fundamental tenet that the law has the right to every person's evidence.'" *Sands*, 2008 WI 89 at ¶ 21 (quoting *State v. Echols,* 152 Wis. 2d 725, 736–37, 449 N.W.2d 320 (Ct. App. 1989)); *see also State v. Denis L.R.*, 2004 WI App 51, ¶ 12, 270 Wis. 2d 663, 678 N.W.2d 326 *aff'd and remanded,* 2005 WI 110, 283 Wis. 2d 358, 699 N.W.2d 154 ("We are also mindful that statutory privileges interfere with the trial court's search for the truth and are to be construed strictly and narrowly."); *State v. Locke*, 177 Wis. 2d 590, 602, 502 N.W.2d 891 (Ct. App. 1993).

The information sought in the Notice falls outside of the Wis. Stat. § 601.465 privilege for two reasons. First, the CarVal Holders limited the topics to communications about Ambac's distributions and long-term operational plans, while the privilege applies only to information that OCI obtains in the course of an investigation or examination made pursuant to Wis. Stat. §§ 601.42 and 601.43. *See* Wis. Stat. § 601.465(1m). The Rehabilitator does not suggest that responsive information was obtained during the course of an OCI statutory investigation or examination, and the CarVal Holders would agree that, should any otherwise-responsive material actually fall within communications during a regulatory investigation or examination, it could be logged and excluded. But communications made to Commissioner of Insurance in connection with the Plan are not within the privilege and should be open to discovery.

Second, the statute states that any presumption of confidentiality "may be rebutted by the requesting party presenting clear and convincing evidence to a court of competent jurisdiction that the public interest in the disclosure of the documents and information substantially

outweighs the potential for harm or competitive disadvantage to the insurer if the documents and information are disclosed and that the public interest concerns cannot be addressed without the disclosure of the documents and information." Wis. Stat. § 601.465(1n)(b). The Rehabilitator makes no claim of any harm that would be caused by the limited deposition of Ambac sought by the CarVal Holders. The CarVal Holders have shown above the significance of management's new Hedge Fund activities. What Ambac has communicated to the Rehabilitator concerning its intentions with regard to funds contemplated for distribution under the Plan is vitally important to the creditors and to this Court's review. The public interest in the requested information is substantial and outweighs the potential for any harm caused by its release.

CONCLUSION

The Rehabilitator's effort to protect Ambac should be rejected. For all of the reasons stated above, the Rehabilitator's Motion to Quash the CarVal Holder's Deposition Notice, and Ambac's joinder thereto, should be denied.

Dated this 23rd day of March, 2016.

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