STATE OF WISCONSIN   COURT OF APPEALS   DIST. IV

In the Matter of the Rehabilitation of:

SEGREGATED ACCOUNT OF
AMBAC ASSURANCE CORPORATION

Appeal of the United States of America:
Appeal No. 2011AP516

UNITED STATES' MOTION FOR RECONSIDERATION OF THE COURT'S MARCH 16, 2011 ORDER CONSOLIDATING THE UNITED STATES' APPEAL (No. 2011AP516) WITH THE OTHER APPEALS FILED IN THIS PROCEEDING

The United States, the appellant in the above-captioned appeal, through its counsel Richard Humphrey and Anthony T. Sheehan, moves for reconsideration of the Court's March 16, 2011 Order consolidating the United States' appeal with the other appeals filed in this proceeding. The consolidation would result in the duplication of judicial effort by the United States Court of Appeals for the Seventh Circuit and by this Court, without any significant efficiency benefits for this Court.

1. On March 15, 2011, the Wisconsin insurance commissioner moved to consolidate all of the appeals in the

rehabilitation of the segregated account of Ambac Assurance Corporation (Ambac). On March 16, 2011, the Court granted that motion. The United States is seeking reconsideration under § 809.14(2) of the Wisconsin Rules of Appellate Procedure.

2. As the United States stated in its notice of appeal and in its docketing statement, and as acknowledged in the motion to consolidate (Mot. at 8 n.5), the United States is the appellant in two pending appeals in the Seventh Circuit arising out of the Ambac rehabilitation. Those appeals are *Nickel v. United States* (7th Cir. – No. 11-1158) and *United States v. Wisconsin State Circuit Court for Dane County; et al.* (7th Cir. – No. 11-1419).

3. The United States also has consistently asserted: (1) that it does not admit that the Wisconsin state courts have properly asserted jurisdiction over the United States; (2) that the federal courts, not Wisconsin state courts, properly have jurisdiction over the issues raised by the United States; and (3) that it was appealing to this Court only to preserve its Wisconsin appellate rights should the Seventh Circuit hold that

the United States had to pursue its rights in the Wisconsin courts. The United States further stated its intention to file a motion to hold this appeal in abeyance pending the outcome of the Seventh Circuit appeals. That motion is submitted along with this opposition.

4. The parent company of Ambac received tentative federal income tax refunds of approximately $700 million pursuant to the special procedure in 26 U.S.C. § 6411.* Ambac's parent, in turn, transferred the $700 million to Ambac, relying on a tax sharing agreement. Ambac and its parent are members of a consolidated group for federal income tax purposes. All members of a

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* Section 6411 of the Internal Revenue Code provides a special procedure under which a taxpayer with a net operating loss can circumvent the audit procedures that are usually applied when a taxpayer files a claim for refund. The special procedure allows a taxpayer to make an "application for a tentative carryback adjustment" (26 U.S.C. § 6411(a)) which is subject only to "limited examination" to discover errors of computation or omissions (26 U.S.C. § 6411(b)). The IRS is required to act on the application within 90 days. *Ibid.* It is only after the expedited refund is paid that the IRS makes a full examination of the relevant return under its regular auditing procedures. M. Saltzman, *IRS Practice and Procedure*, ¶ 11.03 (Rev. 2d ed. 2005).

consolidated group are severally liable for the federal tax liabilities of the group, notwithstanding any private arrangement among the group members to allocate the tax liability. Treas. Reg. (26 C.F.R.) §§ 1.1502-6; 1.1502-78(b)(2).

On November 8, 2010, the last day for objections to the plan of rehabilitation, the insurance commissioner filed a "Notice" in the Dane County Circuit Court of a purported allocation of only Ambac's potential liability for the $700 million to the segregated account being rehabilitated, leaving the money itself in Ambac to be used for the payments to other creditors. (Order of Oct. 18, 2010 at 2; Notice of Nov. 8, 2010; Affidavit dated Nov. 7, 2010 at 1–3.) The court immediately imposed an *ex parte* injunction that expressly enjoined the "United States Internal Revenue Service, and all other federal . . . entities" from taking steps with respect to the "allocated" tax liabilities, thereby raising issues involving the sovereign immunity of the United States. (Order of Nov. 8, 2010 at 2–3.) The filing of a notice of the tax "allocation" in court on November 8 did not inform the United States of the purported

tax allocation in time for it to make an objection to the plan of rehabilitation before the November 8 deadline for filing such objections had expired.

5. In its docketing statement in its appeal to this Court, and in light of the above-summarized facts, the United States noted five potential issues:

- Whether the injunctions issued by the Dane County Circuit Court violated the sovereign immunity of the United States, which cannot be waived except by a statute enacted by Congress.
- Whether certain injunctions are barred by the federal Tax Anti-Injunction Act, 26 U.S.C. § 7421(a), which states that "no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed."
- Whether the circuit court exceeded its jurisdiction when it asserted exclusive state court jurisdiction over a potential

federal tax liability of Ambac not yet asserted by the IRS and where Ambac itself is not in rehabilitation or receivership. *See* 26 U.S.C. § 6871.

- Whether the circuit court erred in concluding that "[t]he rest of the disputed tax allocations, which total approximately $700 million, are subject to the jurisdiction of this Court and the priority structure adopted by the Plan due to the timely, pre-bankruptcy allocation of those disputed liabilities by the Rehabilitator and OCI to the Segregated Account." (Final Order of Jan. 24, 2011 at 30.)
- Whether the circuit court otherwise erred in confirming the rehabiliation plan as it relates to the United States and its agencies.

6. The issues listed above are unique to the United States. The first four issues involve the sovereignty and sovereign immunity of the United States, and the interpretation of the McCarran-Ferguson Act (15 U.S.C. § 1011–1015) as it relates to the Internal Revenue Code (26 U.S.C.) and the Treasury

Regulations governing the tax liability of consolidated groups. As far as we can determine, no other creditor will be able to present such issues. The last issue includes Ambac's and the insurance commissioner's violation of the United States' right to due process by the manner in which they purported to allocate Ambac's potential tax liability to the segregated account at the very end of the objection period. Again, we are not aware of any other creditor that was so mistreated. The issues to be raised by the United States cannot be subsumed in a general discussion of issues common to the other creditors. The United States' issues should be separately decided. Thus, consolidating the United States' appeal with the other appeals will not result in any judicial efficiencies for this Court.

7. There is, moreover, considerable overlap between the issues that the United States is raising in the Seventh Circuit and the issues that it raised in its notice of appeal and its docketing statement in the instant appeal. At a minimum, the Seventh Circuit will need to rule on the interaction between the

McCarran-Ferguson Act and the federal statutes granting the United States district courts original and removal jurisdiction. *See* 26 U.S.C. § 7402(a); 28 U.S.C. §§ 1331, 1340, 1345, 1442. That ruling should resolve the United States' objections to litigating in the Wisconsin courts, thereby sparing this Court from having to consider this appeal with those objections pending. The Seventh Circuit appeals also involve the above-listed issues concerning sovereign immunity, the McCarran-Ferguson Act, and the Internal Revenue Code as they pertain to the allocation of the tax liability to the segregated account and the imposition of an injunction against the United States. Consolidating the United States' appeal with the remaining appeals would result in both this Court and the Seventh Circuit considering the same issues simultaneously — a wasteful duplication of judicial effort. Retaining the United States' appeal as a separate appeal (and holding it in abeyance) would both eliminate that duplication and could reduce the number and complexity of the issues that this Court might ultimately need to decide.

8. Retaining the United States' appeal as a separate appeal (and holding it in abeyance) will not prejudice any of the other creditor-appellants, whose appeals will go forward in this Court. There is also little chance of this Court will issue conflicting rulings, inasmuch as the Court will be able to consider its prior opinions in later deciding an appeal of the United States.

9. In its March 16, 2011 Order, the Court also ordered the parties to advise it of any arrangements for joint briefing or of any special requests regarding the briefing schedule. The United States will file a separate brief. The United States has also filed today a separate motion asking that the Court hold in abeyance the briefing of the United States appeal.

For the foregoing reasons, we oppose the consolidation of the appeal of the United States (No. 2011AP561) with the appeals of the other creditors.

Respectfully submitted,

/s/ Richard D. Humphrey

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Dated this 21st day of March, 2011.

March 22, 2011

STATE OF WISCONSIN   COURT OF APPEALS   DIST. IV

In the Matter of the Rehabilitation of:

SEGREGATED ACCOUNT OF
AMBAC ASSURANCE CORPORATION

Appeal of the United States of America:
Appeal No. 2011AP516

DECLARATION

Anthony T. Sheehan, of the Department of Justice, Washington, D.C., states as follows:

1. I am an attorney employed in the Appellate Section, Tax Division, United States Department of Justice.

2. The facts recited in the foregoing motion are true and correct to the best of my knowledge and belief.

I declare under penalty of perjury, pursuant to 28 U.S.C. § 1746, that the foregoing is true and correct. Executed this 22d day of March, 2011, in Washington, D.C.

/s/ Anthony T. Sheehan

ANTHONY T. SHEEHAN
Attorney

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CERTIFICATE OF SERVICE

I hereby certify that, on this 22d day of March, 2011, that a true and correct copy of the foregoing document has been served upon counsel for the Wisconsin insurance commissioner via First Class Mail, with postage prepaid, in an envelope properly addressed as follows:

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I further certify that a true and correct copy of the foregoing document (except for replacing handwritten dates and signatures with typed versions of the same) has been served on all counsel of record using the e-mail distribution list established by the Circuit Court for Dane County for that purpose, as listed below:

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