STATE OF WISCONSIN CIRCUIT COURT DANE COUNTY

In the Matter of the Rehabilitation of:

Case No. 10 CV 1576 – I

SEGREGATED ACCOUNT OF AMBAC ASSURANCE CORPORATION

WRITTEN OBJECTIONS OF ALL STUDENT LOAN, LLOYDS TSB BANK PLC, FOR HEARING ON CONFIRMATION OF PLAN OF REHABILITATION

In response to this court's Scheduling Order issued October 20, 2010, Access to Loans for Learning Student Loan Corporation ("ALL Student Loan"), in its capacity as an Obligor and policyholder, under Financial Guaranty Insurance Policies ("The Policies") issued by Ambac Assurance Corporation ("Ambac") that have been placed into the Segregated Account, and Lloyds TSB Bank plc ("Lloyds Bank"), in its capacity as bondholder of various bonds issued by ALL Student Loan and purchased by Lloyds Bank and as a beneficiary of such Policies (hereinafter "Movants"), submit the following written objections to the recent Plan of Rehabilitation ("the Plan") filed by the Commissioner of Insurance of the State of Wisconsin ("the Commissioner") as the court-appointed Rehabilitator ("the Rehabilitator") on October 8, 2010. In filing these written objections, Movants do not waive any previous objections or motions they have filed in respect to previous Orders of this Court or actions by the Rehabilitator, Ambac or the Commissioner. Rather, Movants maintain their objections that the actions by the Rehabilitator, Ambac and the Commissioner leading up to March 24, 2010 and since that date have severely and inequitably prejudiced their rights with respect to the three insurance policies placed into the Segregated Account as set forth in their June 22, 2010 Motion to Modify Temporary Injunction and Motion to Intervene (Ct. Rec. Event # 235) ("Motion to Modify"). Movants further object to the continuation of these confirmation

proceedings as scheduled for the reasons set forth in the Petition for Permissive Appeal and Request for Stay of these proceedings now pending in the Wisconsin Court of Appeals, District IV, ("Petition for Permissive Appeal") filed on November 3, 2010.

Pursuant to the Scheduling Order, paragraph 2(a), Movants set forth the following written objections to the Plan.

I. The Plan Should not be Approved Because Movants and Other Parties have not been Afforded the Information and Discovery Necessary to Adequately Prepare for this Hearing

For the reasons set forth in Movants' Motion to Modify and Petition for Permissive Appeal, copies of which have been previously filed with or served on this Court and which Movants incorporate herein by reference, Movants object to the hearing on this motion continuing and any confirmation of the Plan. With respect to the Disclosure Statement, Movants have not been afforded the documentation that forms the basis for the figures set out therein and in the exhibits, including but not limited to: the Base Case and Stress Case Loss Estimates, the various reserves for the Segregated Account and General Account, and the four "scenarios" set out on pages 65-68 and the attached exhibits.

The lack of information shared is especially significant with respect to the lack of response to Movants' requests for information and discovery as set forth in the Affidavit of Lawrence Bensky (Sept. 1, 2010, Ct. Rec. Event # 402) , ¶¶ 1-3 to Movants' Motion to Modify, which Movants incorporate herein by reference. OCI and the Rehabilitator have never explained the full factual basis for the allocation of the ALL policies to the Segregated Account, specifically all of the financial details for their assertion that there is "projected material impairment."

In their rush to judgment in what is by far the largest insurance rehabilitation in the history of Wisconsin, OCI, Ambac and the Rehabilitator want to deny Movants the opportunity for any meaningful review of the Plan by giving the Movants only a few weeks to digest the Plan and the related Disclosure Statement and a week to digest the Plan proponents' papers, which collectively represent hundreds of pages. On the other hand, the Plan proponents have had by their own admission two years to digest the facts and figures in formulating the Plan. OCI, Ambac and the Rehabilitator have provided no basis to Movants for this accelerated schedule, leaving one to conclude that they do not have the confidence that the Plan would survive a measured examination. This is not surprising, considering that the proponents of the Plan are the same parties who either were the architects or the overseers of the policies of Ambac which gave rise to the declared necessity for creating the Segregated Account.

II. The Plan Provides an Unreasonable, Significant Penalty For Filing A Claim

The Plan provides a significant penalty with respect to the ALL Bonds if the policyholder or beneficiary files a Claim. Plan sections 4.04 (g) and (h) provide as follows:

> **(g) Recoveries and Reimbursements on Policy Claims.** Notwithstanding the Proceeding or any provisions of this Plan, including, but not limited to, the satisfaction of Permitted Policy Claims with Surplus Notes in lieu of Cash, AAC shall be entitled to recover the full amount of all recoveries, reimbursements and other payments and to receive any assets it is owed in its capacity as insurer, surety, credit support provider, credit enhancer, credit default swap counterparty or similar capacities, or as assignee or subrogee, under the applicable Policy and any related underlying instrument(s) or contract(s) governing the priority or distribution of cash recoveries or delivery of assets, unless otherwise waived by AAC and the Management Services Provider or the Rehabilitator or approved by AAC and the Management Services Provider or the Rehabilitator.

> **(h) Assignment of Rights.** Without prejudice to (i) the terms and provisions of the applicable Policy and any related underlying instrument(s) or contract(s) and (ii) any assignment previously executed, whether pursuant to a Proof of Policy Claim Form or otherwise, upon receipt of a payment with respect to a Permitted Policy Claim, each such Holder shall be deemed to have assigned its rights relating to payment under the underlying instrument(s) or contract(s) to AAC.

Lloyds has projected the approximate amount owing on the ALL Bonds at maturity in 2013, and determined a projected, approximate financial penalty it would suffer if it files a Claim under the ALL Policy. There is no doubt that the Rehabilitator is fully aware of this financial information and is seeking to place this collateral in the General Account to the detriment of Lloyds and ALL.

Lloyds will present testimony as to the potential prejudice it could suffer as a result of these two Plan provisions based on the projected total amount due and payable on the ALL Bonds at maturity, the total amount of trust collateral that Lloyds has for payment or partial payment on the Bonds and the projected shortfall guaranteed by Ambac. If Ambac were solvent, the policy would require Ambac to pay Lloyds the full amount due on the bonds and Lloyds would assign the bonds and the right to collect the trust collateral to Ambac. However, as presently constituted, if Lloyds files a Claim under the Plan with respect to the ALL Policy, and the claim is allowed in the full amount of the unpaid obligation under the ALL Bonds, the Segregated Account will only pay 25% in cash and Lloyds will be given a contingent, subordinated Surplus Note for the balance. However, this is a note that the Commissioner has stated may never be paid at all, and even in optimum conditions, would not be paid until 2020. In return, under the Plan, the Ambac General Account will then be entitled to seize all of the collateral for the ALL Bonds owned by Lloyds – which collateral is projected to have a readily realizable

value far in excess of the initial cash Lloyds would receive on its claim. This would result not only in Lloyds getting less than 100 cents on the dollar, but it would be subsidizing the policyholders in the General Account, a true perversion of the rehabilitation process.

Ambac is authorized under Plan sections 4.04 (g) and (h) to divert all of Lloyds's trust collateral to pay any other unrelated liabilities of Ambac. Thus, on a cash basis, by filing a Claim under the Plan, Lloyds will lose far more than it would stand to gain in cash and even any projected payment on the Surplus Notes (at present value, especially given the uncertainties associated with the Surplus Notes), and Ambac's General Account will profit immediately by the amount of the collateral which, unlike the Surplus Notes, is readily convertible to cash at or near a par value.

For example, assuming hypothetically that the total outstanding debt on one of Lloyds' policies at maturity will be $200 million, and further assuming that policy will have collateral of $100 million in the form of an indenture trust, if Lloyds files a Claim under the Plan it would result in a $50 million net cash gain to Ambac's General Account. This is because the Segregated Account would pay 25% of Lloyds $200 million claim in cash ($50 million). The Segregated Account would then issue $150 million in surplus notes, the ultimate value of which is entirely speculative. However, the General Account would be enriched by $50 million as a result of Lloyds' $100 million interest in the indentured trust, where it may be used to pay Ambac's unrelated liabilities. This does nothing to strengthen the Segregated Account and it diverts otherwise claims paying resources to the General Account.

It is entirely speculative whether Lloyds will ever see any of the assets from the Surplus Notes in 2020 when the notes are scheduled to mature, and even that date is illusory. Movants object to these onerous and unreasonable provisions in the Plan.

III. The Plan has Disparate Treatment of Similarly Situated Policyholders

Wisconsin law permits allocation of policies to a segregated account based only on certain types of insurance (e.g. mortgage backed securities) that inherently involve more risk than others. Wisconsin law does not permit allocation of policies to a segregated account based on the claims experience, i.e. if there have been claims against the policies. To allow such an after-the-fact allocation method would invite insidious discrimination across all lines of insurances. This should be void as against public policy. It also violates Wis. Stat. § 611.24(2), which requires that a segregated account should not be contrary to "the interests of any class of insureds."[1] It also violates the priorities provisions of Wis. Stat. § 645.68(3)[2], § 645.01(4)(d)[3] and § 601.01(2)[4], which require equitable treatment amongst the same class of creditors, and the Equal Protection clauses of the Wisconsin and United States Constitutions.[5]

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[1] Wis. Stat. § 611.24(2) provides that an "Optional Segregated Account" may only be established "with the approval of the commissioner ... unless he or she finds that the segregated account would be contrary to the law or to the interests of any class of insureds." (Emphasis added.)

[2] Wis. Stat. § 645.68, which the Plan concedes applies, calls for administrative expenses to be paid first and then all policyholders (e.g. the ALL policies and Dunkin Donuts), including third party claims (e.g. Lloyds), to be paid as the next priority. There is no provision in the statute for the inequitable two-tiered system as the Plan requires.

[3] Wis. Stat. § 645.01(4)(d) provides that the purpose of the Insurers Rehabilitation and Liquidation Act is the "equitable apportionment of any avoidable loss."

[4] Wis. Stat. § 601.01(2) provides that the purpose of the insurance statutes is to "ensure that policyholders, claimants and insurers are treated fairly and equitably." (Emphasis added.)

[5] See *In Re Conservation of Alpine Ins. Co.*, 318 Ill. App.3d 457, 741 N.E. 2d 663, 668 (2000) (court rejected rehabilitation plan which sought to discriminate between classes of

Movants contend that it would set significant, adverse precedent for the state of Wisconsin if this Insurance Commissioner is permitted to segregate insurance policies on the basis of prior loss experience as he has done in this instance. If this is permitted in this instance with financial guaranty policies, it would, as a matter of public policy, set a precedent to permit this or a future Commissioner to segregate only those health or life insurance policies that involve cancer or HIV claims into a segregated account, leaving only the policies with no claims or non-cancer/HIV claims in the general account. Or it would allow the Commissioner to segregate only those policies that involve hail or storm damage on homeowner's policies to a segregated account. There is no difference in the treatment of Movants' policies allocated to the Ambac Segregated Account in the present case.

The Rehabilitator and OCI simply chose to place all policies with any claims into the Segregated Account in the present case and leave all policies without adverse claims experience in the General Account. By definition and necessity, this action in the plan creates two classes of claimants from the same creditor priority (§ 645.68(3)) that are being treated in a disparate fashion, with the <u>only</u> factor for that disparate treatment being the existence of loss or claims experience. This is clearly "contrary to the law or to the interests of any class of insureds" which makes it a violation of Wis. Stat. § 611.24(2). It is also a violation of Wis. Stat. § 601.01(2)'s admonition that the purpose of the insurance statutes is to ensure that "policyholders, claimants and insurers are treated

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policyholders based on whether they had additional insurance); *Ferdon ex rel. Petrucelli v. Wisconsin Patients Compensation Fund,* 284 Wis. 2d. 573, 672, 701 N.W.2d 440, 489 (Wis. 2005) (court held cap on malpractice recoveries violated equal protection because it discriminated against only those who suffered damages, exactly as does the Plan at issue).

fairly and equitably." Finally, it violates Wis. Stat. § 645.01(4)(d)'s mandate that the purpose of the Insurers Rehabilitation and Liquidation Act is "equitable apportionment of any avoidable loss." [6]

The Plan purports to adopt the distribution priorities applicable to liquidation proceedings in Wis. Stat. § 645.68, but it ignores those same requirements of parity and equality between creditors in the various classes of creditors. Specifically, the Plan ignores the requirement that all policyholders be treated the same as priority two claimants pursuant to § 645.68(3) and offers as the only basis for this disparate treatment and separate classification of similarly situated policyholders the fact that the subordinated class allocated to the Segregated Account were policyholders who had the temerity to have claims against the policies. Yet this was the reason for their purchasing and Ambac issuance of the policies - - to protect against claims. This is not a rational basis for the disparate treatment within the framework of the statute.

The allocation of the Movants' policies to the Segregated Account further violates Wis. Stat. § 611.24(2) in that (1) the student loan policies were not a "type," "class," "kind," or "branch of insurance business" where the Wisconsin legislature intended that "the fortunes of policyholders in hazardous and secure types of insurance should be separated." *See* Official Commentary of Wis. Stat. § 611.24 Comments at L. 1971, C 260 § 72 (2006). That Commentary provides as follows:

> *Some branches of the insurance business are much riskier than others.* Traditionally, it has been considered desirable for certain kinds of business

[6] Moreover, the experts for ALL and Lloyds contend that it is contrary to custom and practice in the industry to provide for unequal treatment among the same class of creditors. *See* Bingham Affidavit (Sept. 1, 2010, Ct. Rec. Event # 404), ¶¶ 27-19; Barbagallo Affidavit, (Sept. 1, 2010, Ct. Rec. Event # 403), ¶¶ 15-16, submitted in support of Movants' Motion to Modify.

> to be transacted by separate companies, so that adverse experience or failure in the more hazardous venture would not endanger the policyholders in the more stable types of business . . . . [I]nsurers have, for a variety of reasons, often found it desirable to establish separate corporations for certain divisions of their business, even within a single line. High risk automobile business is an illustration. . . . [I]t is not yet possible to abandon completely the notion that *the fortunes of policyholders in hazardous and secure types of insurance should be separated.*

(Emphasis added.)

The Official Commentary to the enabling legislation for segregated accounts makes it clear that the Mandatory Segregated Accounts under § 611.24(1) and Optional Segregated Accounts under § 611.24(2) are reserved for situations where the Commissioner deems it necessary to separate or segregate "hazardous" "types" or "classes" of insurance business from "secure" insurance business. As noted earlier, there is absolutely no authority to segregate policies of insurance simply because there have been claims made against the policies, or where there is no evidence that student loan policies are "hazardous" as to their "type," "branch," or "class." In fact, unlike other policies which have been allocated to the Segregated Account where the assets being insured by Ambac were not performing, the only factor hazardous to the ALL policies was the presence of Ambac, i.e. the credit rating of Ambac caused the market to lose faith in the bonds which it insured. This is not a rational basis for allocating the ALL policies to the Segregated Account, given that there are other similarly situated policies where the underlying assets are performing and they have not been so allocated, e.g. the policies of Dunkin Donuts, Hertz and Sonic, which remain in the General Account solely because they allegedly do not have material claims at present.

Included in this objection is the treatment and classification of the Surplus Notes that are to be paid as part of the Distributions on Permitted Claims because it is clear that the Surplus Notes are wholly subordinated to all other claims of the General Account and other claims and that payment by or before the alleged maturity date of 2020 is illusory because of the Commissioner's discretion. (*See* pages 38-42 of the Disclosure Statement.) Moreover, because of the publically available financial records, it is evident that these notes are unlikely to be paid until long after the 2020 date, which is why the Plan calls for absolute discretion for the Rehabilitator to extend that 2020 date.

For all of these reasons, the Rehabilitator's reliance on *Carpenter v. Pacific Mutual Life Ins. Co. of Cal.*, 10 Cal. 2d 307 (1937), *aff'd sub nom Neblett v. Carpenter*, 305 U.S. 297 (1938) (rehabilitation plan that treated life insurance policies more liberally than non-cancellable accident and health policies, but that gave equal and non-discriminatory treatment to all claims within each class, did not violate equal protection) is misplaced. The relevant statutes cited above in Wisconsin are different. The public policy in the insurance industry has changed since *Carpenter* as set out in Movants' Affidavits. Further, the facts of the two cases are wholly distinguishable. In fact, the California courts later rejected a rehabilitation plan that attempted to do what this Plan seeks to do. *See Commercial Nat'l Bank v. Superior Court of Los Angeles County*, 14 Cal. App. 4th 393, 414 (Ct. App. 1993)(court rejected a proposed rehabilitation plan that utilized a "dual valuation" system in which municipal guaranteed investment contracts were valued at different rates.)

IV. The Plan is Unreasonable Because the Segregated Account Was Created Without "Adequate Capital and Surplus As Required By § 611.24(2)(a)

The Segregated Account was created without "adequate capital and surplus as required by § 611.24(2)(a), as the policies allocated to that account had effectively all of the liabilities of Ambac and very restricted access to its assets. The Rehabilitator's argument that a new Segregated Account can be initiated after the class of policies have been identified as hazardous only because those policies are the ones with "material impairment," and then segregate only those policies while still maintaining "adequate capital and surplus" misinterprets § 611.24(2). It is wholly inconsistent with the legislative intent behind § 611.24(2).

The legislative history behind Wis. Stat. § 611.24(3) fully supports Movants' interpretation of the legislative intent. The "Note" in the Code pertinent to this section provides as follows:

> The basic idea behind segregated accounts is that different operations can be kept independent without formally creating a separate corporation. A segregated account is in some respects like a "corporation within a corporation." Its legal nature and treatment is prescribed in sub. (3). Sub. (3) (a) **requires that a segregated account be equipped with an adequate share of the corporation's capital and surplus.** This is indispensable if the account is to be expected to function and survive like a separate corporation. **If it carries no risks not assumed by the corporation's general account, the commissioner may set the required figure at zero under s. 611.19 (I).** There *is* no reason why a corporation which could create a subsidiary under s. 611 .26 (2) for any portion of its insurance business should not be permitted to achieve the desired separation by establishing a segregated account. **provided it is adequately capitalized to make it independently viable.** and the commissioner approves its creation.

(Emphasis added.)

It is clear from this legislative "Note" that the legislature expected that it was "indispensable" that the newly created Segregated Account was "expected to function and survive like a separate corporation" but "provided it is adequately capitalized to make it independently viable." There is no question here that the Segregated Account into which the ALL policies have been placed do not comply with either the legislative intent or the plain and ordinary meaning of the terms of Wis. Stat. § 611.24(3).

In light of this legislative intent that the Segregated Account be adequately capitalized and that it have surplus, that it not create two classes of policyholders, and that it provide for fair and equitable treatment of the policyholders, the Rehabilitator has insufficient <u>evidence</u> in support of his contention that the Segregated Account has accomplished these statutory mandates. There is no reasonably acceptable, credible evidence that this Segregated Account, which has virtually all of the crystallized liabilities of Ambac, can maintain such "adequate capital and surplus," especially when the assets pledged against the liabilities associated with the policies in the Segregated Account are illusory.

The assets are illusory for several reasons. First, 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. 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.

The alleged backup support for the $2 billion Note is the Aggregate Excess of Loss Reinsurance Agreement ("Reinsurance Agreement"). "Reinsurance is a contractual arrangement whereby one insurer (the ceding insurer) transfers all or a portion of the risk it underwrites pursuant to a policy or group of policies to another insurer (the reinsurer)." Barry R. Ostrager & Thomas R. Newman, *Handbook on Ins. Coverage Disputes* § 15.01[a] (12th ed. 2004) (citing *Colonial Am. Life Ins. Co. v. Commissioner*, 491 U.S. 244, 109 S.Ct. 2408, 105 L.Ed.2d 199 (1989)). *See also National Union Fire Ins. Co. v. American-Re Ins. Co.*, 441 F.Supp.2d 646, 650-652 (S.D.N.Y. 2006). In this case, the Rehabilitator is asserting that it is protecting the Segregated Account with 98% of the assets of Ambac by means of the Secured Note and Reinsurance Agreement (attaching above the Secured Note). Thus, the Reinsurance Agreement, which is issued by the same company that issued the underlying insurance policies it is now purporting to reinsure, should be airtight, with no conditions, i.e. as solid as the insurance policy that it replaces.

In fact, § 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-insurer, 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 the Plan itself provides that it may be modified by the Rehabilitator and the Court at any time. The "follow the fortunes" clause is a very significant protection 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." *See* Barbagallo Affidavit, ¶¶ 12-15; Bingham Affidavit, ¶¶ 23-25 to Movants' Motion to Modify.

In any reinsurance agreement where the cedent is seeking protection, there must also be a "follow the settlements" clause. The "follow the settlements" provision has been interpreted in the same manner as the "follow the fortunes" clause, *i.e.* the reinsurer cannot second-guess the cedent's claims handling. *See, e.g., North River Ins. Co. v. ACE American Reins. Co.*, 361 F.3d 134, 139 (2d Cir. 2004); *Travelers Cas. & Sur. Co. v. Gerling Global Reins. Corp. of America*, 419 F.3d 181, 193 (2d Cir. 2005). A typical such provision provides: "All claims involving this reinsurance, when settled by the Company, shall be binding on the Reinsurer, who shall be bound to pay its proportion of such settlements...." *See* Stuehrk Affidavit (Sept. 1, 2010, Ct. Rec. Event # 405), ¶ 12. There is no such clause in the Reinsurance Agreement here. Rather, it has a clause that provides for somewhat the opposite, i.e. for the reinsurer *not* to be bound in certain instances. The Affidavit of Andrew Stuehrk filed with Movants' Motion to Modify summarizes the effect of this clause:

> The Reinsurance Agreement, § 1.02 has a "finite aggregate reinsurance" section that 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 cover 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.

Stuehrk Affidavit, ¶ 13; Barbagallo Affidavit, ¶¶ 12-15 to Movants' Motion to Modify.

In short, the Rehabilitator's statements in the Plan that the Secured Note and Reinsurance Agreement provide the Segregated Account with "access to all [except 2%] of the assets of Ambac, in pari passu with General account policyholders" are without merit, as they are based on the proverbial "house of cards," i.e. conditions in agreements that, if the policyholders are truly able to have access to the assets of the General Account as promised by the Rehabilitator, cannot be conditional. If the Rehabilitator does not comply with the conditions in the Secured Note and Reinsurance Agreement, and the Surplus Notes are not paid on time and are subordinated, or if there is less than $100 million in surplus in the General Account, the promise of the Segregated Account being protected by "all of the assets of Ambac" is hollow.

The Commissioner exceeded his authority in creating the Segregated Account, and the actions he took beyond his authority are a nullity. *See, e.g., Wis. Compensation Rating & Inspection Bureau v. Mortensen,* 227 Wis. 335, 277 N.W. 679, 86 (1938) (insurance commissioner's actions in violation of statute were void because he "acted without and in excess of his powers.")

V. The Release Provisions of Section 8.01 of the Plan are Unreasonable

Movants object to the "Discharge, Release and Injunction" provisions in Section 8.01 of the Plan in that it requires, in exchange for Distributions on a Permitted Claim, a "full and complete release, discharge and termination..." upon the Segregated Account and AAC with respect to such [Permitted] Claim." It also provides that "all Holders of Claims are precluded from asserting against the Segregated Account, the General Account or AAC, or their respective successors or property or any of their respective or current or former members, shareholders, affiliates, officers, directors, employees or agents, any Claims, obligations, rights, causes of action or liabilities, based upon any act, omission, transaction, or other activity of any kind or nature, other than as expressly provided for in this Plan."

First, there is no basis for requiring a complete release of the Segregated Account and AAC simply because of "the Distributions," as defined in Section 1.20, unless it is interpreted as the full and final payment of <u>all</u> Distributions, including payments under the Surplus Notes, i.e. the simple issuance of a Surplus Note should not be sufficient to effect a release. Until the Surplus Note is paid in full, there should be no release. No creditor should be forced to release all rights under a policy without full payment under that policy, especially where there is only a "mere expectation" of payments beyond the initial 25% cash distribution.

Second, the "preclusion" language effectively vitiates any rights Movants (and other creditors with challenges to this Plan) may have against any and all aspects of the Plan. There is no basis to ask Movants and others to prematurely be precluded from bringing <u>any</u> action whatsoever against any actions of the OCI or Ambac, no matter how egregious, as soon as the Plan is confirmed. This is outrageous and wholly unreasonable,

as it is not even contingent on the filing of a claim or the determination that the claim is a Permitted Claim. There is no reason that all creditors should be precluded from challenges of all kinds without any consideration or resort to the courts.

VI. The Provisions of Articles 3 and 4 of the Plan that Provide Almost Unfettered Discretion in the Administration of the Plan to Ambac are Unreasonable, Arbitrary, and Capricious

Movants further object to Articles 3 and 4 of the Plan insofar as they provide virtually unfettered discretion in the administration of the Plan to Ambac, the Management Service Provider ("MSP"), "in any matter it [Ambac] so chooses." (§ 3.04 and § 3.05). In fact, ¶ 4.01 of the Plan provides Ambac with full responsibility "for administering, disputing, objecting to, compromising or otherwise resolving all claims in accordance with this Plan." Although it makes this "subject" to "any guidelines issued by the Rehabilitator," the Plan has no such "guidelines" and it would appear, based on the preclusion language discussed above, that no one would have a right to challenge these guidelines. Moreover, § 4.04(b) provides that Ambac as MSP "shall evaluate each Pending Policy Claim to determine whether the amount set forth in the Proof of Policy Claim is a Permitted Claim or whether an Objection should be raised as to such Policy Claim in accordance with § 4.06," without any supervision from anyone.

It is completely unreasonable, arbitrary, and capricious for the Plan to literally "let the inmates run the asylum," as this Plan permits Ambac, as MSP, to do. Ambac's management is the reason why there was the financial debacle that initiated these proceedings. To allow that same or similar management to now administer the Segregated Account without any significant oversight is without any reasonable basis. If the response is that the Rehabilitator and OCI would have oversight, this offers little

comfort because just as it was the Ambac's management which was the architect of its demise, so it was the OCI which was overseeing it during this process.

Movants further object to the uncertainty in the Management Services Agreement under § 1.34 of the Plan and concomitant lack of control by the OCI and Rehabilitator over Ambac as MSP in that agreement.

VII. The Plan's Definition of "Late Claim" is Unclear

The definition of "late claim" under Section 1.32 is unclear and uncertain, yet it is extremely important to Movants as a potential claimant. Specifically, the reference in Section 1.32(ii) to "the earliest date on which such Claim, if it had been submitted, would have satisfied all of the requirements to be considered a Permitted Claim" as the second of the two "later of" options within the 120-day period (the first being after the "Effective Date") is unclear and uncertain. Movants and many other claimants have what are often referred to as "long tail' claims that may not mature until a later date and it is unclear whether this "late claim" date is a "bar date" as in many rehabilitations and liquidations and, if so, does it afford long tail claimants the right to wait until their claims are mature or "ripe" before that claim is deemed late or barred.

In other words, is the second of the two - "later of" options - within the 120-day period, where the claim is not due until 120 days of "the earliest date on which such Claim, if it had been submitted, would have satisfied all of the requirements to be considered a Permitted Claim," mean that the claimant may wait until the claim has matured and is no longer contingent before that claim is barred or deemed late-filed? If so, Movants have no objection; if not, Movants object to this late claim provision as unfair and inequitable to long tail claimants.

VIII. The Plan's Definition of "Mature, Non-Contingent Claim" is Unclear

Section 1.42 of the Plan provides as follows with respect to the definition of a Permitted Claim:

> **Permitted / Permitted Claim.**
> A Claim (other than a Late Claim, a Disputed Claim, a Pending Claim, a Duplicate Claim or a Disallowed Claim) submitted by a Holder in compliance with the provisions hereof and determined by the Rehabilitator or the Management Services Provider to be a matured, non-contingent due and payable obligation according to the provisions of the applicable Policy and/or any other underlying instrument(s) or contract(s) giving rise to or governing such Claim.

(Emphasis added.)

Again, because Movants and many other claimants are "long tail' claimants, it is essential that the Plan be very specific as to exactly what the Rehabilitator means by the term "mature and non-contingent due and payable obligation" for the purposes of filing multi-million dollar claims so as to avoid any error in the filing of such.

IX. The Plan's Termination Provision is Unclear

The Plan does not properly define or explain what the language " if rehabilitation has been accomplished" within the provision in § 10.05 for "Termination of Rehabilitation" means. The full provision provides:

> **10.05 Termination of Rehabilitation.** The Rehabilitator may at any time petition the Court for an order terminating the rehabilitation of the Segregated Account if rehabilitation has been accomplished and the grounds for rehabilitation no longer exist.

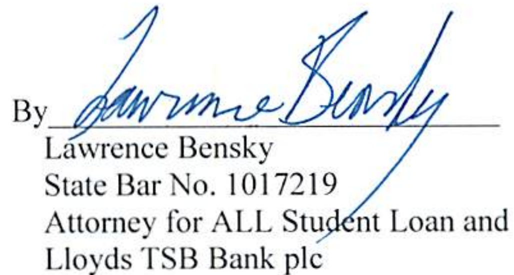
There should be some further definition from the outset as to what the Rehabilitator is considering to be its goal as to what an "accomplished rehabilitation" means so that there is an "end game." Otherwise, this is an invitation to permit Ambac, as the MSP, to earn

huge administration fees and drag this Rehabilitation process on with no incentive to close.

X. Conclusion

For all of these reasons, Movants object to the Plan and ask that the hearing be postponed or, if not postponed, that the Plan be rejected.

November 8, 2010.



By________________________

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