

## **PLAN OF OPERATION FOR THE SEGREGATED ACCOUNT OF AMBAC ASSURANCE CORPORATION**

This Plan of Operation for the Segregated Account of Ambac Assurance Corporation (this "Plan of Operation") sets forth the manner by which Ambac Assurance Corporation (the "Company") will establish and operate the Segregated Account of Ambac Assurance Corporation (the "Segregated Account").

### **I. Establishment of Segregated Account**

Subject to the approval of the Wisconsin Office of the Commissioner of Insurance ("OCI"), the Company will establish and operate the Segregated Account as an optional segregated account pursuant to Wis. Stat. § 611.24(2), effective as of March 24, 2010. This Plan of Operation may be amended from time to time by the Board of Directors of the Company, subject to the approval of the OCI.

### **II. Purpose of Segregated Account**

The Company is establishing the Segregated Account for the purpose of segregating certain segments of its liabilities, and consenting to the subsequent rehabilitation of the Segregated Account under Chapter 645 of the Wisconsin Statutes. Following the execution of an Order for Rehabilitation of the Segregated Account, the rehabilitator will assume control of the management of the Segregated Account for the purpose of conducting an orderly run-off and/or settlement of the policy and other liabilities allocated to the Segregated Account in accordance with a Plan of Rehabilitation to be approved by the rehabilitation court pursuant to Section 645.33(5) of the Wisconsin Statutes (the "Plan of Rehabilitation").

### **III. Management of the Segregated Account**

Pursuant to the terms of the Management Services Agreement (the "Management Services Agreement") attached hereto as Exhibit A, the Company will be appointed as the Management Services Provider for the Segregated Account (the "Management Services Provider") for so long as such agreement is in effect. Nothing in this Section prevents the Segregated Account from retaining additional service providers to provide services in addition to those provided by the Management Services Provider.

In addition, pursuant to the terms of a Cooperation Agreement (the "Cooperation Agreement"), the Company and the Segregated Account will agree to certain matters related to decision-making, information sharing, tax compliance and allocation of expenses, all as set forth in the Cooperation Agreement. The form of the Cooperation Agreement is attached hereto as Exhibit B.

### **IV. Allocations to Segregated Account**

*Financial Guaranty Insurance Policies.* A list of all financial guaranty insurance policies and surety bonds being allocated to the Segregated Account (other than those covering student loans (which are addressed in clause 4 below) and those covering certain residential mortgage backed

securities (which are addressed in the paragraph following clause 4 below)) is attached hereto as Exhibit C. Policies being allocated to the Segregated Account include policies insuring or relating to the following:

1. All credit default swaps with respect to which a forbearance agreement executed by the Company and OCI (among others) to temporarily forbear from collecting or enforcing (or consenting to or directing the collection or enforcement of) claims against the Company or Ambac Credit Products, LLC (“ACP”) arising from termination or acceleration of the obligations of the Company or ACP based upon commencement of the rehabilitation proceedings of the Segregated Account is not in full force and effect.
2. Residential mortgage backed securities.
3. Certain other identified policies expected to suffer material losses, which losses may or may not arise due to the occurrence of an early termination or a loss of control rights arising from the rehabilitation of the Segregated Account.
4. Certain student loan policies, as follows:
  - a. Student loan policies identified on Exhibit D hereto will be allocated to the Segregated Account immediately upon establishment of the Segregated Account.
  - b. Student loan policies identified on Exhibit E hereto shall initially remain in the Company’s general account, but shall be subject to an assessment process. The assessment shall begin following the entry of an Order for Rehabilitation with respect to the Segregated Account and shall continue for 180 days thereafter (the “Assessment Period”). During the Assessment Period and for a period of 90 days thereafter, any such student loan policy may be allocated to the Segregated Account.

Any residential mortgage backed securities not initially allocated to the Segregated Account shall be allocated thereto within 20 days following the establishment of the Segregated Account, subject to any necessary filings or approvals of the rehabilitation court. With the sole exception of the policies described in the immediately preceding sentence and student loan policies described in clause 4b above, none of the Company’s policies shall be subject to an assessment or allocated on an ad hoc or rolling basis into the Segregated Account; provided, however, that clerical errors and oversights may be corrected with the consent of OCI and filed with or approved by the rehabilitation court as required.

*Remediation.* All remediation claims, defenses, offsets, and/or credits (except to the extent described in clause (iv) of Section V - “Collateral Security” below), if any, in respect of policies allocated to the Segregated Account, whether now existing or hereafter arising, are allocated to the Segregated Account together with such policies.

*Lease with One State Street, LLC.* The Company is allocating to the Segregated Account its disputed contingent liability, if any, under the long-term lease with One State Street, LLC, effective January 1, 1992 and amended as of August 1, 1997.

*Liability as Guarantor of Ambac Assurance UK Limited's lease with British Land.* The Company is allocating to the Segregated Account its contingent liability, if any, as guarantor of the obligations of Ambac Assurance UK Limited under its lease with British Land.

*Ownership Interests.* The Company is allocating to the Segregated Account its limited liability interest in ACP, Ambac Conduit Funding LLC, Aleutian Investments LLC and Juneau Investments LLC.

*Reinsurance Agreements.* The Company is allocating to the Segregated Account all liabilities assumed by the Company as reinsurer under the reinsurance agreements listed on Exhibit F attached hereto.

## **V. Provision for Capital and Surplus**

The Segregated Account will support the liabilities allocated to it with the following resources:

*Secured Note.* The Company's general account will issue a secured note to the Segregated Account in the face amount of \$2 billion dollars (the "Secured Note"). Under the terms of the Secured Note, the Segregated Account will be permitted to demand payment of note principal to satisfy liabilities of the Segregated Account due and payable in respect of cash claim payments, payments on other liabilities allocated to the segregated account, administrative and operating expenses, loss settlements, commutation payments, payments under surplus notes or contribution notes, if any, issued by the Segregated Account, and any other amounts directed or ordered to be paid by the rehabilitation court in conjunction with the rehabilitation proceeding, all as more fully set forth in the Secured Note. The demand amount shall be reduced by the amount, as calculated by the Segregated Account, of the Segregated Account's liquid assets available to pay such liabilities at such time. In no case will the Company's general account have any liability to make any payment to the Segregated Account under the Secured Note to the extent that such payment would result in the surplus as regards policyholders of the Company's general account falling below \$100 million (or such higher amount as determined by OCI pursuant to a prescribed accounting practice) and for any period during which the surplus as regards policyholders of the Company's general account is below such amount. The form of the Secured Note is attached hereto as Exhibit G.

*Aggregate Excess of Loss Reinsurance Agreement.* The Company's general account will issue an Aggregate Excess of Loss Reinsurance Agreement to the Segregated Account (the "Reinsurance Agreement"). Under the terms of the Reinsurance Agreement, the Company's general account will provide aggregate excess of loss coverage equal to the liabilities of the Segregated Account due and payable in respect of cash claim payments, loss settlements, commutation payments, payments under surplus notes or contribution notes, if any, issued by the Segregated Account, and any other amounts directed or ordered to be paid by the rehabilitation court in conjunction with the rehabilitation proceeding, all as more fully set forth in the Reinsurance Agreement. The amount of the reinsurance recoverable shall be reduced by the amount, as calculated by the Segregated Account, of the Segregated Account's liquid assets available to pay such liabilities at such time. In no case will the Company's general account have any liability to make any payment to the Segregated Account under the Secured Note to the

extent that such payment would result in the surplus as regards policyholders of the Company's general account falling below \$100 million (or such higher amount as determined by OCI pursuant to a prescribed accounting practice) and for any period during which the surplus as regards policyholders of the Company's general account is below such amount. Coverage under the Reinsurance Agreement will attach after all principal under the Secured Note has been paid by the Company's general account. The form of the Reinsurance Agreement is attached hereto as Exhibit H.

*Surplus Notes.* In accordance with the terms of the Plan of Rehabilitation, the Company's general account may issue surplus or contribution notes ("Surplus Notes") to the holders of policies allocated to the Segregated Account to satisfy that portion of the claim liabilities due and payable under such policies which is not paid directly by the Segregated Account in cash or in surplus notes or contribution notes of the Segregated Account.

*Collateral Security.* As security for the obligations of the Company's general account to the Segregated Account, the Company's general account will grant a security interest to the Segregated Account in the following assets, as more fully set forth in the Secured Note and Reinsurance Agreement:

- (i) installment premiums received in conjunction with policies allocated to the Segregated Account and premiums received under reinsurance agreements;
- (ii) reinsurance premiums received in respect of assumed reinsurance agreements with respect to which the liabilities of the Company have been allocated to the Segregated Account;
- (iii) recoveries under third party reinsurance agreements covering losses on policies allocated to the Segregated Account; and
- (iv) any recoveries arising from remediation efforts or reimbursement or collection rights with respect to policies allocated to the Segregated Account.

All assets within the Segregated Account will be available exclusively for satisfying liabilities attributable to the Segregated Account. The Company will ensure that all assets of the Segregated Account, including any income earned thereon, remain identifiable within the Segregated Account. Pursuant to Wis. Stat. § 611.24(3)(b), any income, gains and losses, whether or not realized, from assets and investments attributable to the Segregated Account, if any, will be credited to or charged against the Segregated Account without regard to other income, gains, or losses of the Company's general account.

In connection with its review and approval of this Plan of Operation, OCI has determined that there is an adequate amount of capital and surplus in the Segregated Account pursuant to Wis. Stat. § 611.24(3)(a) and that the provisions for capital and surplus contemplated herein with respect to the liabilities allocated to the Segregated Account constitute fair consideration within the meaning of Wis. Stat. § 645.03(d).

## **VI. Charges and Expenses**

Pursuant to Wis. Stat. § 611.24(3)(c), assets and investments allocated to the Segregated Account, if any, will be available and used solely to satisfy costs, expenses, charges, and liabilities attributable to the business placed therein. Such assets and investments, if any, will not be charged with any costs, expenses, charges, or liabilities arising out of any other business of the Company, except as otherwise provided in the Secured Note or Reinsurance Agreement. Likewise, assets and investments in the Company's general account will not be charged with any costs, expenses, charges, or liabilities arising out of the direct business allocated to the Segregated Account.

The Company will divide any expenses for which the Company's general account has not been compensated pursuant to the Management Services Agreement, on such reasonable basis as the Rehabilitator and the Company shall mutually agree, between the Company's general account and the Segregated Account.

The Segregated Account may offset and recoup any balance or amount due from the Company to the Segregated Account.

Time is of the essence with respect to all payment obligations from the Company to the Segregated Account. No extension of time for performance of any payment obligation shall be deemed an extension of time for performance of any other payment obligation.

## **VII. Financial Statements**

The Management Services Provider will prepare periodic statutory financial statements for the Segregated Account commencing with the 2010 calendar year.

## **VIII. Dissolution; Merger**

Unless otherwise previously dissolved or merged into the Company's general account, the Company will merge the Segregated Account into the Company's general account upon the final resolution of all liabilities attributable to the business allocated to the Segregated Account, or upon order from the Commissioner.