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September 8, 2010

DELIVERED VIA MESSENGER

Mr. Carlo Esqueda
Clerk of Circuit Court
Dane County Courthouse
215 South Hamilton Street
Madison, Wisconsin 53703-3285

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

Dear Mr. Esqueda:

Enclosed find for filing an original and one copy of Depfa Bank, plc's Brief in Opposition to OCI's Motion to Strike Improper Reply Arguments and Affidavits as it relates to Depfa's previously filed Combined Reply Brief in Support of its Motion to Intervene and to Modify March 24, 2010 Order for Temporary Injunctive Relief. Please return the file-stamped copy to me via our messenger.

Depfa notes that most of OCI's Motion does not relate to Depfa's Combined Reply Brief; it appears from a review of OCI's motion papers that the only Depfa material OCI seeks to strike is Depfa's "shadow rehabilitation" argument set forth on pages 9 and 10 of its Combined Reply Brief. As discussed in Depfa's opposition brief being filed today, this argument was raised in Depfa's initial June 22nd filing and OCI's Motion should be denied.

By copy of this letter, counsel for the State of Wisconsin Office of the Commissioner of Insurance and for Ambac are being served. We also are serving a three-fold punched courtesy copy of this filing upon Judge William D. Johnston, care of the Lafayette County Clerk of Circuit Court, by messenger today as well.

We thank you for your courtesies in this matter. If you have any questions, please contact Greg Lyons or Seth Dizard of this office, or me.

Sincerely,



Grant C. Killoran

GCK/kas
Enclosures

c: Hon. William D. Johnston (c/o Clerk of Lafayette County Circuit Court
(w/enc.) (via messenger)
Thomas J. Welsh, Esq. (w/enc.) (via e-mail)
Seth E. Dizard, Esq. (w/enc.)
Gregory W. Lyons, Esq. (w/enc.)
Michael B. Van Sicklen, Esq. (w/enc.) (via e-mail)
Daniel W. Stolper, Esq. (w/enc.) via e-mail
Service List (w/enc.) (via e-mail)

In the Matter of the Rehabilitation of:

Case No. 10-CV-1576 – B

Segregated Account of Ambac Assurance Corporation

**DEPFA BANK'S BRIEF IN OPPOSITION TO THE COMMISSIONER'S MOTION TO
STRIKE IMPROPER REPLY ARGUMENTS AND AFFIDAVITS**

INTRODUCTION

Depfa Bank, plc ("Depfa") submits the following brief in opposition to the motion to strike filed by the Wisconsin Office of the Commissioner of Insurance (the "Commissioner") dated September 3, 2010.

The Commissioner's motion as it pertains to Depfa should be denied. It is based on the Commissioner's erroneous claim that an argument appearing on pages 9-10 of Depfa's Combined Reply Brief in Support of its Motion to Modify March 24, 2010 Order for Temporary Injunctive Relief is new. The Commissioner is wrong. Depfa's purportedly new argument – found in a section of Depfa's Combined Reply Brief entitled "The 'Shadow Rehabilitation' of Ambac and the Injunction Protecting Ambac Exceed the Court's Jurisdiction" -- was raised and discussed in Depfa's June 22, 2010 initial brief and, as such, the Commissioner's motion should be denied.¹

¹ The Commissioner's motion does not explicitly address, challenge or move to strike the Affidavit of Attorney Gregory W. Lyons filed with Depfa's Combined Reply Brief. Nor could it. The Lyons Affidavit submits three public documents – two from rating agencies, Moody's Investor's Service and Standard & Poor's, and one from the International Swaps and Derivatives Association – all of which directly respond to the Commissioner's opposition (OCI Opp., 9/9/10 at 5) and to Moody's document on which the Commissioner relied in opposing Depfa's opening brief (Van Sicklen Aff., Ex. 3).

ARGUMENT

I. Depfa Explicitly Raised The Challenged Argument In Its Opening Brief.

Contrary to the Commissioner's last-minute motion to strike (filed at the close of business on the Friday preceding a holiday weekend, which itself precedes two hearings in this case by only a few days), Depfa expressly placed the Commissioner on notice in its June 2010 initial brief that it was challenging the creation of the Segregated Account as a "shadow rehabilitation" of Ambac as a whole and that the injunction improperly prevented Depfa from bringing suit against Ambac, an insurer that is not in formal rehabilitation proceedings but is the contracting party named in insurance policies under which Depfa is entitled to coverage. Depfa's opening brief explicitly challenged these proceedings on grounds that the injunction, issued at the Commissioner's request, improperly prevents any party from challenging Ambac for issues relating to the Segregated Account, thereby restraining Depfa from pursuing its legal rights against Ambac. For instance, Depfa's opening brief states:

[T]he Commissioner and Ambac are working together to . . . protect the Ambac General Account from claims of policyholders without placing Ambac as a whole into rehabilitation or liquidation. Such a result is untenable and a clear abuse of the Commissioner's authority and fiduciary responsibilities.

In effect, the Commissioner has established a non-judicial receivership over both the Segregated Account and Ambac. The Commissioner and Ambac benefit from the Temporary Injunction restraining all actions by policyholders in the Segregated Account from challenging Ambac's furtive establishment of the Segregated Account.

Depfa's Opening Brief at 14. Depfa's opening brief continues:

Through the Segregated Account Rehabilitation Order the Court effectively has established jurisdiction over policies in the Ambac General Account without providing policyholders the benefits of a statutorily-authorized and regulated rehabilitation proceeding. This "shadow" rehabilitation violates the letter and spirit of Wisconsin rehabilitation law.

Id. at 16. In fact, when listing the ways the Commissioner's actions were unlawful in its opening brief, Depfa even highlighted this issue in a bullet point at the outset of that brief:

- The Commissioner exceeded his authority by attempting a judicial rehabilitation of Ambac without formally placing Ambac into rehabilitation.

Id. at 3.

Depfa's Combined Reply Brief responds to the justifications offered in the Commissioner's opposition by, among other things, reiterating the impropriety of this "shadow rehabilitation" and the unlawful expansion of the Court's jurisdiction by purporting to restrain parties from bringing actions against Ambac. *See, e.g., Id.* at 10 ("the Injunction . . . impermissibly prevents parties from bringing actions against Ambac, which is not itself in rehabilitation" and "constitutes an impermissible 'shadow rehabilitation' of Ambac."). In addition, both Depfa's initial brief and its Combined Reply Brief seek the same appropriate result: rehabilitation of Ambac as a whole. The Commissioner cannot plausibly argue that it is "fundamentally unfair" for Depfa to reiterate in a reply brief its argument in its initial brief opposing the unlawful shadow rehabilitation of Ambac.

Simply put, the Commissioner's assertion that Depfa's Combined Brief raises a new argument is demonstrably incorrect. The Commissioner has had ample opportunity to address Depfa's argument. Indeed, the Commissioner took full advantage, filling nearly two pages and 20 footnotes of criticism of Depfa's spotlighting of the Ambac "shadow rehabilitation." *See, e.g., OCI Opp.* 9/9/10 at 27-28, nn. 20-36. The Commissioner even directly references an "implicit" argument made by the "Movants" (including Depfa) in favor of rehabilitation of Ambac as a whole. *Id.* at 5. As such, the Court must reject the Commissioner's claim of unfair surprise and deny the motion to strike with respect to Depfa.

II. Any Confusion As To The Proper Time To Challenge The Segregated Account Is A Direct Result Of The Commissioner's Unsupported And Inappropriate Collateral Estoppel Argument And Ambiguity In The Injunction Order.

In addition to unjustifiably claiming surprise regarding Depfa's "shadow rehabilitation" argument, the Commissioner asserts that the Movants have not demonstrated sufficient justification for setting forth arguments and affidavits past the June 22, 2010 deadline for submitting opening briefs challenging the Court's Order for Temporary Injunction. *See* OCI Motion to Strike at 3-4. In this respect, the Commissioner has no one to blame but himself for any muddying of the record. Much of what the Movants submitted on reply may be traced to the Commissioner's improper collateral estoppel argument that purports to bar any future challenge to the Segregated Account unless raised during these summary proceedings. *See* OCI Opp., 9/9/10 at 12-17.

The Commissioner argues that nearly all Movants, having had notice and opportunity to be heard at the May 25, 2010 hearing on the Wells Fargo and RMBS "emergency motions" and to file an opening brief on June 22, 2010, have now waived any future opportunity to challenge the validity of the Segregated Account for reasons not otherwise raised by June 22, 2010. *See* OCI Opp., 9/9/10 at 17 ("In sum, there is no reason for the Court to ignore its prior decisions on the validity of the Segregated Account."). The Commissioner goes so far as to suggest that he will take the position that the parties are precluded from ever raising these issues again, including during future hearings on the as yet undisclosed Rehabilitation Plan. *Id.* at 45 ("This Court should continue to reject Movants' open-ended invitation to transform the "management task" of rehabilitation to protect collective interests into an impractical, adversarial legal battle.") As Depfa has noted in its Reply Brief, the Commissioner improperly seeks to collaterally estop the parties from litigating the propriety of the Segregated Account, and to foreclose all future

challenges to the Segregated Account. *See* Depfa Reply Brief at 11-13. The Commissioner clearly is overreaching, as such an application of collateral estoppel is contrary to the argument advanced by the Commissioner that these are "flexible" proceedings and also is contrary to Wisconsin law, which requires that the precluded issue was *actually litigated and determined*, not merely dealt with in summary "management" proceedings, as has been the case here. *Id.* at 11.

In light of the Commissioner's suggested threat in his opposition brief that he intends to go on the offensive with an improper collateral estoppel argument, it should come as no surprise that the Movants would submit arguments and affidavits on reply. Were the Court to accept the Commissioner's position in total, the appellate record could be wrongly and unfairly limited to the narrow issues raised by Wells Fargo and the LVM Bondholders in self-described "emergency motions" at the outset of these proceedings, and well before the June 22nd filing deadline established by the Court. The Court should reject this apparent attempt by the Commissioner to limit the record and deny the Commissioner's motion to strike in its entirety.²

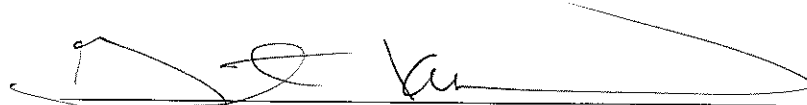
² In addition, much of the procedural confusion that has permeated this rehabilitation proceeding from the very start, and in particular the confusion over the motions invited under paragraph 12 of the Injunction Order, stems from ambiguity within paragraph 12 drafted by the Commissioner. On the one hand, the Commissioner's general position has been that paragraph 12 simply affords parties an opportunity to be heard regarding continuing injunctions (or temporary restraining orders) that originally were entered without notice and an opportunity to be heard. However, the language of paragraph 12 mandates that a party contest "*any portion* of this Order" that the party believes is "unwarranted by the facts or the law...." Injunction Order at 12 (emphasis added). Given that the entire Injunction Order is expressly based on the need to "promote the equitable and orderly rehabilitation of the segregated account," paragraph 12 could be read to mandate that parties object, prior to June 22, 2010, to provisions of a rehabilitation plan that has not yet been filed. *Id.* at 1. Such an absurd result must, of course, be rejected. Rather than filing ill conceived (and, as to Depfa, factually unfounded) motions to strike, the Commissioner can and should alleviate any confusion by simply assuring all policyholders that they will have a full and fair opportunity to appear and be heard on objections to the Segregated Account and the forthcoming Rehabilitation Plan at the confirmation hearings on a Commissioner's Rehabilitation Plan, which presumably will be set after the Rehabilitation Plan actually is filed and publicly disclosed.

III. CONCLUSION

For the above reasons, Depfa respectfully requests that the Court deny the Commissioner's motion to strike, as it pertains to Depfa, and also in its entirety.

Dated this 8th day of September, 2010.

O'NEIL, CANNON, HOLLMAN, DeJONG & LAING S.C.
Co-Counsel for Depfa Bank, plc



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