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

RMBS POLICYHOLDERS' OPPOSITION TO THE REHABILITATOR'S MOTION FOR RELAXED ADMISSIBILITY STANDARDS AND MOTION IN LIMINE TO EXCLUDE FOUNDATIONLESS HEARSAY EVIDENCE

The Rehabilitator has made two requests in connection with the standards of evidence to be applied in the hearing on the Rehabilitator's motion to confirm the Plan of Rehabilitation ("Plan"). First, the Rehabilitator requests that the rules of evidence not apply and that evidence be permitted subject to an undefined, yet relaxed, standard of evidence. Second, as an example of this, the Rehabilitator requests that the disclosure statement and the financial projections submitted by the Rehabilitator simply be admitted.

Aurelius Capital Management, LP, Fir Tree, Inc., King Street Capital, L.P., King Street Capital Master Fund, Ltd., Monarch Alternative Capital LP, and Stonehill Capital Management LLC (collectively, the "RMBS Policyholders"), in their capacity as owners of or managers of funds that own residential mortgage-backed securities, oppose both requests. The RMBS Policyholders request the Court apply the Rules of Evidence to this judicial – not administrative – proceeding. In addition, they move *in limine* to exclude OCI's Disclosure Statement Accompanying Plan of Rehabilitation, including written amendments, supplements, and Written Responses to Written Questions, unless the Rehabilitator establishes the evidentiary basis for the admissibility of each document.

Background

On October 8, 2010, OCI filed its Disclosure Statement Accompanying the Plan of Rehabilitation. The disclosure statement began with two full pages of disclaimers, expressly disclaiming reliance upon the document. It stated that "[t]his Disclosure Statement may not be relied upon for any purpose other than to obtain information about the Plan and the Proceeding generally. Nothing contained herein will constitute an admission of any fact or of any liability by any party with regard to any claim or litigation, including, but not limited to, any proceeding involving the Rehabilitator, the Segregated Account or any other party, or any proceeding with respect to any legal effect of the rehabilitation of the Segregated Account or the transactions contemplated by the Plan and this Disclosure Statement." (Disc. St., at ii.)

The OCI refused to stand behind any of the statements it made in the disclosure statement. It recited that "[n]one of AAC, the General Account, the Segregated Account or the Rehabilitator makes any warranty, express or implied, as to the accuracy or completeness of the information contained herein. In particular, events and forces beyond the control of the Rehabilitator may alter the assumptions upon which the disclosures in this Disclosure Statement are based." (*Id.*) It also disclaimed the accuracy of its predictive statements, conceding that "[a]lthough the Rehabilitator believes that any such forward-looking statements are reasonable, no assurance can be given that such expectations will prove to have been correct. Any such forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause the actual results, performance or achievements of the Segregated Account to be different from any future results, performance and achievements expressed or implied by these statements." (*Id.*)

Upon receiving the Disclosure Statement and the Plan of Rehabilitation, all interested parties in the proceeding requested time to analyze the plan and a limited opportunity to obtain discovery into the Plan and the related materials. (*See* Statement of Certain Policyholders (Oct. 14, 2010).) OCI opposed both requests, and this Court agreed with OCI. (*See* Scheduling Order (Oct. 20, 2010).) Thus, the parties in this proceeding have received only the documents that the OCI has chosen to release, and have had no meaningful opportunity to discover the bases of those materials, or to examine OCI about information that may be inconsistent with the views the OCI has expressed.

OCI has continued to release only the information it wishes to release. Most recently, on November 12, 2010, on the very eve of the hearing in the Plan, OCI added, among other items, a Liquidation Analysis and written responses to written questions proposed by the objectors. On Saturday, November 13, 2010, OCI proposed that the parties stipulate that OCI's Disclosure Statement and any written responses shall be deemed admitted in evidence. (Stip., at 2.)

Argument

1. **The Court Should Deny OCI's Request to Relax The Rules of Evidence.**

On the afternoon of Friday November 12—immediately in advance of the hearing on the Rehabilitation Plan that is scheduled to begin on Monday November 15—OCI filed its Brief Re Evidentiary Standards In These Proceedings ("OCI Br."). Perhaps recognizing that it cannot submit proper evidence in support of its Plan, OCI asked this Court to "allow a less-than-strict application of the Rules of Evidence in these rehabilitation proceedings." (OCI Br., at 1.) OCI's request has no basis in the law, and this Court should reject OCI's attempt to undermine the fairness of this proceeding by permitting it to present and rely on inadmissible materials.

This Court lacks the authority to ignore the Rules of Evidence in this proceeding. The Rules of Evidence are broadly applicable, and "govern proceedings in the courts of the state of Wisconsin except as provided in ss. 911.01 and 972.11." Wis. Stat. § 901.01. The term "proceedings" is broadly defined to include "actions" (which include all civil and criminal matters) and "special proceedings." Wis. Stat. § 801.01; Judicial Council Comm. Note to Wis. Stat. § 911.01(2) ("Actions are of two kinds: civil and criminal. . ."). OCI cites to no authority suggesting that the present proceeding is neither an "action" nor a "special proceeding." Consequently, pursuant to Wis. Stat. § 901.01, the Rules of Evidence apply unless specifically excepted by Wis. Stat. §§ 911.01 or 972.11.

Neither Wis. Stat. § 911.01 nor § 972.11 exempt proceedings regarding a Rehabilitation Plan from the Rules of Evidence. To be sure, when the legislature sought to exempt certain proceedings from the Rules of Evidence, it has done so by statute. In Wis. Stat. § 911.01(4), for example, the legislature specifically identified a number of proceedings in which the Rules of Evidence are inapplicable—rehabilitation proceedings are not among them. *See* Wis. Stat. § 911.01(4); *see also* Wis. Stat. § 799.209(2) (exempting small claims proceedings); Wis. Stat. § 227.45(1) (exempting proceedings before an administrative agency or hearing examiner). The legislature knows how to exempt proceedings from the Rules of Evidence; its decision not to exempt rehabilitation proceedings from the Rules of Evidence must be respected.

OCI's citation of cases that describe the standards of evidence in administrative proceedings is irrelevant. (*See* OCI Br., at 2.) Those cases relied on the legislative exemption to the Rules of Evidence for proceedings before an administrative agency, *i.e.*, Wis. Stat. § 227.45(1). OCI does not contend that Wis. Stat. § 227.45(1) directly applies to exempt this proceeding from the Rules of Evidence, nor could it—this court is not an administrative agency.

Moreover, OCI's reliance on Wis. Stat. § 901.04(1) as a basis for a court to ignore the Rules of Evidence is not supported by the language of that statute. That statute provides that a court is not bound by the Rules of Evidence when addressing certain "preliminary" questions concerning admissibility—not "general" questions as OCI claims in its brief. *Compare* Wis. Stat. § 901.04(1) *with* OCI Br., at 2. These "preliminary" questions relate to the qualification of witnesses and the existence of a privilege; in no sense does Wis. Stat. § 901.04(1) permit a court to disregard the Rules of Evidence on matters that are directly relevant to the proceedings at issue.

Finding no statutory basis for its position, OCI misstates case law to try to fit its circumstances. Citing *Layton School of Art & Design v. WERC*, 82 Wis. 2d 324, 367, 262 N.W.2d 218 (1978), OCI claims that Wisconsin courts have held formal procedural rules are inappropriate in less formal "administrative type" proceedings, suggesting that a court can eschew the Rules of Evidence in an "administrative type" proceeding that takes place in a Wisconsin Court. (OCI Br. at 2.) That case holds no such thing. Instead, *Layton* involved the Supreme Court of Wisconsin's review of proceedings that took place before an administrative agency. The court's comments, quoted by OCI, did not purport to excuse ***courts*** from applying judicial procedural rules; rather, the court's comments reflected the fact that proceedings before administrative agencies need not include the same due process protections that must be afforded in a court proceeding. *Layton*, 262 N.W.2d at 229-39.

Similarly, OCI's argument that the "broad discretion regarding the admission of evidence" somehow permits a court to ignore the Rules of Evidence is groundless. Even the case that OCI relies on, *Estate of Hegarty v. Beauchaine*, 2006 WI App 248, 727 N.W.2d 857, recognizes that the court's discretion regarding the admission of evidence does not extend to

simply ignoring the Rules of Evidence. Rather, the discretion a court can exercise regarding the admission of evidence necessarily requires the court to apply the Rules of Evidence. *Id.* at ¶ 151 ("An appellate court will uphold an evidentiary ruling if it concludes that the [trial] court examined the relevant facts, ***applied a proper standard of law***, used a demonstrated rational process, and reached a conclusion that a reasonable judge could reach.") (emphasis supplied; citation omitted).

2. The Court Should Not Admit The Disclosure Statement and Related Documents Unless OCI Complies With The Requirements of the Rules of Evidence.

As shown above, the Rules of Evidence apply with full force to this proceeding. OCI makes no effort to satisfy the requirements of those rules in seeking the admission of the Disclosure Statement, and related materials. At this point, the OCI cannot satisfy the requirements of the Rules of Evidence. The Disclosure Statement and related materials are inadmissible on three independent grounds: (a) these documents are inadmissible hearsay; (b) OCI has not established a proper foundation for these documents; and (c) OCI did not provide the RMBS Policyholders' with sufficient notice of these documents.

First, the OCI seeks to admit the Disclosure Statement and related materials for their truth. The OCI intends to use the documents to carry its burden that the Plan should be confirmed. OCI intends to rely on the financial projections and other materials in the documents for their truth. As out of court declarations of unknown witnesses, the materials are plainly hearsay. Wis. Stat. § 908.01(3). We are aware of no exception to the hearsay rule that would permit OCI to introduce these documents.

Second, OCI has failed to establish an evidentiary foundation for the Disclosure Statements. To date, OCI has not produced any of the supporting documents underlying the Disclosure Statement. Instead, OCI has essentially told the RMBS Policyholders to trust him

with their money, totaling in excess of $1 billion in Ambac policies. OCI has provided the parties with no basis to verify the accuracy of OCI's statements or calculations. OCI has not even identified the author of the Disclosure Statement, and we are aware of no witness that will admit to having authored the document such that the witness can be cross-examined about the contents of the document. It would be unfair to permit OCI to use this material as evidence because the RMBS Policyholders have had no opportunity to evaluate the documents underlying the Disclosure Statement. Foundation is especially important here as OCI expressly disclaims the "accuracy or completeness" of the Disclosure Statement. (Disc. St., at ii.) The Disclaimer provides that: "The terms of the Plan will govern in case of any inconsistency between the Plan and this Disclosure Statement," (Disc. St., at i); "Nothing contained herein will constitute an admission of any fact or of any liability by any party with regard to any claim," (*id.* at ii); "None of AAC, the General Account, the Segregated Account or the Rehabilitator makes any warranty, express or implied, as to the accuracy or completeness of the information contained herein." (*Id.*)

Third, the RMBS Policyholders object to OCI's use of the supplements to the Disclosure Statement as evidence because OCI did not provide the RMBS Policyholders with adequate notice. OCI's eleventh hour filing of the supplements and amendments to the Disclosure Statement, including the Liquidation Analysis and the Written Responses to the Written Questions, constitute unfair surprise and should be excluded or the hearings postponed to the give the parties adequate time to prepare. The RMBS Policyholders would be unfairly prejudiced by the admission of these documents produced on the eve of the hearing. The Liquidation Analysis that is included as part of the November 12, 2010 filing is a complex financial computation. OCI does not provide who performed the calculations, who prepared the

documents, and on what information they relied. The late introduction of this evidence does not afford the RMBS Policyholders the opportunity to properly evaluate the evidence sufficiently to verify it. This information should have been produced at least with the Plan on October 8, 2010, if not earlier, especially because the liquidation value is the constitutional minimum that policyholders must receive under a rehabilitation plan. *Neblett v. Carpenter*, 305 U.S. 297, 304-05 (1938).

Even if this Court agrees with OCI that this is an appropriate case in which to relax the Rules of Evidence, it should still reject OCI's attempt to admit the Disclosure Statement and related materials without establishing the evidentiary basis for the documents. The very language of the documents undermines their reliability – OCI disclaimed any party's reliance on the documents. Moreover, OCI has refused to disclose information that would bear on the reliability of the documents. In its past filings, OCI has argued that it has "a statutory privilege that prevents discovery directed at its regulatory decision-making" and that it may refuse to disclose reports produced or created "in the course of an inquiry of a regulated insurer." (OCI's Br. in Opp. (May 20, 2010), at 2, 14.) Having refused to provide discovery by claiming privilege, OCI cannot now selectively disclose information and use it as evidence in the hearing.

Conclusion

For the reasons set forth herein, the RMBS Policyholders respectfully request that the Court deny OCI's motion for relaxed evidentiary standards and refuse to admit OCI's Disclosure Statement, including written amendments, supplements, and Written Responses to Written Questions, unless OCI establishes the evidentiary basis for their admission.

Dated this 15th day of November, 2010.

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