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** **Hon. Richard G. Niess**

REHABILITATOR'S BRIEF IN RESPONSE TO OBJECTIONS TO ITS MOTION TO FURTHER AMEND THE PLAN OF REHABILITATION

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INTRODUCTION

The Rehabilitator's Motion to Further Amend the Plan of Rehabilitation[1] placed before the Court two issues under the exit standards of Section 645.35: *first*, whether the proposed Second Amended Plan (the "Plan") and the Consensual Transaction the Plan is designed to facilitate, treats existing Segregated Account claim holders fairly and equitably; and, *second*, whether the circumstances that lead to the Rehabilitation no longer exist (*i.e.* whether AAC will be able pay future claims in full going forward). No interested party has disputed that the Consensual Transaction is beneficial, fair and equitable to Segregated Account policyholders so the first issue should be considered resolved.

The only objections to the Plan have been to (1) the breadth of the final confirmation order; and (2) and the timing of the hearing on the proposed Plan amendments from a group of General Account policy beneficiaries in light of the hurricane that hit Puerto Rico. The underlying terms of the Consensual Transaction and the discount in particular, have not drawn an objection. In fact, no beneficial holder of an obligation insured by the Segregated Account has objected on any grounds related to the consideration offered in the Consensual Transaction.[2]

The Rehabilitator's evidence on the second element of the statutory exit standard drew an objection from a group of three distressed asset hedge funds that own bonds issued by an instrumentality of the Commonwealth of Puerto Rico that are insured by AAC policies in the General Account. Those bondholders have no current insured losses; they have presented no claims; and, the policies that insure their investments are in the General Account, not the Segregated Account. They thus have no standing to object to the Consensual Transaction or the

[1] Capitalized Terms used herein have the meanings ascribed to them in the proposed Second Amended Plan, the Payments Guidelines, and the Rehabilitator's Motion.

[2] Wells Fargo Bank, N.A., Deutsche Bank National Trust Company, Deutsche Bank Trust Company Americas, and U.S. Bank, N.A., filed limited objections in their capacity as Trustees of various RMBS securities trusts (the "Trustees"). The Trustees objections have been resolved in principle and will be withdrawn.

scheduling order that sets a hearing to decide whether Segregated Account policyholders and policy beneficiaries with existing claims will be paid for actual losses.

Not deterred, these bondholders seek an indefinite adjournment of the Rehabilitator's motion hearing and argue that economic conditions in Puerto Rico and alleged uncertainty over whether the Commonwealth or its instrumentalities will pay its debts, make estimating AAC's prospective losses in respect of its Puerto Rico exposure too difficult right now. It *is* possible however to estimate a range of losses due to AAC's exposure on Puerto Rico's debt and measure whether or not the Company will be able to meet its obligations. The Rehabilitator and its financial advisors have continually analyzed these risks and determined, as a regulatory matter, that AAC has sufficient capital and reserves to pay policy claims in full on a going forward basis, despite increased loss estimates on its Puerto Rico exposure that the COFINA Bondholders argue, wrongly so, the Rehabilitator ignored.

Pending approval from this Court, the Rehabilitator has given its regulatory approval to conclude this Rehabilitation and return AAC to normal business operations pursuant to the terms of the Consensual Transaction. In the Rehabilitator's judgment, the Plan provides for fair and equitable resolution of Segregated Account policy claims by allowing for 100% recovery on the principal amount of claims while providing sufficient capital reserves to pay future policy claims in cash, in full. That judgment should be afforded deference, because it is up to the Rehabilitator to determine the best way to balance potentially competing interests at issue. *See Nickel v. Wells Fargo Bank*, 2013 WI App 129, ¶ 130, 351 Wis. 2d 539, 841 N.W.2d 482 ("We must defer to the commissioner's extensive experience and expertise in determining the best approach to protecting the interests of long-term [vs. short-term] policyholders."). Further, the financial analyses relied upon by the Rehabilitator, as updated and filed concurrently with this Response, confirm that AAC will remain solvent following the closing of the Consensual Transaction and be able to pay policy claims in full on a going-forward basis. As a result, the Rehabilitator requests the Court grant its Motion, confirm the proposed Second Amended Plan, and allow the Consensual Transaction to close.

SUMMARY OF THE OBJECTIONS AND THE REHABILITATOR'S RESPONSE

Two groups of investors that own financial instruments insured by policies in the General Account (the "**Objectors**") dispute the proposed amendments and the Rehabilitator's decision to support the Segregated Account's exit from Rehabilitation. Their objections (the "**Objections**"), and the Rehabilitator's responses, are as follows:

1. *COFINA Bondholders.*[3] Cyrus Capital Partners, L.P., Polygon Global Partners LLP, and Taconic Capital Advisors, LP (the "**COFINA Bondholders**") object to the proposed Plan, arguing that (1) it is premature to confirm the plan due to the alleged unknown ultimate losses on AAC-insured governmental bonds in Puerto Rico; (2) continued rehabilitation or run-off is necessary to protect long-term General Account policyholders; and (3) the Rehabilitator has not properly exercised its discretion through its reliance on the Expert Report and its projections (the "Projections").

Rehabilitator's Response: First, the COFINA Bondholders are not parties to this Rehabilitation; they are policy beneficiaries of a single AAC policy in the General Account as a result of their purchase of bonds issued by an instrumentality of Puerto Rico. As beneficiaries of a General Account policy, the COFINA Bondholders lack standing to object to the Rehabilitator's decision to pay Segregated Account policy claims pursuant to the Consensual

[3] The terminology the COFINA Bondholders use to define themselves is misleading. They are not the "General Account Stakeholders." They are a group of three hedge funds that own bonds issued by an instrumentality of the Commonwealth of Puerto Rico, known as COFINA, that are insured by a single Ambac policy in the General Account.

Transaction and exit the Segregated Account from rehabilitation, both because their policy is in the General Account and because this is not an adversarial proceeding where third parties have standing.

The interests of policy beneficiaries of AAC are not the proper subject of this Rehabilitation which is directed to the Segregated Account. Instead, the interests of these AAC policy beneficiaries are protected by OCI which has approved the Consensual Transaction. Second, to the extent the Court considers the merits of the COFINA Bondholders' objections at all, the Plan remains durable; thus, the conditions that lead to the Rehabilitation under Wis. Stat. § 645.31 no longer exist. Third, the Rehabilitator's durability model, which has been continuously updated and incorporates many conservative assumptions, accounts for the risks associated with Puerto Rico; in fact, there is sufficient capital and reserves to pay 100% of potential losses under all 4 of the scenarios – base and stress cases, in the Rehabilitator's model.

2. *The MHPI Projects.* Developers that built housing projects for the military under the federal law known as the Military Housing Privatization Initiative (the "**MHPI Projects**"), object solely to injunctive language in Article 6.13 of the proposed Plan. They argue that the Court's confirmation of the Plan cannot enjoin suits against the General Account by purporting to cure what they claim are contractual defaults of AAC allegedly caused by the filing of the Rehabilitation itself.

Rehabilitator's Response: The MHPI Projects attempt to rehash arguments that this Court has squarely adjudicated in prior orders; this Court has confirmed that OCI established the structure of the Segregated Account specifically to *avoid* triggering defaults in policies left in the General Account. The proposed Article 6.13 is thus necessary to render this Court's prior Orders permanent as part of a durable exit from Rehabilitation. The final order in this case should reflect that intent of the Rehabilitator and the purpose behind the structure of the Segregated Account.

The inclusion of Article 6.13 in the final order to "prevent . . . further prosecution of any actions or proceedings" and to cure defaults that could be alleged to have arisen due to the filing of this Rehabilitation is in line with the Rehabilitator's ability to restructure policies and compromise contractual liabilities to avoid greater harm to all policyholders and the general public. *See* Wis. Stat. § 645.05(1)(f). Simply stated, if exiting the Segregated Account from Rehabilitation by merging it into the General Account will result in third parties using the fact of the Rehabilitation to stage unchecked litigation against the General Account, then these proceedings would be compromised and not wholly effective. That absurd result demonstrates that the MHPI Projects' objections are not well grounded in the law of insurance rehabilitation.

For all of these reasons and as further detailed below, the Rehabilitator respectfully requests that the Court overrule the Objections, grant the Rehabilitator's Motion, and confirm the Second Amended Plan to facilitate the Consensual Transaction and allow for an exit of the Segregated Account from Rehabilitation.

ARGUMENTS

I. THE ONLY ISSUE REMAINING BEFORE THE REHABILITATION COURT IS WHETHER THE REHABILITATOR HAS ABUSED ITS DISCRETION TO ADJUDGE AAC DURABLE AFTER CLOSING THE CONSENSUAL TRANSACTION.

This proceeding is controlled in large part by the Rehabilitator's discretion to determine whether an exit from Rehabilitation is in the best interests of the Segregated Account policyholders, creditors and the public as a whole. *See Nickel*, 351 Wis. 2d 539, ¶¶ 90-91. Under Wisconsin law, the "rehabilitator may take the action he or she deems necessary or expedient to reform and revitalize the insurer," subject to court approval. Wis. Stat. § 645.33(2).

This general power allows the rehabilitator to seek "[a]n order to rehabilitate the [insurer] and shall direct the rehabilitator to take possession of the assets of the insurer and to administer them under the orders of the court." Wis. Stat. § 645.32(1). More specifically, chapter 645 permits the rehabilitator to take significant steps in re-ordering an insurer's business, including enjoining contractual remedies. Wis. Stat. § 645.05(1). *See also Nickel*, 351 Wis. 2d 539, ¶ 127 ("[T]he commissioner acted reasonably in balancing the competing interests of short-term and long-term policyholders.").

The enumerated powers in chapter 645 are not an exclusive list of actions a rehabilitator may take. If that were so, there would have been no need for the Legislature to include in the statutes the language permitting the Rehabilitator to take any "action he or she deems necessary or expedient to reform and revitalize the insurer." Wis. Stat. § 645.33(2). Some powers will be enumerated, some implied; but as courts have articulated repeatedly, chapter 645 is to be liberally construed. *Nickel*, 351 Wis. 2d 539, ¶ 91 ("[I]t is axiomatic that the commissioner, in the reasonable exercise of the state's police power, may structure a rehabilitation plan that has the potential to adversely affect the interests of individual policyholders when the plan advances the broader interests of the policyholders, the creditors, and the public as a whole.") (citing *Am. Eagle Ins. Co. v. Wis. Ins. Sec. Fund*, 2005 WI App 177, ¶ 37, 286 Wis. 2d 689, 704 N.W.2d 44 (State may exercise the powers vested in it for the general good of the public even when doing so has the potential to impair contracts)). This Court has recognized the extent of this discretion indicating that the Rehabilitator has "absolute discretion" which is a "very high threshold, pretty much a breach or a complete disregard . . . of one of the important competing interests. . . ." (3/29/16 Hrg. Tr. pp. 59-60.)

Under the auspices of that responsibility and legal authority, the Rehabilitator has thoroughly analyzed the Objections and the issues that underlie them. Indeed, the bases of the COFINA Bondholders' objections, in particular, have been known to the Rehabilitator for months. Before and since filing the Motion, the Rehabilitator and its advisors met and conferred with the COFINA Bondholders, discussed and attempted to resolve their concerns, re-analyzed the financial models in the wake of Hurricane Maria, traveled to Puerto Rico and met with various officials to learn about rebuilding efforts, and continued to monitor AAC and its efforts to mitigate ongoing risk on all other aspects of its business operations. As a result of that due diligence, the Rehabilitator concludes that the Plan is durable and provides the best outcome for all policyholders, policy beneficiaries, creditors and the public generally under the circumstances.

II. THE COFINA BONDHOLDERS & MHPI PROJECTS DO NOT PRESENTLY HAVE ANY VESTED RIGHTS IN THIS DISPUTE AND THUS LACK STANDING AND SHOULD NOT BE AFFORDED ADDITIONAL PARTICIPATION BEYOND WHAT THE COURT HAS ALREADY ALLOWED.

A. This Rehabilitation is Not a Dispute Between Private Parties.

The COFINA Bondholders' objections treat the Consensual Transaction as a deal they can reject or approve based on their own self-interest and biased assessment of the future durability of AAC. Likewise, the MHPI Projects object to the terms of the Rehabilitator's confirmation order as though this is a civil action to which they are a party entitled to submit their own order. Neither of these objecting parties however are, nor can they be, parties to this proceeding because a rehabilitation "is not a controversy between private parties but a proceeding by the state in the interest of the public." *Padway v. Pac. Mut. Life Ins. Co.*, 42 F. Supp. 569, 575 (E.D. Wis. 1942) (citing *Carpenter v. Pac. Mut. Life Ins. Co.*, 10 Cal. 2d 307, 338, 74 P.2d 761 (1937)); *see also Four Star Ins. Agency, Inc. v. Hawaiian Elec. Indus., Inc.,* 89 Haw. 427, 434-35, 974 P.2d 1017, 1024-25 (1999) ("Commissioner has exclusive standing to assert claims arising out of the liquidation or rehabilitation of an insurance company on behalf of not only the insolvent insurer, but also its policyholders, creditors, and all other interested parties."); *Marino v. Cont'l Cas. Co.*, 308 F. Supp. 2d 906, 909 (E.D. Wis. 2003) (Wisconsin insurance statutes "create no private right of action and afford no basis on which" relief could be granted.).

This principle has also been noted in other appellate decisions within this Rehabilitation proceeding, including the appeal in *Nickel v. FFI Fund Ltd.*, No. 2014AP2033 (Wis. Ct. App. Mar. 4, 2016) (motion for reconsideration denied). Principally, the *FFI Fund* court held in its summary disposition that "the only formal parties to the current proceeding are the . . . rehabilitator, Ted Nickel, and the subject insurer, Ambac." *Id*. at 3. Other parties may have "a right of limited participation," but that does not equate to an ability to raise objections and meddle with the ongoing affairs of the Rehabilitation. *See id.* The limited right of participation certainly does not allow the COFINA Bondholders to act as a party to seek to alter the schedule of the Rehabilitation.

This Court has also explicitly recognized the same purpose of these proceedings, indicating that "these are not principally litigation proceedings. They are management tools, not legal tasks. And the Rehabilitator should be granted broad authority and flexibility to act without cumbersome procedures." (3/29/16 Hrg. Tr. pp. 58-59.) Although the Rehabilitator has allowed 60 days for objections to the proposed Plan amendments prior to confirmation, ultimately it is the sound determination of the Rehabilitator, not arguments of self-interested third parties which should control this Court's decision to grant the Motion to confirm the Plan.

B. Third Parties Outside the Segregated Account Lack Standing to Object to the Plan.

In addition to being outside third-parties to this proceeding, the COFINA Bondholders and MHPI Projects do not have standing to challenge the timing and amount of claims payments to holders of Deferred Amounts because the policies that insure their investments are not in the Segregated Account. The Court of Appeals decision that rejected issues raised by FFI Fund in this case is instructive. Specifically, in *Nickel v. FFI Fund*, No. 2014AP2033, the court discussed the standing issue and rejected an appeal by holders of investment trust interests insured by a policy allocated to the Segregated Account that challenged the Rehabilitation Court's decision construing certain contracts. *Id.* at 3-4. The court acknowledged that the Rehabilitation affected the amount and timing of payments to the investors, allowed the opportunity to be heard, but did not allow them to intervene and obtain discovery. *Id.* at 3. Here, neither the COFINA Bondholders nor the MHPI Projects are beneficiaries of policies in the Segregated Account; they are therefore even further removed in interest than were the FFI Fund investors. Thus, they have no standing to object to the terms of the Consensual Transaction.

In addition, the Objectors have no current claims. The Court of Appeals in *FFI Fund* explained that that the appealing investors, also without claims, would not be adversely impacted if they were barred from objecting. *Id.* The court also noted "legal principles and judicial policies" that underlie a rehabilitation proceeding weigh against allowing individual certificate or policy holders to have standing to challenge orders issued by the rehabilitation court following the adoption of a rehabilitation plan. *Id.* at 4 (citing Wis. Stat. § 645.32; *Nickel v. Wells Fargo Bank*, 351 Wis. 2d 539, ¶¶ 12-14); *see also Nickel v. Aurelius Capital Mgmt. LP*, No. 2011AP2708, at 6-7 (Wis. Ct. App. Mar. 1, 2013) (dismissing appeal for lack of standing by group of investors who challenged the rehabilitator's decision to enter into an agreement they claimed affected their financial interests).[4] That decision stands for the proposition that

[4] Courts in other jurisdictions agree that, for example, even stockholders of an insurer do not have standing in rehabilitation/liquidation proceedings in insurance litigation. *See, e.g., Cohen v. State ex rel. Stewart*, 89 A.3d 65,

investors that own financial instruments insured by an AAC policy, but without losses and who have not presented a claim, do not have standing to challenge claims payments to policyholders with actual losses. That proposition squarely applies here.

Although chapter 645 permits "any person whose interests are substantially affected" to seek judicial review of a summary order, it does not grant a similar right to challenge discretionary acts of a Rehabilitator, which suggests a legislative choice not to provide third-party standing in the rehabilitation context. *See* Wis. Stat. § 645.21(4).[5] The Wisconsin Legislature's decision to limit the right to judicial review in chapter 645 reflects the special nature and remedial public purpose of rehabilitation proceedings. A rehabilitation is not an adversarial proceeding to adjudicate the individual interests of literally thousands of policyholders; rather, it is a formal remedial measure to "rehabilitate the business of a domestic insurer." Wis. Stat. § 645.32(1). *See also Nickel v. FFI Fund*, No. 2014AP2033, at 3 ("A rehabilitation proceeding is not an adversarial action…").

The COFINA Bondholders want individualized attention purportedly to ensure under extreme scenarios that the Company can pay their *potential* future claims, while delaying claims payments to policyholders and policy beneficiaries with actual unpaid losses. As the Court of

93-94 (Del. 2014) ("Jurisdictions that have considered the issue [of stockholder intervention to oppose a rehabilitation order] have typically held that stockholders do not have standing to intervene in a delinquency proceeding."); *see also Metcalf v. Investors Equity Life Ins. Co.,* 80 Haw. 339, 910 P.2d 110 (1996) (stockholder did not have standing to oppose liquidation petition); *Hartnett v. Southern Am. Fire Ins. Co*., 495 So. 2d 902, 903 (Fla. Ct. App. 1986) (stockholders of insolvent insurance corporation sought to challenge receiver's actions, but were denied due to lack of standing); S*tate ex rel. Holland v. Heritage Nat. Ins. Co.*, 2008 OK CIV APP 50, 184 P.3d 1093, 1097 (2008) ("Shareholders do not have standing to intervene in a receivership proceeding"); *State ex rel. Crawford v. Am. Standard Life & Acc. Ins. Co.,* 2001 OK CIV APP 152, 37 P.3d 971, 974 (2001) (holding that stockholders do not have standing to intervene); Steven Plitt, et al., *Couch on Insurance* § 5:36 (3d ed. 2013) ("Stockholders of insurer placed in receivership pursuant to the Uniform Insurers Liquidation Act do not have standing to intervene in a receivership proceeding.").

[5] That chapter 645 is not "silent" on third-party standing, but instead explicitly provides for such standing in connection with a summary order, not in a rehabilitation proceeding, *see* Wis. Stat. § 645.21(4), presumably represents a deliberate legislative choice. "Where the legislature has employed a term in one place and excluded it in another, it should not be implied where excluded." 2A Norman J. Singer & J.D. Shambie Singer, *Sutherland on Statutes and Statutory Construction* § 46:5 (7th ed. 2007).

Appeals however wrote in *Nickel v. Wells Fargo Bank*: "nothing in the statutes requires that long-term policyholders be treated equal to the short-term policyholders." 351 Wis. 2d 539, ¶ 128. Taken to its extreme, the COFINA Bondholders are asking this Court to disallow the Consensual Transaction and continue the Segregated Account Rehabilitation, not because of actual adverse developments with respect to policies allocated to the Segregated Account but instead because of their prediction of future alleged "mushrooming" losses related to AAC's Puerto Rico exposures – an argument that fails to meet any fairness "sniff test," much less applicable regulatory or legal precedent. (*See* COFINA Obj. at p. 3.)

Chapter 645 reflects the legislative intent that the Commissioner pursue rehabilitation in a prompt, efficient manner, perceiving rehabilitation as a "*management* rather than as a legal task" and "without cumbersome procedures." Wis. Stat. Ann. § 645.32 cmt. to 1967 law (West 2014) (emphasis added). This intent would be frustrated if every bondholder, note holder, or investor owning an insured instrument had the ability to challenge the claims payment decisions made as part of the Rehabilitator's "management task." It also would undermine the very purpose of chapter 645, which is to provide the Rehabilitator with the discretion and the tools needed to fashion a rehabilitation plan that is fair and equitable to Segregated Account policy beneficiaries and in the best interests of policyholders, creditors, and the public generally. *See* Wis. Stat. § 601.01(2); *see also Four Star Ins. Agency, Inc.*, 89 Haw. at 434-35, 974 P.2d at 1024-25.

Interested parties to a rehabilitation are entitled to notice and a hearing; they are not entitled to an individualized award or to have loss reserves set aside for their particular durability concerns. The Rehabilitator must have the *exclusive* discretion to regulate the insurer in the context of a rehabilitation. As the court in *Four Star*, explained:

> [A] flood of claims arising from an insurer's insolvency brought by *each creditor of the insolvent insurer would potentially result in an award to one creditor that*

> *could be disproportionate to that of another creditor*. Under such a system, which encourages creditors to race to the courthouse, it is difficult to imagine how a party faced with the prospect of numerous lawsuits from various creditors would be able to settle the multitude of lawsuits in an orderly and equitable manner. Such a construction of the ISRLA would be inconsistent to its purposes of ensuring the equitable apportionment of losses and minimizing litigation. Because we presume that the legislature did not intend such an absurd result, the *exclusivity of the Commissioner's standing is necessary* to minimize litigation and to ensure the equitable apportionment of losses.

Id. (emphasis added) (holding the "Commissioner has exclusive standing to assert claims arising out of the liquidation or rehabilitation of an insurance company on behalf of not only the insolvent insurer, but also its policyholders, creditors, and all other interested parties").

In summary, this Court has already heard and ruled on arguments related to standing issues in this proceeding generally, holding that certain parties did not have standing within the context of this Rehabilitation proceeding. (3/29/16 Hrg. Tr. p. 58.) In this instance, the COFINA Bondholders and MHPI Projects are not Segregated Account policyholders – they are at best General Account policy beneficiaries with no actual losses, and thus no claims. This places these objectors yet another level removed from the parties that the Court of Appeals held lacked standing in *Nickel*. They should not be allowed to seek particularized modifications or accommodations to further their own economic interest at the expense of others. For this reason, their objections should be summarily overruled.

C. The COFINA Bondholders Have Suffered No Actual Injury.

The next reason the CONFINA Bondholders lack standing is that they have suffered no actual injury. They are beneficiaries of a single AAC policy, out of thousands in the General Account. They have incurred *no losses* and made *no claims* on the policy; indeed, their bonds do not require payment until at least 2047.[6] Any potential injury upon which they seek to base a

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[6] AAC insured two senior COFINA capital appreciation bonds; one bond matures in 2047 (CUSIP No. 74529JAN5) and the other in 2054 (CUSIP No. 74529JAP0).

claim of standing therefore is a potential injury only and is simply too remote in time and too speculative to satisfy the standing requirement. *See Nader v. Altermatt*, 166 Conn. 43, 59, 347 A.2d 89, 97-98 (1974) (rejecting a policyholder's challenge to rehabilitation because policyholder's concern that terms of his coverage may change or be terminated was speculative, and "[m]ere generalizations and fears [of a future adverse impact] are not sufficient to establish aggrievement").

In yet another decision from this Rehabilitation, the Court of Appeals reviewed a standing dispute and rejected the arguments of a party alleging it had standing because the harm to such party was purely speculative. *Nickel v. Aurelius Capital Mgmt. LP*, No. 2011AP2708 (Wis. Ct. App. Mar. 1, 2013) (finding no standing and stating that a party alleging "that 'there are no assurances that [their] insurance policy claims will ever be paid in full' is entirely speculative in nature, and not direct injury"). Therefore, the COFINA Bondholders and MHPI Projects should be denied standing because they have no actual injury and their interests have not yet vested. Accordingly, their objections should be denied.

D. Third Parties Outside the Segregated Account Should be Afforded Only the Process Set Forth in Wis. Stat. § 645.33(5).

Although the COFINA Bondholders and MHPI Projects lack standing, they may be allowed to "notice and hearing as the court prescribes." Wis. Stat. § 645.33(5). Neither party however holds a ripe property interest. Generally, "the due process analysis focuses on whether the claimant has a vested property interest in the cause of action." *Aicher v. Wis. Patients Comp. Fund*, 2000 WI 98, ¶ 81, 237 Wis. 2d 99, 613 N.W.2d 849. Their objections, if granted on the other hand, would only prejudice policyholders of the Segregated Account with actual claims, and thus actual property rights.

The notice and hearing provisions of the statute must also be applied here in context. That is, the Rehabilitator in this case provided advanced notice of the Consensual Transaction and, further, has allowed interested parties to be heard: it held listening sessions to describe the Consensual Transaction, filed its Motion with an extensive Disclosure Statement, allowed sixty days for objections, and continued communications with creditor constituencies. Through this process, the Rehabilitator was able to resolve the Trustees' objections. The Rehabilitator provided due process that went far beyond any requirements of the statute.

The statutory right to notice and hearing is not however strictly mandated but rather may be limited within this Court's discretion given the nature of a rehabilitation proceeding. *See* 9-100 New Appleman on Insurance Law Library Edition § 100.05 ("due process is not violated when the insurer fails to give notice to policyholders of its rehabilitation proceedings, because the policyholders' interest is represented by the insurance commissioner and protected by the state court"). The result is that the Court is not required to grant to the objecting parties notice and an opportunity to be heard; any additional process this Court affords over that provided by the Rehabilitator should be for a purpose, and not simply to allow more litigation.

Given the Court's role under Wisconsin law in rehabilitation proceedings (*i.e.* to review the Plan for an abuse of the Rehabilitator's discretion), the Rehabilitator is proposing in its Pretrial Report to allow the COFINA Bondholders to argue their Motion to Adjourn at the Pretrial Conference but hear the MHPI Projects on their objections to the Confirmation Order after the Rehabilitator presents its case at the Confirmation Hearing.[7] That process would address the COFINA Bondholders' Motion to Adjourn immediately but then put the MHPI Projects' objection in context after the evidence is in from the Rehabilitator. Unless the COFINA Bondholders' and MHPI Projects demonstrate a complete disregard by the Rehabilitator of an

[7] To be clear, the Rehabilitator, as set forth in the Pretrial Report, is proposing only arguments on the objections.

important competing interest, they have not made so much as a *prima facia* case for an abuse of discretion. Under these circumstances, the Court should confirm that these requested procedures satisfy the notice and hearing requirements of WIS. STAT. § 645.33(5).

III. THE COFINA BONDHOLDERS' OBJECTIONS PROVIDE NO BASIS TO DENY THE MOTION.

A. The COFINA Bondholders Mischaracterize The Roles And Functions Of The Rehabilitator And The Court As Part Of This Rehabilitation.

The COFINA Bondholders wrongly assert that: (a) the Rehabilitator has no obligation to disclose information that "might undermine his effort to obtain this Court's approval" which would "counterbalance the pro-Exchange Transaction advocacy of the Rehabilitator" and (b) that the Court should allow active participation of the COFINA Bondholders to "identify[] and sharpen[] the genuine issues and . . . the reams of financial data presented in this Motion." (COFINA Obj. at p. 7.) These assertions demonstrate a fundamental misunderstanding of the obligations and responsibilities of the Rehabilitator and this Court's role.

The Rehabilitator is an independent, appointed official with a duty to "administer and enforce" the Insurance Code and protect "insureds, creditors, and the public generally, with minimum interference with the normal prerogatives of proprietors. . . ." Wis. Stat. §§ 601.41(1) and 645.01(4). The Rehabilitator does not act as an advocate for itself or any particular party and has no economic interest in the Consensual Transaction. Its role is to protect claimholders, mitigate losses, and rehabilitate the insurer, if possible. As such, the Rehabilitator has no incentive to ignore or hide facts in pursuit of any alleged agenda, and is afforded deference in its discretionary, decision-making powers. *See Nickel*, 351 Wis. 2d 539, ¶¶ 19-22 (factual determinations are reviewed for an abuse of discretion; the great weight standard applies to issues of statutory interpretations); *but see* Wis. Stat. § 227.57(10) (the "due weight" standard).

This Court functions in a familiar over-sight role, deferring to the Rehabilitator's discretion on factual determinations and giving deference to questions of statutory interpretation. Wisconsin courts "cannot rule . . . on the wisdom of an agency's decision" but should only determine whether the agency is empowered by statute to perform the function at hand. *Maple Leaf Farms, Inc. v. DNR*, 2001 WI App 170, ¶ 35, 247 Wis. 2d 96, 633 N.W.2d 720; *see also* Wis. Stat. § 227.57(8) ("[T]he court shall not substitute its judgment for that of the agency on an issue of discretion."). Here, the Court is *not* tasked with "devot[ing] substantial resources to assessing and vetting the assertions made in the Motion and to analyzing the opaque financial statements presented. . ." as the COFINA Bondholders argue. (*See* Obj. at p. 7.) The Court should not, and could not possibly do that by "objectively evaluating the Exchange Transaction." (*Id*. at p. 7, n. 8.) That is the *Rehabilitator's* role — not the Court's job. The role of the Court is to "find[] that rehabilitation has been accomplished and that grounds for rehabilitation . . . no longer exist." Wis. Stat. § 645.35(2). That task is not a *de novo* review of the minutiae of a Rehabilitation Plan covering $10 billion in Segregated Account net par outstanding to which OCI, then the Rehabilitator and its advisors, have devoted nearly a decade of intensive oversight, review and analysis. Instead, the Court must ensure "the commissioner appropriately exercised its discretion in formulating a plan" to pay claims in a way that is "fair and equitable" and "in the best interests of policyholders." *Nickel*, 351 Wis. 2d 539, ¶ 28.

B. The Rehabilitator Has Taken Into Account Recent Events In Puerto Rico.

Despite ongoing risks within Puerto Rico (and in a number of other AAC-insured exposures), the Rehabilitator has soundly exercised its discretion to evaluate and assess AAC's exposure in Puerto Rico. The Rehabilitator has taken multiple steps to incorporate the economic impact of Hurricane Maria into its financial model and has indeed performed additional financial analyses and made changes to the Margin of Safety. The Rehabilitator has also held listening sessions and met with the COFINA Bondholders. Finally, the Rehabilitator conducted on-island due diligence to observe the aftermath of the hurricane itself. All of these steps have confirmed the Rehabilitator's determination that AAC remains durable after the Segregated Account exits Rehabilitation under the terms of the Consensual Transaction.

The Rehabilitator's September 22, 2017 Expert Report did not ignore economic conditions in Puerto Rico, as the COFINA Bondholders argue. The Report recognized the potential for AAC's Puerto Rico exposures to generate substantial losses. In fact, the entirety of the General Account's exposure to Puerto Rico, as originally contemplated in the Report, may well have met the criteria to allocate Puerto Rico exposures to the Segregated Account in the absence of the Consensual Transaction and the additional capital and other benefits generated by the Consensual Transaction. As set forth in the Updated Report, the Rehabilitator's Expert, Dennis McGettigan, has assumed now even greater losses associated with Puerto Rico, which he submits "will generate the largest creditor losses ever experienced in the United States municipal finance market." (McGettigan Update at p. 4.) After giving effect to the Consensual Transaction, four of the five single risks in AAC's insured portfolio with the largest projected losses are Puerto Rico exposures. The Rehabilitator however, based on the Expert Report and the Update, has adjudged that the Consensual Transaction provides for a durable exit from Rehabilitation despite the economic impact Hurricane Maria had on Puerto Rico. (*See* McGettigan Update at p. 4.) For the COFINA Bondholders to state that the Rehabilitator and its Expert, however, ignored the "elephant in the room" is simply wrong.[8]

[8] (*See* COFINA Obj. at p. 15.) Instead, the true elephant in the room is why AAC's Puerto Rico exposures are afforded superior treatment to that of, for example, the Student Loan insured portfolio, which was allocated to the Segregated Account in 2010 with no paid policy claims and lower levels of prospective losses than currently contemplated for AAC's Puerto Rico exposures. The reason, of course, is that the Rehabilitator believes that post-Transaction AAC can pay even the elevated levels of Puerto Rico policy claims contemplated in the Projections.

The Updated Expert Report incorporates the following assumptions related to Puerto Rico loss development:

- An increase in the term of the debt service moratorium contemplated in the Projections; and,
- An increase to the loss given default assumptions associated with AAC's various Puerto Rico exposures in both the base and stress case scenarios.

(McGettigan Update at p. 3.) The projected losses associated with AAC's Puerto Rico exposures now account more than 60% of all losses on a present value basis and more than 55% of all post-exit losses on a nominal basis through the end of 2023. (McGettigan Update at p. 3.) The Updated Expert Report further reflects a 25% decrease in the minimum margin of safety (from $637 million to $476 million) in its most conservative scenario, and a 29% decrease in the four-scenario average minimum margin of safety (from $946 million to $671 million). (McGettigan Update at page 7.) The Rehabilitator's Expert notes in his Update that "(i) the margin of safety, and (ii) the inherent conservatism of the Projections as a whole" lead him to conclude that the Plan remains durable. (McGettigan Update at p. 6.)

The COFINA Bondholders' statement that losses in COFINA could be $3 billion (i.e., a 0% recovery) is simply a brash argument developed using an unrealistic discount rate[9] and a self-serving presumption that the COFINA governing documents will be found invalid. This is the type of extreme scenario the Rehabilitator is not required to assume nor is the Court obligated to consider. *See Nickel*, 351 Wis. 2d 539, ¶ 131 (the court need not consider alternative plans,

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[9] (COFINA Obj. at p. 19.) The COFINA Bondholders employ the 30-year Treasury bond yield in developing their COFINA loss estimate. In contrast, AAC has employed a 5.1% discount rate on statutory loss reserves since December 31, 2009, which is not inconsistent with the discount rates employed for statutory reserving purposes by other financial guarantors. For example, MBIA Insurance Corporation used a 5.1% discount rate for reserving purposes in its publicly filed statutory financial statements; Assured Guaranty Municipal Corp. disclosed 5.0%; Assured Guaranty Corp. 4%, and FGIC 4.27%.

including a creditor's "worst case" scenario). Given that, the COFINA Bondholders arguments simply do not mesh with the reality of the expected resolution of the case.

The Expert Report assumes, reasonably, that existing laws and municipal finance structures in place for decades are constitutional; it assumes further that disputes as to the entitlement to tax revenue streams in Puerto Rico will be settled. That assumption is based on facts that have been well publicized. Specifically, the parties in the PROMESA Title III restructuring proceeding are currently involved in complex mediation, involving six federal judges, indicating a meaningful possibility of a consensual agreement. The financial markets agree: the trading prices of uninsured senior COFINA bonds do not reflect anything close to a 100% loss.

It does not appear that even the COFINA Bondholders believe their losses will be 100%. At least one, Taconic Capital Advisors, LP, owns $11.85 million of *uninsured* senior COFINA and $8.2 million of *uninsured* subordinated COFINA bonds.[10] It seems implausible that sophisticated investors such as the COFINA Bondholders would have purchased any insured or uninsured COFINA interests if they held any *bona fide* concerns about the validity of any part of COFINA's legal foundation; such a contradiction would have severe personal repercussions. Viewed in that light, the arguments put forth by the COFINA Bondholders look particularly hypocritical.[11]

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[10] *See* Form 2019 filed on October 26, 2017 in PROMESA proceedings. Second Supplemental Verified Statement of the Senior COFINA Bondholders' Coalition Pursuant to Fed. R. Bankr. P. 2019, *In re Commonwealth of Puerto Rico*, No. 3:17BK3282, at ex. A (Bankr. P.R. filed Oct. 26, 2017) (Dkt. #1552).

[11] The position taken by the COFINA Bondholders is also at odds with publications authored by their counsel in the article *In re City of Detroit: Nine Lessons for Creditors*. One excerpt from that publication: "Given that Chapter 9 cases are generally dominated by negotiated, rather than litigated, outcomes, municipal creditors (acting individually or collectively through an insurer or trustee) should aggressively engage in mediation when available from the outset." Lawrence A. Larose & Samuel S. Kohn, *In re City of Detroit: Nine Lessons for Creditors*, Lexology (Dec. 11, 2014), https://www.lexology.com/library/detail.aspx?g=505d88b8-7567-44c9-9a16-0a3c174da2db (last visited

C. The Expert Report and Updated Report Demonstrate a Sound Financial Analysis of the Company and Projected Future Losses.

1. The COFINA Bondholders Ignore Significant Aspects of the Company's Finances.

The Rehabilitator is charged with fashioning a final Plan that balances many competing interests, and is durable, to rehabilitate the Segregated Account in the context of a dynamic market, the financial guarantee insurance market, in which risks and returns fluctuate regularly in the normal course of business. The COFINA Bondholders adopt a self-serving, self-focused approach to durability that fails to recognize the Rehabilitator's holistic or long term approach. They argue that it is unclear where money would come from to fund expected payments, and then conclude under their assumed facts that the exit plan is not durable. Yet, as the court in *Nickel* explained, the COFINA Bondholders are not entitled to have their particularized "worst case" scenario included in the model. *Nickel*, 351 Wis. 2d 539, ¶ 131.

There is some uncertainty in any model that uses estimates. But not all uncertainties are negative. Puerto Rico aside, the majority of recent developments have been positive and signal the possibility of further positive upside not included in the model. For example, AAC consummated several de-risking transactions in the 77 days between the filing of the Expert Report and Updated Report that, in aggregate, involved approximately $400 million of adversely classified credits. (McGettigan Update at p. 1.) As set forth in the Updated Report, these exposures were settled on favorable terms such that, in aggregate, these transactions were accretive relative to the loss expectations contained in the Projections. (*Id.*) Further, these transactions collectively served to reduce portfolio "tail risk," which is an important consideration in evaluating durability. (*Id.*)

Dec. 11, 2017). Yet the COFINA Bondholders argue that the Court should ignore this creditor lesson, and assume *both* a mediation failure ***and*** a zero-sum outcome adverse to the COFINA structure.

Such "de-risking" transactions are a primary example of the innate conservatism employed in the Projections. For example, the Projections do not incorporate de-risking or value creation transactions that are not yet finalized, even though at any given time AAC has a pipeline of such opportunities in progress. (McGettigan Update at p. 2.) At this time, AAC is exploring de-risking transactions with single risks aggregating more than $2.5 billion in net par outstanding. (*Id.*) Over the next four to six months, some of these opportunities will result in transactions; others will not. At the same time, new opportunities will be identified, continuing the de-risking cycle. Based on their experience in this matter, the Rehabilitator and his advisory team expect this cycle to represent a significant but unquantifiable source of value for policyholders after the consummation of the Consensual Transaction. (*Id.*) This approach, namely, highly conservative estimating practices and leaving certain value creating opportunities out of the model until finalized, is reason to have confidence in the Company's ability to eliminate risk.

Other examples of this innate conservatism are found in the assumptions used in RMBS and Student Loan loss estimation. In recent years, RMBS loss development has generally performed in line or slightly better than that contemplated by the base case loss estimates. (McGettigan Update at p. 2.) Yet the stress case RMBS loss estimates employed in the Projections are developed using a macroeconomic scenario created by Moody's Analytics that reflects a moderate recession.[12] Both the base and stress case Student Loan losses incorporated in the Projections are premised on interest rate assumptions that exceed prevailing forward rates by more than 100 basis points on average. Further, stress case loss student loan estimates

[12] As noted by Moody's Analytics, this particular macroeconomic scenario is designed such that "there is a 90% probability that the economy will perform better, broadly speaking, and a 10% probability that it will perform worse." *See* Moody's Analytics, *U.S. Macroeconomic Outlook Alternative Scenarios*, at 7 (July 2017) https://www.economy.com/home/products/samples/moodys-analytics-us-alternative-scenarios.pdf (last visited Dec. 11, 2017).

contemplate an immediate 25% decline in collateral performance. We believe these examples underscore the innate conservatism of the loss estimates contained in the Projections.

Another notable example is the conservatism employed in developing projected RMBS recovery (the "RMBS Litigation Proceeds") for use in the Projections, with the JPMorgan Chase settlement representing a single example. Specifically, the Rehabilitator and its financial advisors had valued, conservatively, RMBS litigation against JPMorgan Chase by arbitrarily reducing AAC's estimated remediation numbers in two scenarios, even as AAC's own data already incorporated probabilities of recoveries and did not fully reflect the high end recovery figures. The conservatism of the valuation is evidenced by the understatement of the JPMorgan settlement. As the litigation took shape, AAC's estimated remediation recovery for this dispute was approximately $640 million; an estimate that the Rehabilitator further discounted in two of his four scenarios. The JPMorgan RMBS litigation later settled for $992.8 million. There are scores of other examples.

There are also many misstatements to point out in the COFINA Bondholders' objections. To provide the Court with a flavor for how misguided and flat-out wrong some of them are, but not burdening the case any further with a point-by-point reply, we consider two examples. One, the COFINA Bondholders argue there is "mystery income" built into the model. (COFINA Obj. at p. 21.) There are no such things in the model: AAC is able to meet its obligations in Scenario 4 due, in part, to dividends paid by AUK (AAC's operating subsidiary in the United Kingdom) to AAC, which are assumed to commence in 2036. (*See* Disclosure Statement at § 9.) The COFINA Bondholders leave those cash-flows out of their "analysis."

Two, they argue that the RMBS Litigation Proceeds are the key to durability, but unpredictable. (COFINA Obj. at p. 21.) Although all litigation is subject to risk, and to some extent unpredictable, the potential recovery in litigation can be, and has been, reliably estimated. RMBS litigation in particular has become a mature legal field and the expected recoveries are within the normative range of recoveries in similar proceedings, including an extrapolation of the JPMorgan Chase settlement. In addition, as part of the Consensual Transaction, sophisticated investors were willing to invest $240 million of new money (*i.e.* the Tier Two Financing) for the right to receive litigation proceeds in excess of $1.6 billion. The COFINA Bondholders mention nothing about these positive market indicators. The Rehabilitator and its advisors however find the Tier Two Financing in particular to be a compelling market validation of the estimated value of the RMBS Litigation Proceeds.

2. The Rehabilitator's Reinvestment Rate of 5.1% Is Appropriate.

The COFINA Bondholders, purposefully or not, misconstrue and falsely misrepresent statements regarding investment returns in the Expert Report. The COFINA Bondholders state:

> [the Expert Report's] conclusions depend on the unrealistic assumption that Ambac's investments will earn 5.1% annually, compounded indefinitely. The Gordian Report provides no support for its use of the 5.1% figure. Mr. McGettigan's only defense for this obvious lapse in the analysis is his summary assertion that he "believe[s] that [5.1%] is a reasonable estimate for [Ambac]'s long-term reinvestment rate. See Gordian Report at 20. . . . After backing out returns attributable to Ambac-insured RMBS (which are intended to be retired in connection with the proposed Exchange Transaction), Ambac's portfolio yield falls to approximately 3.7%.

(COFINA Obj. at p. 18.) Before explaining why their analysis is fatally flawed, we need to correct their terminology. The reinvestment rate is the rate of return AAC is projected to earn on its excess cash flows (*i.e.* when cash flows in a period are more than required for the business); AAC is thus projected to buy assets and add to its current portfolio being run-off. The reinvestment rate combined with the portfolio run-off creates the investment return. The

COFINA Bondholders incorrectly use the terms investment rate and re-investment rate interchangeably.

There are at least two reasons why the COFINA Bondholders' reinvestment rate objection is wrong. First, Ambac has a large investment portfolio which the Rehabilitator has gone through in great depth to project cash flows, using security-by-security level detail. Thus the investment return numbers are not pulled out of thin air but are a projection of current known holdings, many of which are expected to be held until maturity.

Secondly, the COFINA Bondholders exclude returns on insured RMBS indicting they will be retired in connection with the Consensual Transaction. Selling insured RMBS is completely illogical and it has never been stated that Ambac will sell its RMBS after the Consensual Transaction. That is a baseless "fact" the COFINA Bondholders have simply made up.

Disregarding the COFINA Bondholders' mistakes and misrepresentations, including mixing up the investment rate and reinvestment rate, the 5.1% "reinvestment rate" in the Expert Report is reasonable. Until the Rehabilitator's Motion, AAC employed a 5.1% rate to discount losses in every statutory financial statement it filed since December 31, 2009, as a practice prescribed by OCI. AAC has routinely noted in the statutory financial statements that this discount rate was less than the rate of return of admitted assets.[13] The Rehabilitator also reported the statutory yield of AAC's investment portfolio using AAC data in the 2010 Disclosure Statement and every Annual Report filed with the Court since the Rehabilitation began. Rates varied from 5.78 to 10.65%. Overall, AAC's investment portfolio has generated a compound

[13] AAC's third quarter 2017 statutory financial statement for example, provides: "Ambac Assurance also discounts probable losses on guarantees of subsidiary obligations using a discount rate equal to the average rate of return on its admitted assets. The Company's average rate of return on its admitted assets at December 31, 2016 was 6.98%. OCI has directed the Company to utilize a prescribed discount rate of 5.10%...." *Quarterly Statement of the Condition & Affairs of the Ambac Assurance Corp.*, at Q06 (Sept. 30, 2017).

annual return of 8.3% from February 2010 through September 2017. In that context, a 5.1% assumed rate is reasonable.

The COFINA Bondholders' feigned concern over the assumed reinvestment rate also defies the terms of the Rehabilitator's model, the industry standard and the investment options Wisconsin insurance law specifically allows. The reinvestment rate employed in the Projections, again reflecting the Rehabilitator's conservative approach, is assumed to start at 4.3% in 2017, not 5.1%. Over time the model assumes the rate increases to 4.6% in 2018, 4.9% in 2019, and finally to 5.1% in 2020 (and remaining constant at 5.1% thereafter).

The Rehabilitator's Expert also performed a reinvestment rate sensitivity analysis to show how a change in the assumed rate affected the Margin of Safety. That analysis showed in Scenario Four the Margin of Safety increased by approximately $250 million with a 100 basis point reinvestment rate increase and decreased by approximately $175 million with a 100 basis point reinvestment rate reduction. Applying this same sensitivity test to Scenario One indicates that the projected Margin of Safety would increase by approximately $325 million with a 100 basis point increase in reinvestment rate and would decrease by approximately $230 million with a 100 basis point decline in reinvestment rate. These results are substantially different from the huge Margin of Safety sensitivity to the reinvestment rate indicated by the COFINA Bondholders in part due to their conflation of reinvestment rate with overall investment portfolio return.

Moreover, the Wisconsin Administrative Code clearly allows AAC to invest in various asset classes besides risk-free U.S. Treasury Bonds. *See* Wis. Stat. § 620.22; Wis. Admin. Code § Ins. 6.20(8) (which allows investment in stocks, high-yield bonds, hedge funds, real property, loans, etc.). The COFINA Bondholders on the other hand argue that the model should use the

30-year Treasury Bond risk-free rate as the assumed reinvestment rate for purposes of the Rehabilitator's durability analysis. Forcing AAC to invest only in 30-year T-bonds however does not reflect prudent investing, actionable asset-liability matching strategies, market realities, or the options and opportunities for portfolio diversification allowed under Wisconsin law. The COFINA Bondholders' argument is merely their opportunistic attempt used to inflate prospective losses and reduce reasonable prospective investment portfolio returns.

3. The Rehabilitator Should Not Adopt a "Wait and See" Approach.

The Rehabilitator and its expert advisors are quite accustomed to making decisions with imperfect information. Had OCI back in 2008 and 2009 waited until perfect information existed to evaluate exposures to Credit Default Obligations (or "CDOs") and RMBS losses, many value-creating transactions would not have been consummated prior to the Rehabilitation filing – in the depths of the Great Recession – or during the pendency of the Rehabilitation. Had OCI waited until perfect information was available with respect to prospective Student Loan losses, that insured portfolio would not have been allocated to the Segregated Account in 2010. Those decisions, made with imperfect information in the midst and/or aftermath of the greatest financial crisis since the Great Depression, were successful. Both the Company's financial position and the risk profile of the Segregated Account have improved substantially.

Finally, the potential for a lengthy Puerto Rico debt service moratorium makes the analogy to 2010 even stronger. The moratorium is a suspension by the Puerto Rican government of debt-service payments that could last for as long as five years. The Rehabilitator's Expert believes that AAC has sufficient financial wherewithal to weather projected yet substantial policy claims associated with a multi-year moratorium, as well as substantial post-moratorium losses. In fact, for the long-term, the Rehabilitator has concluded, based on a conservative analysis, that the nominal cash buffer in the Company is expected to average over $4.1 billion by the end of 2054. (McGettigan Update at p 9.) The Rehabilitator believes that this analysis shows AAC has ample financial wherewithal to pay policy claims in the ordinary course even in the event of adverse developments, including additional issues that arise in Puerto Rico. That makes the Rehabilitator's exit plan durable.

Therefore, approval of the proposed Plan, closing of the Consensual Transaction, and payment – finally, to Segregated Account policy beneficiaries is appropriate now, because these actions will (i) allow for new investment in AAC (in the form of the Tier Two Financing), (ii) allow AAC to realize a discount on the settlement of Segregated Account liabilities; (iii) satisfy existing insurance contracts, and instruments that have been treated as *pari passu* with such insurance contracts, with 'true" surplus notes (thus increasing financial flexibility); and (iv) facilitate further portfolio de-risking. Delaying approval of the Second Amended Plan, even a few months, deprives AAC and Segregated Account policy beneficiaries of value and puts the entire Consensual Transaction, needlessly, at risk.

D. The Rehabilitator's Conclusions That the Consensual Transaction is Fair and Equitable and the Company is Durable Post-Exit Takes Into Account and Balances the Needs of Short-term and Long-term Policyholders.

1. The Plan Protects All Policyholders While Treating Segregated Account Policy Beneficiaries Equitably.

One objective in moving forward with the Consensual Transaction is to level the playing field between General Account and Segregated Account policyholders. Since the Segregated Account was established, crystalized claims have been paid at a rate of 45% of their losses; whereas crystalized claims in the General Account have been paid at 100%. On top of this, the risk profile of AAC's global exposures has indeed shifted from the Segregated Account to the General Account (primarily due to risks in Puerto Rico). (*See* McGettigan Update at p. 7.)

Short-term policyholders and beneficiaries in the Segregated Account are agreeing to accept a discount and non-cash consideration as full consideration of their policy claims. The COFINA Bondholders ignore these concessions and would prefer the Segregated Account policyholders to remain at a 45% payout, thereby forcing a long-term deferral of the remaining 55% just to ensure under extreme scenarios that COFINA Bondholders are paid 100%. Their argument regarding favoritism of the Segregated Account is purely self-serving and hypocritical. The existing structure of these proceedings has shifted into an inequitable balance that currently benefits only the COFINA Bondholders. The Second Amended Plan levels those inequities and provides for payment of all claims from a single entity going forward. In other words, balance is restored to pre-rehabilitation levels.

The court in *Nickel*, has, essentially, set precedent in this case mandating overruling their objection to unequal treatment. In denying objections to the Rehabilitation Plan asserted by the Las Vegas Monorail bondholders and Eaton Vance, the court ruled that, "nothing in the statutes requires that long-term policyholders be treated *equal* to the short-term policyholders." *Nickel*, 351 Wis. 2d 539, ¶ 128 (emphasis in original). The court wrote further that policyholders are to be treated "equitably" under Wis. Stat. § 645.01(4)(d), not "equally." *Id.* Here, Segregated Account policyholders are being treated inequitably under the status quo; the Consensual Transaction restores balance to the treatment of Segregated Account and General Account policyholders, giving the COFINA Bondholders more than they are entitled to under the statute.

The Updated Expert Report assumes the Consensual Transaction is consummated by March 31, 2018; in that case policy claims related to AAC's Puerto Rico exposures would represent between 57% and 63% of all post-Transaction claim payments through the end of 2023, and the vast majority of all projected losses associated with policies in the General

Account. (McGettigan Update at pp. 3-4.) In short, the very arguments used in the original Disclosure Statement are – based upon the arguments espoused by the COFINA Bondholders – most applicable to AAC's Puerto Rico exposures. This begs the question: if the COFINA Bondholders are right, why not allocate the Company's Puerto Rico exposure to the Segregated Account? The key difference is that the Rehabilitator and its advisors determined that such "mushrooming" Puerto Rico claims ***can be paid while consummating the Consensual Transaction*** (and receiving the equitable benefits thereof), rather than prematurely creating a Segregated Account for AAC's Puerto Rico's exposures. The Rehabilitator believes this is a better outcome for all parties. It would be unfair and inequitable in the Rehabilitator's judgment to continue to impair the Segregated Account holders when the Segregated Account is in a position to exit rehabilitation.

2. The Standards to Conclude This Rehabilitation Have Been Met.

It is unclear how the COFINA Bondholders are defining the purpose of rehabilitation, other than conflating "Segregated Account" with "Subordinated Account." From the Rehabilitator's standpoint, the Segregated Account has been rehabilitated and the Consensual Transaction allows for payment in full on the principal of existing as well as all future claims. The COFINA Bondholders argue however that the Second Amended Plan "siphons billions" of dollars from AAC, and "places heaps of liabilities" onto AAC in return. This argument ignores the coexistence of the Segregated Account and AAC particularly through the reinsurance agreement that has been in place since the beginning of this case.

Through the reinsurance agreement, the Segregated Account may make demands on the General Account for payment so long as the demands do not cause the General Account's policyholders' surplus to fall below $100 million. Notably, AAC's Third-Quarter 2017 statutory surplus is approximately $750 million, well in excess of the minimum surplus that would limit the reinsurance agreement; the Projections incidentally do not include the surplus beneath $100 million.

With that fact, it is clear the proposed Plan, and the Consensual Transaction it facilitates, does not siphon billions of dollars from AAC, only to place "heaps of liabilities" upon it; to the contrary, the Plan would allow for payments to existing Segregated Account policy beneficiaries and leave the Company in a financial position to pay future claims in full, and in cash. That is the considered conclusion of the Rehabilitator and the opinion of its Expert. The COFINA Bondholders have neither the right nor the regulatory insights into the Company to interfere with the Rehabilitator carrying out this Plan.

It is also misleading for the COFINA Bondholders to characterize the Plan as creating additional liabilities for the General Account. All of the liabilities of the Segregated Account are reinsured by the General Account, subject to AAC maintaining a surplus of at least $100 million. Indeed, the Plan itself actually reduces policyholder level liabilities through the 6.5% discount in the Consensual Transaction and subordinated surplus notes, which are currently treated *pari passu* with DPOs.

Last, the COFINA Bondholders state that because the Second Amended Plan does not restore full and unsupervised control of the business to AAC (in accordance with Wis. Stat. § 645.35(2)), the Plan does not comply with the law, implying that OCI's anticipated increased regulatory scrutiny means that AAC remains too volatile to be durable. This argument is a red herring. First, post-rehabilitation, OCI is free to exercise its regulatory powers to perform whatever oversight and review is necessary of AAC in a manner consistent with Wisconsin law. The additional scrutiny reflects an ordinary course use of OCI's regulatory power. Indeed, failing to use protective measures would be inconsistent with OCI's fundamental operations.

Moreover, the mere fact that regulatory oversight will continue has nothing to do with AAC's "possession of its property and the control of its business." OCI has no expectation of interfering with AAC's day-to-day business operations.

E. Current Market Conditions have Little Bearing on AAC's Durability.

The Rehabilitator's primary concern is that Segregated Account policyholders and policy beneficiaries with unpaid claims receive the consideration in the Transaction; it is *not* concerned about bond prices. The COFINA Bondholders rely on the trading prices of their bonds to assert that AAC cannot guarantee payment of principal and interest in full on its Puerto Rico policies. (Obj. p. 14.) This argument is overly simplistic and shortsighted. With any financial investment, trading values show merely a snapshot in time. The value of bond prices has nothing to do with long-term capability of AAC, as an insurer, to actually perform under the terms of its policy commitments which guarantee timely payment of principal and interest but do not guarantee market value. Rather, market prices for bonds are driven by a number of factors, some of which are unrelated to the ultimate recovery on the principal of the bond, including: the term structure of interest rates, duration and other factors. Bonds trade at premiums or at discounts to par in order to create required *yields*, and are not necessarily based on the investors' expectation of extraordinary gains or losses.

For example, bonds with low interest rates will trade at below par to achieve market-required yields. Due to their longer durations, bonds with cash flows that are far in the future (like the COFINA capital appreciation bonds held by the COFINA Bondholders) are more sensitive to these factors irrespective of credit quality. It is notable that prices of the insured Puerto Rico bonds owned by the COFINA bondholders did not change materially following the announcement of the Consensual Transaction indicating the Consensual Transaction was not perceived as materially adverse. Prices for AAC-insured COFINA Bonds have declined somewhat in recent weeks, although prevailing price levels remain materially greater than the prices of uninsured COFINA bonds with shorter duration (and thus less interest rate sensitivity).

The COFINA Bondholders calculate AAC's "implied loss" as the difference between 100 (%) and the market price of Puerto Rico "unwrapped" (i.e. uninsured) bonds. This faulty methodology yields an "implied loss" based on market prices as of November 17, 2017, of $1.933 million. By focusing on current market prices, which reflect for the most part short term investor expectations, the COFINA Bondholders conveniently ignore that AAC's exposure is long-tailed. Indeed, AAC has no debt service coverage on COFINA until *2047*. In fact, current market prices do not even necessarily reflect negatively on AAC's long-term exposure.

To the contrary, looking at the price charts for other AAC-wrapped issues, shows that for the most part substantial value is being applied to the AAC wrap. (as shown by prices for: (i) various AAC-wrapped Puerto Rico issues and (ii) various AAC-wrapped issues from a group of non-investment grade issuers (the City of Chicago, Chicago Board of Education, Bridgeview, among others) or issuers that are perceived to have problems (*e.g.* the State of Illinois).) For example, AAC-insured General Obligation bonds are trading around 93% of par; uninsured General Obligation bonds are trading around 22-23%. AAC-insured PRHTA bonds are trading near par; uninsured PRHTA bonds are trading in the mmid-teens. AAC-insured PRIFA bonds trade near par; uninsured PRIFA bonds are also trading in the mid-teens. While it is true that prices for AAC-insured Puerto Rico exposures have traded down somewhat in the aftermath of Hurricane Maria, and AAC's credit worthiness may be a factor behind this trade-off, it is important to note this trade-off pales in comparison to the sell-off in uninsured Puerto Rico bonds. Furthermore, AAC has not provided an AAA-rated wrap since early 2008, so such modest price movements are not unexpected. But no matter, providing an AAC wrap is not a requirement to end a Rehabilitation.

If there was a truly a substantial risk of default, prices for AAC-wrapped Puerto Rico bonds would likely trade far below prevailing levels. Further, if prospective Puerto Rico losses were so substantial, and the margin of safety so thin, that Puerto Rico losses could "break" post-exit AAC, as seemingly argued by the COFINA Bondholders, we would likely see that credit concern reflected in post-Hurricane Maria price levels for other AAC-wrapped instruments, which is not the case.

F. The Parties to the RESA in the Segregated Account Support the Exit Plan.

Finally, the Consensual Transaction satisfies crystalized claims in full as soon as the Plan is confirmed. In agreeing to discount their claims, the parties to the RESA expect to be paid ***now***, not months or years from now. This requirement is clearly outlined in the RESA which includes a number of strict deadlines that must be met.

Since filing the Motion, additional creditors have signed on in support of the Second Amended Plan by joining the RESA without any additional consideration. For example, on November 15, 2017, CVC Credit Partners signed the RESA. The additional holders of all outstanding Deferred Amounts that now support the Second Amended Plan means that more than 61% at the time the Motion was filed support the Plan. This only bolsters the Rehabilitator's support of the Consensual Transaction and decision to move forward with its approval to facilitate AAC's exit from rehabilitation.

Prolonging the Rehabilitation would jeopardize the support of the Ad Hoc Group, the RESA and the corresponding discount in the Consensual Transaction. It would then lead to a lengthy, administratively burdensome run-off that would continue to disparately treat Segregated Account policyholders. The Consensual Transaction on the other hand is a material benefit to Segregated Account policyholders and policy beneficiaries, and at the same time benefits AAC in that it allows it to remain durable after full implementation of the Plan.

IV. THIS COURT SHOULD DISMISS THE OBJECTIONS BY THE MILITARY HOUSING PROJECTS BECAUSE (1) THEY ARE BOUND BY PRIOR COURT ORDERS THAT DISPOSE OF THEIR OBJECTIONS, (2) ARTICLE 6.13 IS ENTITLED TO COMITY AND DEFERENCE IN OTHER JURISDICTIONS; AND (3) THE MHPI PROJECTS DO NOT HAVE DUE PROCESS RIGHTS.

A. The Military Housing Projects Are Bound By The Orders Of This Court.

The MHPI Projects object to Article 6.13 of the Second Amended Plan. Article 6.13 however extends and is consistent with the Rehabilitation Court's Order Granting the Rehabilitator's Motion to Confirm and Declare the Nature of These Proceedings, entered October 24, 2016 (the "Military Housing Order"). That Order confirmed, among others, the January 24, 2011 Decision and Final Order Confirming the Rehabilitator's Plan of Rehabilitation, with Findings of Fact and Conclusions of Law (the "Confirmation Order"). Specifically, the MHPI Projects appeared before this Court in 2016 to argue their issues related to the Rehabilitation Court's authority to declare the impact of the rehabilitation case on AAC's contracts and, as a result, the Military Housing Order declared that "it would run counter to OCI's stated purpose of capitalizing the Segregated Account in a manner that avoided triggering contractual defaults and causing collateral damage if AAC's issuance of the Secured Note and Excess-of-Loss Reinsurance Agreement were considered to constitute a transfer of assets from Ambac to the Segregated Account or the appointment of a receiver for Ambac's assets." This declaration forms the basis for Article 6.13.

Now, the MHPI Projects have returned affirmatively to raise the issues underlying this declaration by challenging Article 6.13. They had a full and fair opportunity in 2016 to litigate their issues, and had full access to the Rehabilitation Court that has jurisdiction over these issues. This Court reaffirmed that the Segregated Account structure was intended by OCI to ensure that the fact of the Rehabilitation Proceedings did not trigger a default on the policies left in the

General Account. In other words, the MHPI Projects already lost the fight to avoid those Orders. Article 6.13 simply makes the injunctive effect of those Orders permanent.

B. Article 6.13 is Necessary to Protect the Fundamental Purpose of the Segregated Account Statute, Wis. Stat. § 611.24, Which is to Permit Rehabilitation of a Segregated Portion of AAC Pursuant to Wisconsin's Rehabilitation and Liquidation Act ("the "Act"), Wis. Stat. § 645.01, et seq., While at the Same Time Safeguarding this Rehabilitation.

1. The Plan and Article 6.13 Serve the Remedial Purposes Underlying the Act by "protect[ing] the nterests of insureds, creditors, and the public generally. . ." Wis. Stat. § 645.01(4).

Article 6.13 serves the remedial purposes underlying the Act by "protect[ing] the interests of insureds, creditors, and the public generally. . .." Wis. Stat. § 645.01(4). Because the Commissioner is required to act within the public interest under Wis. Stat. § 601.15, its conclusion that declaratory or injunctive relief is "necessary and proper" to prevent prejudice to "policyholders, creditors or shareholders, or the administration of the proceeding" warrants considerable deference. *Cf.* Wis. Stat. § 227.57(10) ("[U]pon such review of [agency decisions] due weight shall be accorded the experience, technical competence, and specialized knowledge of the agency involved, as well as discretionary authority conferred upon it.").

The Segregated Account is being separately rehabilitated pursuant to Wis. Stat. § 611.24, and upon exit, will be merged into the General Account. The Rehabilitator has properly invoked its authority to include Article 6.13 in the Plan to protect the rehabilitation effort and the subsequent merger of the Segregated Account with the General Account. If this structure were not protected, and if the Rehabilitation were to cause defaults under AAC's General Account contracts, section 611.24 of the Wisconsin Insurance Code - which expressly permits the targeted rehabilitation of a segregated account - would be rendered ineffective and the successful conclusion of this rehabilitation case would be jeopardized. The MHPI Projects' opposition to

Article 6.13 seeks to undermine the entirety of the targeted approach to rehabilitation that is authorized by Wisconsin law and upheld by the *Nickel* decision.

2. This Court has Discretion to Approve the Plan As Proposed.

Because Article 6.13 is necessary to carry out the Plan, consistent with chapter 645 this Court has discretion to include the Article as proposed in the Plan because it preserves AAC's contract rights that have been put at risk by virtue of the Rehabilitation proceedings. In fact, this instance would not be the first exercise by the Rehabilitation court of discretion to preserve contract rights. On September 12, 2012, the Rehabilitation Court exercised its jurisdiction to clarify that the temporary injunction issued on January 24, 2012 was intended to prevent loss of rights by Ambac and the Segregated Account. (Sept. 12, 2012 Order ¶ 2.) The Rehabilitation Court concluded that the temporary injunction prohibited actions that would prevent Ambac and the Segregated Account from exercising particular rights, interests or claims based on the "Events" that resulted in the Segregated Account's rehabilitation case, and that Ambac and the Segregated Account retained "control rights" under certain transaction documents, regardless of occurrences described in such documents as a default. In that September 12 Order, the court also ordered that "[t]he rehabilitation court has jurisdiction over any challenges regarding the content, scope meaning or legal effect of the [2010] Injunction and this Order." (*Id.* ¶ 3.) Likewise, Article 6.13 is an exercise of discretion within this Court's jurisdiction.

3. This Is Not An Appropriate Case For Judicial Estoppel.

The MPHI Projects incorrectly claim that Article 6.13 contradicts the Rehabilitator's prior unequivocal representation to this Court: "[B]ecause the Ambac policies relevant to the MHPI Cases have not been allocated to the Segregated Account, but remain instead with the General Account, disputes concerning these Projects ***fall outside the jurisdiction of this Court***." (MPHI Objection, p. 8, citing 7/15/16 Rehabilitator's Motion at 6 n.6) (emphasis added).). The

Rehabilitator's statement is consistent with its position that it would not invoke the Rehabilitation Court's jurisdiction to deal with a matter having nothing to do with and having no impact on the rehabilitation case.

For example, if the General Account did not pay a policy claim, the Rehabilitation Court would not be asked to assist in resolving the attendant dispute. But, that is not what Article 6.13 is about. Article 6.13 is about a dispute now resulting from arguments made by the MHPI Projects in other courts that events that have taken place in this rehabilitation case have had certain effects – transfer of assets and receivership of AAC – that, because of Wisconsin's statutory scheme and the manner in which this Rehabilitation was purposefully fashioned, did not occur. An incorrect resolution of this dispute poses the great risk of derailing the Rehabilitation and the Second Amended Plan. The Rehabilitator has never given up, and would never give up, the mandate to protect the rehabilitation effort, and is exercising its discretion now to do so by including Article 6.13 in the Plan.

Article 6.13 expressly addresses the concern stated by the Rehabilitation Court in remarking that it was entering the Military Housing Order to provide guidance to those courts concerning the Wisconsin Court's orders and OCI's intent in structuring the rehabilitation: "I don't want because of ignorance of what has gone on here, because of lack of clarity from this Court that contributes to a lack of understanding in other courts for some court to innocently do something that pulls the thread of the fabric of this rehabilitation and unravels the whole thing. That's my concern." (Oct. 11, 2016 Hrg. Tr., pp. 12 – 18.) Although the Rehabilitator has said nothing in the past inconsistent with its current position, it is worth noting that the MHPI Projects' estoppel arguments ignore the standards for estoppel applicable to government agencies.

4. The Rehabilitation Court's Jurisdiction Is Sufficiently Broad To Permit The Rehabilitation Court To Approve Article 6.13.

The Rehabilitation Court is authorized to approve Article 6.13 because (i) the Rehabilitation Court is tasked with interpreting and applying Wisconsin law, including the segregated account statute and the Act; (ii) the Rehabilitation Court has properly retained jurisdiction in the initial Plan and the First Amended Plan; (iii) the Wisconsin Declaratory Judgment Act authorizes Article 6.13 as a declaration of the scope and effect of the Proceedings; and (iv) the intertwined nature of the General and Segregated Accounts is such that – although they are separate entities for purposes of the segregated account's rehabilitation – they are such an interrelated economic unit that the Appellate Court concluded that "what is in the best interests of Ambac as a whole is also in the best interests of the policyholders in the segregated account." *Nickel*, 351 Wis. 2d 539, ¶ 73.

The Rehabilitation Court – over any other court - has the jurisdiction and authority to interpret and apply these Wisconsin statutes, and to declare and effectuate their application in this case by approving Article 6.13. Specifically, section 645.04 confers exclusive jurisdiction on the courts of the State of Wisconsin. *See* Wis. Stat. § 645.04(1) ("no delinquency proceeding may be commenced under this chapter by anyone other than the commissioner of this state and no court has jurisdiction to entertain, hear or determine any proceeding commenced by any other person"). *See also United States v. Wis. Cir. Ct. for Dane Cty.*, 767 F. Supp. 2d 980, 983 (W.D. Wis. 2011) (Wisconsin laws "set up a comprehensive framework for state insurance rehabilitation proceedings"), *motion granted by* 2013 WL 3466812, *vacated*, 2013 WL 3761295 (W.D. Wis. July 15, 2013).

None of the cases cited by the MHPI Projects involves rehabilitation or the broad jurisdiction granted to the Rehabilitation Court pursuant to chapter 645. *See In re Clark*, 135

Wis. 437, 115 N.W 387 (1908) (validity of incorporation of township); *Frederickson v. Schaumburger*, 210 Wis. 127, 245 N.W. 206 (1932); *Orient Ins. Co. v. Sloan*, 70 Wis. 611, 36 N.W. 388 (1888) (interpleader action commenced and injunction requested from county court to prevent garnishment in county where judgment was rendered); *Syver v. Hahn*, 6 Wis. 2d 154, 159–60, 94 N.W.2d 161 (1959) (Foreclosure action pending in county court precluded foreclosure and sale order by circuit court in later-filed action). The notion that the seven courts in which MHPI and AAC are litigating have jurisdiction "coordinate" with the Rehabilitation Court is antithetical to the Act, which gives the Rehabilitation Court – and only the Rehabilitation Court – jurisdiction over this rehabilitation case.[14]

C. Article 6.13 of the Plan Is Entitled To Comity And Deference From Courts Of Other Jurisdictions.

The MHPI Projects' argument that seven other state courts should decide the impact of the Rehabilitation on AAC's contracts is entirely misguided, and is dangerous to the rehabilitation process envisioned by Wisconsin's legislature in enacting the Insurers Rehabilitation and Liquidation Act ("IRLA"). (*See* MHPI Obj. at pp. 3-4.) It is a previous version of the model law of National Association of Insurance Commissioners that provides for a

[14] The Rehabilitation Court has retained jurisdiction pursuant to the Initial Plan and the First Amended Plan:

> ...(b) to enter such orders and injunctions as are necessary to enforce the respective title, rights, and powers of the Segregated Account, the terms of this Plan, and to impose such limitations, restrictions, terms, and conditions on such title, rights, and powers as the Court may deem necessary;
>
> ... (f) to consider any amendment or modification of this Plan or any Plan Document;
>
> (g) to determine all controversies, suits, and disputes that may arise in connection with the interpretation, enforcement, or consummation of this Plan;
>
> ...(i) to determine such other matters or proceedings as may be provided for under the Act, this Plan, or in any order or orders of the Court, including, but not limited to, the Confirmation Order or any order that may arise in connection with this Plan, the Proceeding, or the Confirmation Order; and
>
> (j) to interpret and enforce, and determine all questions and disputes regarding, the injunctions, releases, exculpations, and indemnifications provided for or set forth in this Plan or the Confirmation Order.

centralized rehabilitation process. The Act requires recognition of injunctions issued by courts of "reciprocal states," Wisconsin defines as "any state other than this state in which in substance and effect ss. 645.42 (1), 645.83 (1) and (3), 645.84 and 645.86 to 645.89 are in force, and in which provisions are in force requiring that the commissioner be the receiver of a delinquent insurer, and in which some provision exists for the avoidance of fraudulent conveyances and preferential transfers." Wis. Stat. § 645.03(1)(i).

As recognized by the Court of Appeals in *Isermann v. MBL Life Assurance Corp.*, 231 Wis. 2d 136, 605 N.W.2d 210 (Ct. App. 1999), without the centralized forum to promote reciprocity, comity and deference, rehabilitation of an insurance company would be impossible. *See id.* at 150-51 (citing *In re Mut. Benefit Life Ins. Co.*, 258 N.J. Super. 356, 609 A.2d 768, 775 (1992) ("The purpose, thus, of the UILA is to provide for a uniform, orderly and equitable method of making and processing claims against financially troubled insurers and to provide for fair procedures for rehabilitating the business of such insurers and, if necessary, distributing their assets. The UILA also recognizes the benefits of centralizing the management of delinquency proceedings in the courts of one state.")). [15]

In *Isermann,* the Court granted comity to the injunction issued by the New Jersey Chancery court upon approval of Mutual Benefit Life's rehabilitation plan in order protect a reinsurer affiliate (MBL Life Assurance Corp. or "MBLLAC") of Mutual Benefit Life. There, the New Jersey injunction was challenged by claims that Isermann sought to litigate in

[15] The *Isermann* court's conclusions are echoed in the Rutgers Law Review Note, *Injunctions Barring Suit Against Insolvent Insurance Companies: State Cooperation Through Tit-For-Tat Strategy,* 57 Rutgers L. Rev. 1377 (Summer 2005). That Note argues that "[i]njunctions are the most common tool to ensure centralization of proceedings and protection of all interested parties" and concludes that "courts must eliminate short-sightedness for states to effectively conduct delinquency proceedings for the benefits of all creditors and to ensure continuing availability and affordability of insurance for the dependent public in rehabilitation proceedings." *Id*. at 1379, 1416. Although not all states have expressly adopted the UILA, comity is generally granted in non-adopting states to orders issued by state courts in insurance rehabilitations in recognition of similar rehabilitation laws and goals.

Wisconsin. The Court rejected the argument that the injunction approved by the New Jersey court should not protect MBLLAC and held that the purposes of the Uniform Insurer Liquidation Act require that comity be granted to plan injunctions that protected MBLLAC from determination of claims by other courts. Upon review of the broad injunction protecting MBLLAC, as reinsurer, the *Isermann* court concluded that the scope of the injunction was justified by the purposes served by state rehabilitation laws, was in the public interest and that Mutual Benefit and its successor/reinsurer, MBLLAC, were both entitled to protection from the New Jersey rehabilitation court's plan injunction. Thus, comity was granted in Wisconsin to that injunction. There is no basis to believe now that courts of other jurisdictions will not observe the same rule of law.

D. Article 6.13 Has No Due Process Impact on the MHPI Projects.[16]

The MHPI Projects ignore the language of the very Constitutional provision on which they rely in support of their Due Process argument. As art. I, § 9 of the Wisconsin Constitution states "[e]very person is entitled to a certain remedy ... <u>conformably to the laws.</u>" (Emphasis added). Wisconsin courts have applied the language "conformably to the laws" to hold that art. I, § 9 does not entitle Wisconsin litigants to the exact remedy they desire, but merely to their day in court. *See Wiener v. J.C. Penney Co.,* 65 Wis. 2d 139, 150–51, 222 N.W.2d 149 (1974) (citing *New York Life Ins. Co. v. State*, 192 Wis. 404, 412, 211 N.W. 288, 212 N.W. 801 (1927)).

Article I, § 9 of the Wisconsin Constitution is not violated by the Rehabilitator's application of the pre-existing Act in these Proceedings. The cases MHPI Projects cite are inapposite. For example, *State ex rel. Blockwitz v. Diehl*, 198 Wis. 326, 223 N.W. 852, 853 (1929) on which they rely to claim that "wholesale removal of a remedy is prohibited" (MHPI

[16] The Rehabilitator disputes that the MHPI Bondholders' have any Due Process rights to begin with for the additional reasons stated above. (*See Supra* Section II.)

brief, p. 11-12) dealt with retroactive legislation, not application by the judiciary or executive branch of a pre-existing law. Likewise *Soc'y Ins. v. LIRC*, 2010 WI 68, ¶ 5, 326 Wis. 2d 444, 786 N.W.2d 385, held the legislature's retroactive application of a statutory amendment to be unconstitutional. To the extent that Article 6.13 could be considered a modification of the MHPI policies, such a modification of an insurance contract as a result of regulation is foreseeable in light of states' pervasive and long-standing regulation of insurance industry.[17]

CONCLUSION

For the foregoing reasons, the Rehabilitator respectfully requests that that the Court grant its Motion to approve the Second Amended Plan and enter the Confirmation Order to effectuate the Segregated Account's exit from Rehabilitation.

[17] Yet another reason to overrule the MHPI Projects' objection is the numerous misstatements in their submission. For example, MHPI Projects suggest that AAC has conceded that the state courts handling the MHPI litigations have "jurisdiction" to decide whether an AAC Default / Credit Enhancer Default has occurred. (MHPI Obj. at pp. 3-4.) However, The MHPI Projects' statement is misleading in that AAC has repeatedly argued that the MHPI Projects have no standing to raise an AAC Default / Credit Enhancer Default, and standing goes to a court's jurisdiction. Also, AAC has repeatedly argued that the state courts handling the MHPI litigations should, as a matter of Full Faith and Credit and comity, defer to the Wisconsin Court's own rulings regarding the scope and meaning of its orders.

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