

In the Matter of the Rehabilitation of:

Case No. 10 CV 1576

SEGREGATED ACCOUNT OF  
AMBAC ASSURANCE CORPORATION

**AFFIDAVIT OF FREDERICH J. BINGHAM IN SUPPORT OF ALL STUDENT LOAN  
AND LLOYDS TSB BANK plc's MOTION TO MODIFY TEMPORARY  
INJUNCTION AND TO INTERVENE**

State of Illinois                    )  
  ) ss  
County of Kane                    )

Frederich J. Bingham, being first duly sworn, on oath, deposes and states as follows in this Affidavit:

1. I am currently a principal of Glynloen Consulting, a firm that renders services to solvent and insolvent insurance and reinsurance entities, Guaranty Funds, Receivers, Insurance Regulators, and various other insurance related entities. Attached hereto as Exhibit A is a copy of my Curriculum Vitae.
2. I am a Certified Insurance Receiver – Multiple Lines Designation, with the International Association of Insurance Receivers (“IAIR”), which recognizes me within this international organization of insurance experts as possessing the highest level of competency in the disciplines of Receiverships and Run-Offs. It is IAIR’s highest level accreditation.
3. Prior to my current position, I was a project consultant of Navigant Consulting, Inc., a publicly held consulting company, from November 2008 to January 2010, where my responsibilities included developing a practice for troubled insurance companies;, working as

part of a team of experts testifying on behalf of a Receiver for a company in Liquidation and advising various parties on insurance/ regulatory matters within my areas of expertise.

4. Prior to my position at Navigant, I was employed as Claims and Reinsurance Officer at the Office of the Special Deputy Receiver, from October 1994 to November 2008. The Office of the Special Deputy Receiver performs the functions of the Illinois Director of Insurance as statutory receiver for insolvent insurers/ reinsurers domiciled in the state of Illinois. As Claims and Reinsurance Officer for the Office of the Special Deputy Receiver, I oversaw the Claims, Claims Service, Reinsurance and Special Project departments for the conservation, rehabilitation and liquidation operation of the State of Illinois. This officer level position was responsible for the management, administration and production of approximately 120 personnel. I was responsible for the assets, claims and receivables of approximately 80 insurance companies in various stages of receivership. I represented the state of Illinois on the NAIC working groups responsible for developing Model Legislation for Receiverships and Guaranty Funds. I also acted as an advisor to the Director of Insurance and the Illinois Department of Insurance where I provided and implemented proposals to place impaired companies into receivership.

5. Prior to my work for the Office of the Special Deputy Receiver, I was an Executive Consultant/Vice President, working for Peterson Consulting in Chicago, Illinois. In this capacity I helped Peterson develop a specialized practice assisting Receivers, State Departments and Guaranty Funds on claims, reinsurance and system matters pertaining to financially troubled companies. I was a Branch Claim Manager at CNA Insurance prior to Peterson Consulting. I was an Assistant Superintendent at USF&G Insurance Company prior to CNA. Prior to that I was an adjuster with the Hartford Insurance Company.

6. I have testified as an expert in the cases that are set out in my Curriculum Vitae.

7. I make this Affidavit in support of ALL Student Loan and Lloyds Bank's June, 2010 Motion to Modify Injunction and to Intervene.

8. From my limited review of the court filings in this matter, it is my understanding that, on March 21, 2010, Ambac's board of directors, with the approval of the Commissioner of Insurance for the State of Wisconsin, voted to (1) establish the Segregated Account that is the subject of this proceeding, and (2) take the ALL policies and Lloyds Bank Surety Bond out of Ambac's General Account and transfer them to the Segregated Account, along with other liabilities.

9. I have reviewed the Verified Petition for Order of Rehabilitation of Ambac Assurance Corporation ("Ambac"). The Verified Petition, ¶8(a), calls for the establishment of a Segregated Account in accordance with a "Plan of Operation." Paragraph 12(c) calls for a "Payment Plan" for policies allocated to the Segregated Account but contains no detail as to the split between the cash payments and the surplus notes, and only states that it is a "formulated plan" to be set out in the Rehabilitation Plan which has yet to be published.

10. Based on knowledge, information and belief, ALL Student Loan, Lloyds and others have asked for information and documentation to support the basis for many of the statements made in support of the Rehabilitator's Plan of Operation, including support for the Reinsurance Agreement, Secured Note, Collateral, and statements by the Rehabilitator that the Segregated Account was required to "have and maintain an adequate amount of capital and surplus." I have been advised that this information was not provided to ALL Student Loan and Lloyds and I have not been able to review it.

11. I have reviewed the Plan of Operation, including Section V regarding the “Provision for Capital and Surplus,” which provides that “The Segregated Account will support the liabilities allocated to it with the following resources,” and lists four resources:

(1) A \$2 billion Secured Note the principal of which is not payable in full for forty (40) years, subject to “mandatory prepayments” of cash for claim liabilities, loss settlements, commutations, surplus notes on Covered Policies “in accordance with the Plan of Rehabilitation” and administrative expenses or other amounts “as ordered by the Rehabilitator” minus the liquid assets available to the Segregated Account. I have not seen the Plan of Rehabilitation and I am advised that it has not yet been published.

(2) An Aggregate Excess of Loss Reinsurance Agreement (“Reinsurance Agreement”) which provides that Ambac agrees to reinsure the Segregated Account, above the amounts covered under the \$2 billion Secured Note, whereby the Segregated Account may cede the losses under the Covered Policies as they come due to Ambac according to the Plan of Operation.

(3) Surplus Notes: The Plan of Operation provides that the general account may issue surplus notes to the policyholders of the Segregated Account “in accordance with the Plan of Rehabilitation” if the cash payments and surplus notes from that account are insufficient to pay claims liabilities.

(4) Collateral Security: The Plan of Operation also sets out the collateral that the Segregated Account will have in the General Account as security for the obligations of Ambac in the Secured Note, and those are the installment premiums for the policies allocated to the Segregated account, including those under direct and assumed reinsurance agreements as well as the reinsurance recoveries for those losses and remediation/reimbursement/collection rights associated with the policies.

12. Section V of the Plan of Operation has a provision that provides that the General Account will not have liability to the Segregated Account in the following fashion:

In no case will the Company’s general account have any liability to make payment to the Segregated Account under the Secured Note to the extent that such payment would result in the surplus as regards policyholders of the Company’s general account falling below \$100 million (or such higher amount as determined by OCI pursuant to a prescribed accounting practice) and for any period during which the surplus as regards policyholders of the Company’s general account is below such amount.

This limitation is on potential liability of the \$2 billion Secured Note (§ 1(c)) and also as a Coverage Limit on the Reinsurance Agreement (§ 1.04).

13. The Secured Note does not have the exact same language as the Plan of Operation regarding this limitation, but has Section 1(c) with the heading “Limitation on Liability of Maker” which provides that:

Notwithstanding any other provision of the Note, Ambac will have no obligation to make any payments that make its surplus as regards policyholders, as reflected on its statutory financial statements, (its “Surplus”), is [sic] less than \$100 million, or such higher amount as determined by OCI pursuant to a prescribed accounting practice, (“the **Surplus Amount**”), or to the extent that such payment would result in Maker’s Surplus being less than the Surplus Amount, *it being understood that* any principal payment deferred as a result of the foregoing shall, unless otherwise agreed by Payee, be due and payable (together with accrued and unpaid interest thereon at the rate provide in clause 1(b) above, accrued but through the date of payment) at such time as the payment thereof would not result in the Maker’s Surplus being less than the Surplus Amount.

14. I have reviewed the Rehabilitator’s Consolidated Brief in Opposition to All Motions Scheduled for Hearing on September 9, 2010 (“Consolidated Brief”). In his brief (p.18), he states that “the Segregated Account has access to all of the assets of Ambac, in pari passu with General account policyholders, unless the payment of claims would cause Ambac’s assets to fall below \$100 million, a number that constitutes less than two percent of Ambac’s claim paying assets.”

15. I have further reviewed the Rehabilitator’s Consolidated Brief where it states on page 19 that “the Segregated Account was capitalized with more than 98 percent of Ambac’s current assets, despite being allocated the liabilities of less than 1,000 of the 15,000 policies.”

16. The Rehabilitator’s statements in the Consolidated Brief set out in paragraphs 14 and 15 are not supported by sufficient facts and documents. The only support that may be utilized for such statements (that have been made available to me through ALL and Lloyds) could be based on the four sources set out in of the Plan of Operation’s “Provision for Capital and Surplus” set forth in paragraph 11 above. However, in my professional opinion, based on

my knowledge, experience and training, those four sources do not support the conclusion that:

(a)“the Segregated Account was capitalized with more than 98 percent of Ambac’s current assets, despite being allocated the liabilities of less than 1,000 of the 15,000 policies;” or (b) “the Segregated Account has access to all of the assets of Ambac, in pari passu with General account policyholders, unless the payment of claims would cause Ambac’s assets to fall below \$100 million, a number that constitutes less than two percent of Ambac’s claim paying assets.”

17. First, the Consolidated Brief has a concept that “adequate capital and surplus” in the Segregated Account may be supported by the Secured Note and Reinsurance Agreement notwithstanding the fact that each of those documents has provisions that make payment to the claimants conditional on various events that are unrelated to the policies that were originally issued by Ambac (the original insurer).

18. Second, the term “surplus” is intended to ensure that there were more assets than liabilities in the Segregated Account when that account was formed. In this case, the Segregated Account was formed as an offshoot of a going concern, i.e. after Ambac was in existence for a long time and had policies in effect with active losses and premiums. Thus, the statute in question, 611.24(3)(a) titled “Special Provisions For Segregated Accounts,” required that if such a “segregated account is established after a certificate of authority has been issued, the commissioner shall require the corporation to have and maintain an adequate amount of capital and surplus in the segregated account.”

19. The only way that anyone could gauge whether there was adequate capital and surplus in the Segregated Account would have been, at a minimum, to determine the current paid losses and the future case and Incurred But Not Reported (IBNR) reserves for all of the Covered Policies that were being allocated to the Segregated Account, determining the ownership, value

and liquidity of the assets pledged to the Segregated Account and then balancing the liabilities against the assets. There is no indication from the information made available to ALL and Lloyds or in the public record that I have reviewed that this has been performed. More importantly, the statements that Ambac was in a hazardous financial condition before it moved the toxic policies to the Segregated Account in order to protect the policies with no claims that remain in the General Account are wholly contrary to a conclusion that there could possibly be adequate capital, much less “surplus” in the Segregated Account.

20. The Wisconsin statutes, §§ 611.19 and 611.24(3)(a) refer to minimum capital and surplus requirements in the context of “Initial capital and surplus requirements” or “in the certificate of authority of a newly organized corporation.” These statutes are not the ones that I would refer to as applicable where again, there are existing policies transferred into a corporation, and there is another statutory provision that requires adequate capital and surplus for the liabilities associated with those policies.

21. The concept of being “adequately capitalized” involves assessing financial strength or weakness utilizing a number of metrics and measures in addition to bare assets. These measures and metrics include, among others, total fixed income, total equity, current liabilities, current loss and ALAE reserves, previous year’s net earned premium volumes, current statutory surplus and some review of the combined loss ratios.

22. Whatever value the Secured Note has for counting towards a calculation of surplus is dubious because of the numerous contingencies contained therein which make the terms, timing and amounts of payments very speculative. I have worked for and with state Departments of Insurance and with Plans of Rehabilitation under statutory language similar to the language in Wisconsin and the fact is that Plans of Rehabilitation are always subject to

modification by the Rehabilitator and Court. Moreover, the “mandatory prepayments” under the Note call for payouts of “surplus notes’ which must be subordinated to all other policyholder, claimant and beneficiary claims, and all other classes of creditors other than surplus note holders, and require that interest and principal repayments require prior approval of the Commissioner. In short, the Note is based on conditional, uncertain payments, some of which can be subordinated and modified if the Rehabilitator and Court decide to modify the Plan of Rehabilitation.

23. The Rehabilitator asserts that Reinsurance Agreement (attaching above the Secured Note) is protecting the Segregated Account. Again, this is a key element of his support for his surplus argument alleging the Segregated Account has access to 98% of the assets of Ambac. However, in this case, the Reinsurance Agreement is issued by the same company that issued the underlying insurance policies it is now purporting to reinsure. Therefore, to afford identical protection there should be no conditions: that is, if it is to afford identical protection as the original policy, it should be 100% reinsurance above the Secured Note and as solid as the insurance policy that it replaces. The inclusion of so many contingencies in the Plan, the Note and the Reinsurance Agreement makes this result difficult to foresee and impossible to infallibly predict.

24. Section 4.01 of the Reinsurance Agreement purports to be a standard “follow the fortunes” clause. However, it has a significant caveat whereby the protection of the Segregated Account, as the cedent, under such a clause is illusory, as it states that the reinsurer’s liability follows that of the cedent “except as modified by the Plan of Rehabilitation” and again, no such Plan has been filed and any such plan, may be modified by the Rehabilitator and the Court at any time. The follow the fortune clause is one of the most significant protections for the cedent

under a reinsurance clause and, if it is severely undercut in this manner, the reinsurance contract as a whole is undercut. In the absence of a “follow the settlements” clause and with a “follow the fortunes” clause that has a caveat that makes it effectively unenforceable, the Reinsurance Agreement is hardly the same as permitting the creditors of the Segregated Account to have “access to all of the assets of Ambac.”

25. The “finite aggregate reinsurance” is defined under section 1.02 and calls for payment of cash claim payments, including ALAE, loss settlements, commutations and various other payments. It also provides for payments of secured notes but only for surplus notes issued to claimants if the cash or interest payments are authorized for payment by the Rehabilitator. However, all of these payments must be “in accordance with the Plan of Rehabilitation and not otherwise disapproved by the Rehabilitator.” This would effectively allow the Rehabilitator to order the Segregated Account to potentially cover/ pay/ accelerate claims by amending the Plan of Rehabilitation while at the same time refusing to cover the same claim when presented to the Reinsurer, which is actually the General Account of what was the same company. This is not the case with contracts between a policyholder and an insurance company negotiated at arm’s length in the marketplace where a party may rely on the sanctity of the contract. In short, the reinsurance contract is capable of being rendered illusory, one-sided, of dubious value and may afford little actual protection for the policyholders.

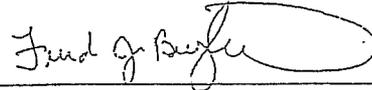
26. The Rehabilitator’s theory of protecting the assets of the General Account by segregating the “toxic policies” into the Segregated Account is contradicted by his other assertion that “the Segregated Account has access to all [except 2%] of the assets of Ambac, in pari passu with General account policyholders.” The only way to accomplish such protection is if the Plan of Rehabilitation, which is yet to be published, would be to create preferences

amongst the same class of claimants, i.e. policyholders, which is repugnant to industry and statutory methods of fair treatment of creditors in a rehabilitation or liquidation.

27. More specifically, the only way to protect the policyholders in the General Account who ostensibly do not have claims, from those in the Segregated Account, who do have claims, is not to pay the claimants in the Segregated Account when their claim are presented and due, but to pay them over time. The problem with this is that it creates a second-tier of creditors in the same class or, otherwise stated, a “preference” among the same class of creditors by creating one subclass versus another subclass of the same class of creditors.

28. The “Payment Plan” for policies allocated to the Segregated Account set out in the Verified Petition refers to a “formulated plan” to be set out in the Rehabilitation Plan, and calls for a split between immediate cash payments and interest bearing surplus notes. This is a nebulous concept that would create a preference among the same set of creditors, i.e. policyholders and the third party beneficiaries, who under Wisconsin law are treated equally, both generally (“equitable apportionment” under § 645.01) and for purposes of distribution of assets in Receivership (§ 645.68). I have practiced in this area for 20 years and, based on my knowledge, experience and training, it is against good industry custom and practice to create any Plan in Rehabilitation or Receivership that treats policyholders or their third party claimants disparately as class creditors as does this Ambac Plan of Operation with the Segregated Account on the basis selected by OCI in this case. It is even more egregious in that it punishes the ALL and Lloyds policyholder/third party claimant simply because they have claims, irrespective of the reason those claims arose.

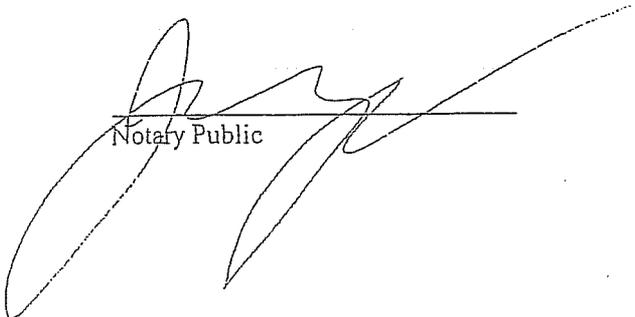
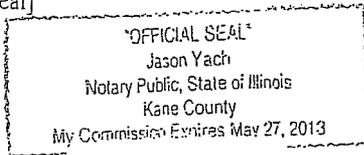
FURTHER AFFIANT SAYETH NAUGHT.



Frederich J. Bingham

Subscribed and sworn to before me this 31<sup>st</sup> day of August, 2010

[Seal]



Notary Public

Notary Public

My Commission Expires:

05/17/13

## Frederich J. Bingham, CIR-ML

Frederich J. Bingham, CIR-ML

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### Professional History

- Principal, Glynloen Consulting
- Project Consultant, Navigant Consulting
- Claims and Reinsurance Officer, Office of the Special Deputy Receiver
- Executive Consultant / Vice President, Peterson Consulting
- Branch Claim Manager, CNA Insurance
- Assistant Superintendent, USF&G Insurance Company
- Adjuster, Hartford Insurance Company

### Education

- Bachelor of Arts, History  
Centre College

### Professional Associations

- Certified Insurance Receiver – Multiple Lines, International Association of Insurance Receivers
- Hearing Board, Attorney Registration and Disciplinary Commission
- Oversight Board, Attorney Registration and Disciplinary Commission
- Tutor, Literacy Volunteers of Illinois, Illinois Youth Center- St Charles
- Chairman, Advisory Council- Stateville, Kairos Prison Ministry International

As a seasoned senior level Insurance, Reinsurance, Regulatory and Run-Off Practitioner with over 31 years of industry, consulting and receivership experience, Mr. Bingham possesses a demonstrated ability to lead diverse teams of professionals to new levels of success in a variety of competitive, fast paced and evolving environments. He has strong technical, managerial and board level qualifications with an impressive track record of hands-on involvement in strategic planning, change management, project direction and departmental leadership. Mr. Bingham has proven his ability to successfully analyze an organization's critical business requirements, identify deficiencies and potential opportunities, and develop innovative and cost-effective solutions for enhancing competitiveness, improving service, increasing production and widening organizational vision and commitment.

Mr. Bingham has demonstrated an understanding and command of Claims, Reinsurance, Regulatory and Run-Off issues of the highest complexity. He offers strong and quantitatively based analyses and solutions quickly and in highly pressurized business situations.

As a recipient of the Certified Insurance Receiver – Multiple Lines Designation, Mr. Bingham has been recognized by the International Association of Insurance Receivers as possessing the highest level of competency in the disciplines of Receiverships and Run-Offs.

### Recent Professional Experiences

Mr. Bingham, throughout his distinguished career has developed significant experience in the insurance and reinsurance industry. The following provides recent highlights of his extensive industry experience.

- » Developed claims performance metrics to measure, improve and plan major claims activities. Productivity improved 238% in 4 months.

## Frederich J. Bingham, CIR-ML

- » Collected over \$100 million in reinsurance in last 5 years.
- » Performed several reserve adequacy studies for troubled property and casualty, life and accident, auto warranty and workers compensation carriers.
- » Working as expert for Director as Receiver in pursuit of company's Directors and Officers, Risk Managers and Financial Advisors for regulatory noncompliance and violations of their Certificate of Authority.
- » Testified as Receiver's expert in the case of Legion Indemnity Insurance Company. The judge ruled in favor of the Receiver and ordered Legion into liquidation.
- » Successfully concluded major asbestos litigation which exposed \$45 million of coverage. Obtained court approved settlement for \$31,950,000.
- » Developed a two year operational plan which directed all claims activities including the evaluation, adjudication and payment of tens of thousands of claims and the collection of the commensurate reinsurance.
- » In the last 5 years, led teams which closed 14+ open estates and distributed in excess of \$150 million to the creditors of the insolvent companies.
- » Successfully concluded the liquidation of 5 self-insured workers compensation funds. Three of five pools paid lost wage benefit at 100%.

### **Representative Business Experience**

- » As Claims and Reinsurance Officer for the Office of the Special Deputy Receiver, Mr. Bingham oversaw the Claims, Claims Service, Reinsurance and Special Project departments for the conservation, rehabilitation and liquidation operation of the State of Illinois. This officer level position was responsible for the management, administration and production of approximately 120 personnel.
- » Acted as an advisor to the Director of Insurance and the Illinois Department of Insurance. Provided and implemented proposals to place subject companies into receivership.
- » Handled the assets, claims and receivables of approximately 80 insurance companies in various stages of receivership. Direct responsibilities include mentoring, staffing, budgeting, training and supporting the various functional departments with the goal of marshalling all the assets, evaluating the claims, collecting the reinsurance and subsequently closing the estates.
- » Represented the state of Illinois on the NAIC working groups responsible for developing Model Legislation for Receiverships and Guaranty Funds.

## Frederich J. Bingham, CIR-ML

- » As a board member, was responsible for identifying organizational risk and implementing cost effective, auditable control strategies. Duties included being a member of the executive compensation committee and the design and administration of OSD's self-insured health plan.
- » Working for Peterson Consulting in Chicago, Illinois, began as an executive consultant in the firm's insurance practice. Helped Peterson develop a specialized practice assisting receivers, state departments and guaranty funds on claims, reinsurance and system matters pertaining to financially troubled companies.
- » Led major projects responsible for the physical control of 1 million files, the evaluation and adjudication of 150,000 claims, the coding and capture of reinsurance billing information and the performance and productivity of over 100 personnel.
- » Worked on numerous engagements and in testifying roles for major clients in Illinois, New York, Texas, Tennessee, Utah and others.
- » Promoted to Vice President in December 1993 and was integral in directing the future of the insolvency practice including the procurement and performance of a large number of diverse Run-Off and Receivership projects.
- » With almost 10 years of experience at CNA Insurance, Mr. Bingham began as a supervisor responsible for 7 adjusters handling all lines of professional liability and excess claims.
- » Promoted to Liability Division manager in May 1985. Responsible for 6 supervisors and 45 adjusters handling all claims involving serious injuries, complex coverage issues and major litigation.
- » Promoted to Regional Casualty Specialist in July 1986 to assist Regional Claims Manager. Handled all non-property matters for the 8 offices in the region, including technical, staffing, budgeting, training and system issues for same. Acted as Regional Coordinator for Subrogation, Medical Cost Containment, Workers Compensation and Legal file management. Worked on a team to centralize all Asbestos, Environmental and Toxic tort claims in Home Office location.
- » Promoted to Branch Claim Manager in April 1988 to run the Claims Department in Cleveland, Ohio. Responsible for 7 supervisors and 53 adjusters handling all claims in the state of Ohio and Northern Kentucky.
- » Worked for almost 5 years at USF&G Insurance Company in Cincinnati, Ohio and with Hartford Insurance Company in Lexington Kentucky.
- » Handled all lines of claims, including major contract surety cases and specialized in complex workers compensation claims, specifically Longshoreman and Harbor workers cases.
- » Began as adjuster trainee and was eventually promoted to Assistant Superintendent.

## Presentations

- » National Association of Insurance Commissioners; Hosted International Association of Insurance Receivers Roundtable; Chicago, IL; September 2003.
- » International Association of Insurance Receivers Insolvency Workshop; "Contested Receiverships"; Miami, FL; January 2004.
- » International Association of Insurance Receivers Joint Guaranty Fund / Receivers Conference; "Recovering Reinsurance Foreign and Domestic"; San Diego, CA; November 2004.
- » International Association of Insurance Receivers Insolvency Workshop; "Debating the Merits of State versus Federal Based Regulation"; Orlando, FL; January 2005.
- » Mealey's Fundamentals of Reinsurance and Insolvency Conference; "The Basics of Receivership Reinsurance Practice"; Chicago, IL; October 2003.
- » AON's Association of Risk Managers; "What to Expect When Filing Your Claim in a Receivership Proceedings"; Chicago, IL; July 2005.

## Testimony Experience

- » J. Anthony Clark, Illinois Director of Insurance as Receiver v. Legion Indemnity Insurance Company; Expert opinion report, sworn deposition testimony, sworn testimonial opinion.
- » Nathaniel Shapo, Illinois Director of Insurance as Receiver v. Illinois Environmental, Expert opinion report; sworn deposition testimony.
- » Nathaniel Shapo, Illinois Director of Insurance as Liquidator v. Alliance General Insurance Company; Expert opinion report, sworn deposition testimony.
- » Mark Boozell, Illinois Director of Insurance as Receiver v. Merit Insurance Company; Expert opinion report, sworn deposition testimony, sworn testimonial opinion.