

In the Matter of the Rehabilitation of:

Case No.: 10-CV-1576

Segregated Account of Ambac Assurance Corporation

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**COUNTER-PROPOSED ORDER WITH FINDINGS OF FACT AND  
CONCLUSIONS OF LAW OF BANK OF AMERICA, N.A. AND WELLS FARGO  
BANK, N.A., IN THEIR CAPACITIES AS SECURITIZATION TRUSTEES**

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This matter came before the Court on the Motion of the Wisconsin Commissioner of Insurance, as appointed Rehabilitator for the Segregated Account of Ambac Assurance Corporation (“Ambac”), to confirm the Plan of Rehabilitation for the Segregated Account filed on October 8, 2010 (the “Motion”).

Based on the Court’s review and consideration of the Plan and the briefs, objections, affidavits, exhibits and other materials filed in this proceeding, as well as the testimony and argument presented at the Hearing on Confirmation of the Plan, the Court makes the following Findings of Fact and reaches the following Conclusions of Law.

**FINDINGS OF FACT**

1. The terms of the policies issued by Ambac that have been placed in the Segregated Account (the “Policies”) require that Ambac pay claims in cash. (*See, e.g.*, Affidavit of Charles Brehm, sworn to November 5, 2010 (“Brehm Aff.”) Ex. B; Affidavit of Kimberly Jacobs, sworn to November 5, 2010 (“Jacobs Aff.”) Ex. B.)

2. The Plan of Rehabilitation would initially allow the Segregated Account to pay claims under the Policies 25% in cash and 75% in Surplus Notes. (*See Plan of*

Rehabilitation §§ 1.08, 1.42, 1.62 & 2.02.) The Commissioner would be permitted to adjust the cash to Surplus Notes ratio in the future. (*See id.* § 7.02.)

3. The Plan of Rehabilitation would allow the Commissioner unfettered discretion as to whether to pay any interest on or principal of the Surplus Notes. (*See id.* § 4.04(e).)

4. Holders of claims under policies in Ambac's General Account will receive payment of claims 100% in cash. (*See* Transcript of November 17, 2010 Hearing ("11/17 Tr.") at 59:24-60:6; Transcript of November 18, 2010 Hearing ("11/18 Tr.") at 167:21-25 (Testimony of Roger A. Peterson).)

5. The Commissioner has refused to disclose certain information requested by interested persons about the Plan, the Disclosure Statement and documents filed therewith. (*See, e.g.*, 11/18 Tr. at 211:15-17 (Testimony of Roger A. Peterson).)

6. The Commissioner has failed to demonstrate that holders of Policies ("Policyholders") would receive more under the Plan of Rehabilitation than they would receive in a liquidation. (*See* Amendment No. 2 to Disclosure Statement Accompanying Plan of Rehabilitation ("Amendment No. 2") at 8.)

7. The Plan of Rehabilitation would not permit Policyholders to choose to receive a liquidation amount in lieu of the consideration that would be paid under the Plan of Rehabilitation. (*See* Plan of Rehabilitation.)

8. Under the terms of many Policies and associated Operative Documents,<sup>1</sup> Ambac enjoys certain rights of subrogation and reimbursement rights for claims previously paid. (*See* Brehm Aff. ¶ 13; Jacobs Aff. ¶ 12.)

9. Although the terms of the Governing Documents vary from transaction to transaction, in many RMBS transactions, Ambac enjoys a priority right of reimbursement for claims previously paid, to the extent it was required to pay policy claims on earlier distribution dates. (*See* Brehm Aff. Ex. A; Jacobs Aff. Ex. A)

10. The Commissioner asserts that, in other RMBS transactions, Ambac enjoys similar rights to reimbursement from “excess cash” that may be generated by the transactions. (*See* Amendment No. 2 at 4.)

11. The Plan of Rehabilitation would provide that, where the Policies or Operative Documents grant Ambac any right of reimbursement, Ambac would be entitled to continue to receive all reimbursement amounts 100% in cash. (*See* Plan of Rehabilitation § 4.04(g); Disclosure Statement Accompanying Plan of Rehabilitation (“Disclosure Statement”) at 32.)

12. If Ambac were permitted to insist that all reimbursements be paid 100% in cash, it would effectively be able to drain RMBS transactions of cash, notwithstanding the fact that the Segregated Account had delivered Surplus Notes in lieu of cash in respect of a portion of the claims giving rise to the rights of reimbursement. (*See* Amendment No. 2 at 4; 11/17 Tr. at 232:3-21 (Testimony of Roger A. Peterson).)

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<sup>1</sup> The Operative Documents can include a pooling and servicing agreement, servicing agreements, a sale and servicing agreement, a trust agreement and/or an indenture and other related documents. RMBS and SLS transactions usually also incorporate an insurance agreement, which further delineates the rights and responsibilities of the parties to the transaction vis-à-vis the insurance policy (together with the Operative Documents, the “Governing Documents”).

13. The Commissioner has recognized that “[t]he payment of claims in part with Surplus Notes in non-netting deals presents a complication, as AAC benefits from receiving 100% of excess cash flow in cash, while the Segregated Account is paying 25% of claims in cash.” (Amendment No. 2 at 4.)

14. The Plan of Rehabilitation would also require that holders that receive cash and Surplus Notes in respect of claims under Policies must assign to Ambac certain rights that such holders have to receive payments under the insured notes, certificates or contracts (the “Assignment of Rights”). (*See* Plan of Rehabilitation § 4.04(h); Disclosure Statement at 32; Proof of Policy Claim Form (Ex. C to Plan of Rehabilitation).)

15. The Assignment of Rights would foreclose holders in RMBS transactions from pursuing claims for payment of cash against the primary obligors on the notes, certificates or contracts. (*Id.*)

16. The Assignment of Rights would permit Ambac to pursue remedies to be paid 100% in cash by the primary obligors on the insured notes, certificates or contracts, even though the Segregated Account paid the holders’ claims only 25% in cash. (*Id.*)

17. In SLS transactions, the Policies and/or Operative Documents entitle Ambac to receive the insured note, or an interest in a portion thereof in an amount equal to the reimbursement amount, upon payment to a Policyholder of all or a portion of the principal amount owed by the primary obligor on the underlying note (the “Assignment of Notes”). (*See* Brehm Aff. ¶ 15 & Ex. C.)

18. Under the terms of the Plan of Rehabilitation, Policyholders in SLS transactions would be foreclosed from pursuing claims for payment of cash against the

primary obligors on the notes. (*See* Plan of Rehabilitation § 4.04(g) & (h); Disclosure Statement at 32.)

19. The Assignment of Notes would permit Ambac to pursue remedies to be paid 100% in cash by the primary obligors on the notes, even though the Segregated Account paid the SLS Policyholders' claims only 25% in cash. (*See id.*)

20. The Governing Documents require that Ambac pay all timely submitted claims within a finite period of time. (*See* Brehm Aff. ¶ 7; Jacobs Aff. ¶ 6.)

21. The Plan of Rehabilitation would permit the Segregated Account an indefinite period of time in which to evaluate and deliver consideration in respect of each Policy claim. (*See* Plan of Rehabilitation § 4.04(b), (c) & (d).)

22. If the Plan of Rehabilitation were confirmed, the delay in delivery of consideration in respect of claims would present trustees, similarly situated persons and other parties to Operative Documents ("Securitization Trustees") with difficult operational issues and Holders of Ambac-insured certificates and notes could be prejudiced. (*See* Brehm Aff. ¶¶ 8-10; Jacobs Aff. ¶¶ 7-9.)

23. Under the Plan of Rehabilitation, the claims of Policyholders and others on the Surplus Notes would be subordinated to the claims of various other Ambac creditors, including Policyholders with current claims on Ambac policies. (*See* Disclosure Statement at 40-41; *see also* Form of Surplus Note, Form of Reverse § 10.)

24. The Commissioner has acknowledged that the Surplus Notes are simply a mechanism by which Ambac's cash claims payment obligations would be "slowed." (*See* Disclosure Statement at 7.)

25. The Plan of Rehabilitation would impose certain duties on “trustees” that, in some instances, are not the responsibility of trustees under the governing Operative Documents. (*See* Plan of Rehabilitation § 4.04; Brehm Aff. Ex. A § 5.05; Jacobs Aff. Ex. A § 5.01.)

26. The Operative Documents generally provide that the trustee’s duties are limited to those expressly set forth therein. (*See, e.g.*, Brehm Aff. Ex. A § 8.01; Jacobs Aff. Ex. A § 9.01.)

27. The delivery of Surplus Notes to Securitization Trustees for the benefit of the holders of Ambac-insured certificates and notes would require Securitization Trustees to assume additional responsibilities and perform new tasks, including identifying and contacting individual investors to facilitate the delivery of Surplus Notes, and implementing and managing new reporting, reconciliation, oversight, quality control, staffing, documentation, compliance and audit procedures. (*See* Plan of Rehabilitation § 4.04(d); Brehm Aff. ¶ 11; Jacobs Aff. ¶ 10.)

28. The Plan of Rehabilitation would also force Securitization Trustees to incur a number of out-of-pocket expenses, including professional services fees (attorneys, accountants and consultants) and fees charged by the Depositary Trust Corporation (“DTC”). (*See* Brehm Aff. ¶ 11; Jacobs Aff. ¶ 10.)

29. The Plan of Rehabilitation contains no provision that would permit Securitization Trustees to be compensated for tasks they would be required to perform or expenses they would be required to incur under the Plan of Rehabilitation. (*See* 11/17 Tr. at 239:12-242:15 (Testimony of Roger A. Peterson).)

30. The Commissioner asked the DTC whether it would be willing to perform certain of the tasks and incur certain of the expenses described above, and the DTC refused to do so voluntarily. (*See* 11/18 Tr. at 118:18-119:6 (Testimony of Roger A. Peterson).)

31. The Plan of Rehabilitation would provide sweeping exculpation and indemnification to the Commissioner, Ambac and certain related person, in respect of any claims that might be asserted against them in connection with the Plan of Rehabilitation. (*See* Plan of Rehabilitation §§ 9.01 & 9.02.)

32. The Plan of Rehabilitation includes terms exculpating certain (but not all) Securitization Trustees from some sources of liability and indemnifying such entities in respect of claims that might be asserted against them in connection with their compliance with the Plan of Rehabilitation, but it does not provide protection for, and it cannot anticipate the full scope of issues that may arise from, the adoption and implementation of the proposed Plan. (*See* Plan of Rehabilitation.)

### **CONCLUSIONS OF LAW**

1. The Plan of Rehabilitation does not adequately protect the interests of all Policyholders. *See* Wis. Stats. § 645.01(4). The Plan of Rehabilitation also does not treat all Policyholders fairly and equitably. *See* Wis. Stats. § 601.01(2).

2. The Commissioner has not demonstrated that Policyholders would be better off under the Plan of Rehabilitation than in a liquidation, nor has he permitted Policyholders to opt out of the Plan of Rehabilitation. *See Carpenter v. Pacific Mut. Life Ins. Co.*, 74 P.2d 761 (Cal. 1937) (en banc), *aff'd sub nom. Neblett v. Carpenter*, 305 U.S.

297 (1938); *Commercial Nat'l Bank in Shreveport v. Garmendi*, 17 Cal. Rptr. 884 (Cal. Ct. App. 1993).

3. The Commissioner has failed to establish that an injunction permanently memorializing the terms of the Order for Temporary Injunctive Relief, dated March 24, 2010, is necessary and proper. *See* Wis. Stats. § 645.05.

4. The Plan of Rehabilitation's reimbursement, Assignment of Rights and Assignment of Notes provisions would violate the "made whole" doctrine, which provides that a party claiming subrogation rights may not recover until the insured is fully compensated for his or her losses. *See Ruckel v. Gassner*, 2002 WI 67, ¶ 17, 253 Wis. 2d 280, ¶ 17, 646 N.W.2d 11, ¶ 17 ("The burden of loss should rest on the party paid to assume the risk, and not on an inadequately compensated insured.") (quoting *Couch on Insurance*, §§ 223:133, 223:136 (3d ed. 2000)).

5. The Commissioner has no regulatory responsibility in respect of Securitization Trustees and has no authority to alter their vested contractual and economic rights. The Commissioner therefore has no authority to impose on Securitization Trustees, through the Plan of Rehabilitation, duties and responsibilities that are not set forth in Operative Documents to which the Securitization Trustees are parties. *See, e.g., Elliott Assocs. v. J. Henry Schroder Bank & Trust Co.*, 838 F.2d 66 (2d Cir. 1988) (holding that it is "well-established under state common law that the duties of an indenture trustee are strictly defined and limited to the terms of the indenture" and that "we have consistently rejected the imposition of additional duties on the trustee."); *AG Capital Funding Partners, L.P. v. State St. Bank & Trust Co.*, 866 N.Y.S.2d 578, 583

(N.Y. 2008) (reviewing authorities and concluding that an indenture trustee shall not be liable except for the performance of such duties as are specifically set out in the applicable indenture).

WHEREFORE, IT IS HEREBY ORDERED that the Rehabilitator's Motion for Confirmation of Plan of Rehabilitation is DENIED.

Dated: \_\_\_\_\_

BY THE COURT

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Honorable William D. Johnston  
Lafayette County Circuit Court Judge  
Presiding by Judicial Appointment