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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re AMBAC FINANCIAL GROUP, INC., Debtor.	Chapter 11 Case No.: 10-15973 (SCC)
AMBAC FINANCIAL GROUP, INC., Plaintiff, v. KARTHIKEYAN V. VEERA, Defendant.	Adv. Pro. No.: 11-1265 (SCC)

LIMITED OBJECTION OF KARTHIKEYAN V. VEERA TO DEBTOR'S THIRD AMENDED PLAN OF REORGANIZATION UNDER CHAPTER 11 OF THE BANKRUPTCY CODE

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Karthikeyan V. Veera ("Veera" or "Objector") on behalf of himself, the participants in the Ambac Savings and Investment Plan ("SIP") and the SIP, files this limited objection[1] to the Third Amended Plan of Reorganization under Chapter 11 of the Bankruptcy Code, filed on February 24, 2012 (Docket No. 829) ("Plan of Reorganization" or "Plan") by the Debtor Ambac Financial Group, Inc. ("Debtor" or "Ambac") and would show the Court:

SUMMARY OF THE OBJECTION

1. Veera is the plaintiff in the action entitled *Veera v. Ambac Plan Administrative Committee, et al.*, Civil Action No: 1:10-cv-4191 (HB) (S.D.N.Y) (the "*ERISA Action*") and objects to the proposed release terms and provisions of the Plan as being over-broad and improper because they attempt to release the claims in the *ERISA Action* against the non-debtor defendants in the *ERISA Action*. Specifically, Veera objects to Articles I.A.115[2] and VIII.E of the Plan, and any other provisions of the Plan, to the extent that those provisions attempt to release non-debtors from any claims that Veera has asserted in the *ERISA Action*. Such overly broad releases for non-debtors as those found in the Plan are a blatant attempt to create an escape hatch for non-debtors of their obligations where there is none allowed under the law. *See In re Metromedia Fiber Network, Inc.*, 416 F.3d 136, 142 (2d Cir. 2005) (recognizing that "a nondebtor release is a device that lends itself to abuse" and holding that "A nondebtor release in a plan of reorganization should not be approved absent the finding that truly unusual circumstances render the release terms important to success of the plan...").

2. Veera respectfully proposes adding the following language to Article VIII.E of the Plan and the Order of Confirmation to remedy this objection:

[1] By agreement between the parties, Veera's time to object to Debtor's Plan or Reorganization was extended through Friday, March 2, 2012.

[2] Article I.A.113 in the Second Amended Plan.

> Neither the Plan nor any contract, instrument, release, agreement or document executed or delivered in connection therewith, nor the occurrence of the Effective Date shall release, waive, discharge, contribute, or assign any of the claims or causes of action against the non-debtor defendants in *Veera v. Ambac Plan Administrative Committee, et al.*, Civil Action No: 1:10-cv-3191 (HB) (the "*ERISA Action*").[3]

BACKGROUND OF THE OBJECTOR'S INTERESTS

3. Veera brought the *ERISA Action* on behalf of himself, the SIP, and SIP Participants whose plan accounts included investments in Ambac stock or units. He alleges that during the Class Period,[4] as defined in the *ERISA Action*, the non-debtor fiduciaries of the SIP caused losses to the SIP and to the SIP Participants by offering Ambac stock as a retirement investment in the SIP when it was imprudent to do so and otherwise violated their obligations under the SIP and under ERISA.

4. Although the Debtor was named in Veera's original complaint, preliminary discovery revealed that the Debtor was not a fiduciary of the SIP and, as a result, Veera amended the complaint on September 7, 2010 (before the Debtor filed for bankruptcy protection) removing the Debtor as a defendant.

5. The *ERISA Action* does not name the Debtor as a defendant. The only defendants are non-debtors who served as fiduciaries of the SIP.[5] The claims asserted in the *ERISA Action* against each of the non-debtors are brought against the named Non-Debtor ERISA Defendants

[3] This language is intended to mirror the new language included in the Third Amended Plan expressly excluding from the release provisions of Article VIII.E any claims against the Released Parties relating *In re Ambac Financial Group Inc. Sec. Litig.*, No. 08-cv-411(NRB). *See* Article VIII.E.

[4] The Class Period in the *ERISA Action* is October 1, 2006 through July 2, 2008.

[5] The named defendants in the *ERISA Action* include fourteen individuals and three committee defendants. Specifically the non-debtor individual defendants in the *ERISA Action* are: Diana Adams, Gregg L. Bienstock, Jill M. Considine, Thomas J. Gandolfo, Anne Gill Kelly, Sean T. Leonard, William McKinnon, Douglas C. Renfield-Miller, Timothy J. Stevens, Thomas C. Theobald, Laura S. Unger, and Henry D.G. Wallace. To the best of Veera's knowledge, non-debtor defendants Bienstock, Gandolfo, Kelly, Leonard, McKinnon, Renfield-Miller, and Stevens are no longer with the Debtor or Ambac Assurance. The committee defendants, which were comprised of the individual non-debtor defendants listed above are the Ambac Plan Administrative Committee, the Ambac Compensation Committee and the Ambac Plan Investment Committee (collectively "Non-Debtor ERISA Defendants").

only in their capacity as fiduciaries to the SIP for breaching their fiduciary duties.

6. The Debtor filed a voluntary petition for bankruptcy on November 8, 2010.

7. On January 6, 2011, Judge Baer, presiding over the *ERISA Action*, denied the Non-Debtor ERISA Defendants' motion to dismiss Veera's claims. *See Veera v. Ambac Plan Administrative Committee et al.*, 769 F. Supp. 2d 233 (S.D.N.Y. 2011). Less than two months later, on March 4, 2011, Judge Baer denied the Non-Debtor ERISA Defendants' motion to certify his January 6, 2011 ruling for interlocutory appeal.

8. On March 7, 2011, this Court granted the Debtor's motion for summary judgment against Veera and extended the automatic stay to temporarily halt the prosecution of the *ERISA Action* pending Ambac's reorganization. The primary reason for the Court's decision to extend the § 362(a) stay to the *ERISA Action* was to provide "breathing room" for the Debtor to focus on negotiating its Plan. *See* Debtor's Motion for Summary Judgment at 5 [Adv. Pr. Dkt. No. 05].

9. On May 9, 2011, Debtor filed a proposed order modifying the automatic stay so that the parties to a parallel securities class action could seek preliminary approval of a proposed settlement in that case. [Dkt. No. 262]. The settlement ("Securities Settlement Agreement") related to *In re Ambac Financial Group Inc. Sec. Litig.*, No. 08-cv-411(NRB) ("*Securities Action*"), then pending in the Southern District of New York.

10. Because the release provisions in the Securities Settlement Agreement threatened to release the claims in the *ERISA Action*, Veera objected to the proposed release. Similar to the objection that Veera now presents to this Court, Veera objected to the broad release provisions in the proposed Securities Settlement Agreement to the extent that they could be read to release any of the claims in the *ERISA Action*, and Veera proposed amending the Securities Settlement Agreement to expressly carve out the *ERISA Action* from the release.

11. On May 15, 2011, the parties to the *Securities Action*, including Ambac, resolved Veera's objection by amending the Securities Settlement Agreement as Veera suggested to specifically exclude the *ERISA Action* from the release provisions of the stipulation. *See* Second Amended Disclosure Statement at 34 [Dkt. No. 601].

12. On July 15, 2011, having secured an exclusion for the *ERISA Action* from the Securities Settlement Agreement, Veera sought permission from this Court to move forward with the *ERISA Action*. This Court however denied that request, citing the "critical and delicate situation" the Debtor remained in while negotiating the terms of its plan of reorganization. *See* Transcript of Hearing held on July 19, 2011, 27:1 [Dkt. No. 501].

13. Since then Veera has cooperated with Ambac's counsel to avoid unnecessarily distracting the Debtor while it worked to resolve and overcome the remaining impediments to a successful reorganization. Now, despite agreeing in the Securities Settlement Agreement to not release the claims in the *ERISA Action*, Debtor takes a contrary position in its Plan and seeks to extinguish the claims in the *ERISA Action* for the Non-Debtor ERISA Defendants without justification or any legal basis for doing so. Second Circuit law rejects this type of proposed release. *Metromedia*, 416 F.3d at 142.

OBJECTION TO THE PLAN

14. The Plan defines Released Parties as:

> collectively, the Debtor, the Reorganized Debtor, AAC, the Segregated Account, OCI, the Rehabilitator, the board of directors and board committees of the Debtor and AAC, **all current and former individual directors, officers, or employees of the Debtor and AAC**, the Committee and the individual members thereof, the Indenture Trustees, the Informal Group and the individual members thereof, and each of their respective Representatives (each of the foregoing in its individual capacity as such).

See Article I.A.115 (emphasis supplied).

15. The Plan also provides a general release by holders of claims and equity interests which states:

> Except as otherwise provided in Article VIII.H of the Plan and to the extent permitted by applicable law, as of the Effective Date, each Entity that has held, holds, or may hold a Claim or an Equity Interest, as applicable, in consideration for the obligations of the Debtor under the Plan, the Plan distributions, and other agreements, securities, instruments, or other documents executed or delivered in connection with the Plan, **shall be deemed to have conclusively, absolutely, unconditionally, irrevocably, and forever released and discharged the Released Parties from any and all Claims and Causes of Action of any nature whatsoever, including any derivative Claims asserted by or on behalf of the Debtor, that such entity would have been legally entitled to assert based upon or relating to any act, omission, transaction, event, or other occurrence taking place on or prior to the Effective Date and based upon or relating to the Debtor, the Estate, the Reorganized Debtor, the Chapter 11 Case, or the preparation, negotiation, or implementation of the Plan or Disclosure Statement;** *provided*, *however*, that the foregoing shall not apply to (i) any act which constitutes a bankruptcy crime under title 18 of the United States Code, (ii) any claims that policyholders or securities holders may have against AAC or the Segregated Account pursuant to their respective policies or securities, (iii) any obligations of the Reorganized Debtor pursuant to the Plan and (iv) any claims arising under the Amended TSA, the Cost Allocation Agreement, the Cooperation Agreement, the Mediation Agreement or any other documents entered into in connection with the Amended Plan Settlement; *provided further*, *however*, that the Released Parties shall not be released from any Claims arising out of or relating to the Securities Actions, and any releases of the Released Parties granted pursuant to the Stipulation of Settlement shall not become effective, unless and until the Stipulation of Settlement 9019 Approval Order becomes a Final Order. Notwithstanding anything to the contrary in the Plan, One State Street, LLC shall continue to be entitled to the benefits set forth in the OSS Settlement Agreement.

See Article VIII.E (emphasis supplied).

16. Veera objects to the provisions in Articles I.A.115 and VIII.E of the Plan and any other provisions of the Plan to the extent that these provisions purport to release, discharge, exculpate or enjoin any claims or causes of action against the Non-Debtor ERISA Defendants named in the *ERISA Action*. Specifically Article VIII.E of the Plan (in conjunction with Article

I.A.115) would improperly release various non-debtors, including the Non-Debtor ERISA Defendants, when there is no legitimate basis for releasing them.

17. Veera objects on the grounds that (1) these broad non-debtor releases fail to comport with the requirements established by the Second Circuit; and (2) the release of the claims in the *ERISA Action* is inconsistent with the remaining provisions of the Plan.

18. The Debtor fails to provide any justification for the breadth of the Plan's releases, most likely because there is none.

DISCUSSION

1. The Debtor Does Not Satisfy the *Metromedia* Standards

Non-debtor releases in the Second Circuit are the exception – not the rule. Indeed, non-debtor releases are only appropriate in *rare* cases, and a non-debtor release in a plan of reorganization should not be approved absent a finding that *truly unusual* circumstances render the release terms important to the success of the plan. *Metromedia*, 416 F.3d at 141-43. As explained below, there are no unusual or rare circumstances that would justify the broad releases proposed in the Plan.

In *Metromedia*, the Second Circuit held that non-debtor releases do not pass muster simply because they are contemplated by a debtor in the plan. The Second Circuit criticized these releases as "a bankruptcy discharge arranged without a filing and without the safeguards of the Code." *Id.* at 142 (recognizing that "a nondebtor release is a device that lends itself to abuse"). In analyzing the applicable case law, the *Metromedia* Court opined that approving non-debtor releases is "not a matter of factors and prongs," and that "no case has tolerated nondebtor releases absent the finding of circumstances that may be characterized as unique." *Id.* at 142. These "unique" circumstances have been found in only a limited number of cases, *i.e.*, where (1)

the estate received substantial consideration from the released party, *see Drexel Burnham Lambert Group, Inc.*, 960 F.2d 285, 292 (2d Cir. 1992) (multi-billion dollar settlement including a payment of over a billion dollars into fund by Michael Milken and other co-liable Drexel personnel); (2) the enjoined claims were "channeled" to a settlement fund rather than extinguished, *see MacArthur Co. v. Johns-Manville Corp. (In re Johns-Manville Corp.)*, 837 F.2d 89, 93-94 (2d Cir. 1988); (3) the enjoined claims would indirectly impact the debtor's reorganization "by way of indemnity or contribution," *and* the plan otherwise provided for full payment of the enjoined claims, *see In re A.H. Robins Co., Inc.*, 880 F.2d 694, 701 (4th Cir. 1989); and (4) the affected creditors consented. *See In re Specialty Equip. Cos.*, 3 F.3d 1043, 1047 (7th Cir. 1993); *see also Metromedia,* 416 F.3d at 142 (citing cases).

Subsequent cases further clarify the *Metromedia* requirements. In *In re Karta Corp.*, 342 B.R. 45 (S.D.N.Y. 2006), the Court, with an eye on *Metromedia* and following the Second Circuit's narrow standard, found that the case before it was "the rare case" involving unusual facts that justified the release of certain non-debtor parties, including the plan funders and an affiliated company. *Id.* at 55. In *Karta* the Court expressly determined that the non-debtor releases provisions were "important" to the Debtor's plan of reorganization because the released parties agreed to make a substantial financial contribution to fund the plan only if they would be released from creditors' claims *and* the released parties were the principals of a company affiliated with the debtor owning difference assets used to run a single integrated empire with the debtor company. *Id* at 56. The court expressly held that it was not enough that the released parties would not fund the plan absent approval of the releases. *Id* at 55 (finding that it would be an abuse of process simply to allow the release of a non-debtor in return for its financial contribution). Something else was therefore needed in order to make a case "unique." *Id.* The

Court framed the issue as "whether a significant non-debtor financial contribution plus other unusual factors render a situation so 'unique' that non-debtor releases are appropriate." *Id.*[6]

The circumstances of Ambac's reorganization lack any of the "uniqueness" factors necessary to justify the broad non-debtor releases contained within the Plan. And while some of the beneficiaries of the non-debtor releases – namely Ambac Assurance Corporation ("AAC"), Ambac's principal operating subsidiary – may have contributed assets and other valuable consideration toward the successful reorganization of the Debtor, the same cannot be said for the Non-Debtor ERISA Defendants, who have not. In fact, many of the individual Non-Debtor ERISA Defendants are no longer affiliated with Ambac in any way.[7]

Insofar as any threat of indemnification against the Debtor has existed– a factor that the Court considered in its earlier decision to apply the § 362 automatic stay – by operation of the Plan's remaining release provisions in Article VIII, the claims by Veera against the Non-Debtor ERISA Defendants will no longer be subject to indemnification by the Debtor. Specifically, Article VIII.D (*General Releases By the Debtor*) proposes to release all claims by the Released Parties against the Debtor "of any nature whatsoever…based upon or relating to any act, omission, transaction, event or other occurrence taking place on or prior to the Effective Date." Even if the Debtor's indemnification obligations were to somehow survive the bankruptcy, the mere possibility of such a requirement is not enough to justify releasing third-party claims. *See In re Saint Vincent's Catholic Medical Centers of NY*, 417 B.R. 688, 696 (S.D.N.Y. 2009)

[6] *See also In re Spiegel Inc.*, No. 03-11540-BRL, 2006 WL 2577825, *7 (Bankr. S.D.N.Y. Aug. 16, 2006) (Plan's third-party releases and injunctions were critical components of the settlement that played a "vital part in the plan" and were "necessary to the proposed reorganization of the Debtors and the successful administration of their estates"); *In re XO Communications, Inc.*, 330 B.R. 394, 440 (Bankr. S.D.N.Y. 2005) (third-party releases permissible where non-debtors provided significant consideration, releases were integral to the Plan, and non-debtors' interests aligned with those of the Debtors with regard to claims.)

[7] The Non-Debtor Defendants no longer affiliated with the Debtor or AAC are: Gregg L. Bienstock, Anne Gill Kelly, Sean T. Leonard, William McKinnon, Douglas C. Renfield-Miller, Timothy J. Stevens, and Thomas Gandolfo.

(upholding Bankruptcy Court's rejection of non-debtor releases noting that the Bankruptcy Court "did not make any findings that discharging the liability of third-party Covered Persons would be important to the Plan.").

Moreover, the Plan provides for no means of "channeling" the claims in the *ERISA Acton*, nor does it provide Veera, the SIP or the SIP Participants with any consideration of any kind. *Saint Vincent's*, 417 B.R. at 696 (noting that "the Bankruptcy Court [did not find that] the third-party Covered Persons had given substantial consideration to the estate; that enjoined claims against Covered Persons would be channeled to a settlement fund, and not just extinguished; nor that the Plan provided for payment of such claims in any way.").

Finally, neither Veera nor the members of the putative class in the *ERISA Action* have consented to the Plan's proposed releases. In fact, as mere owners of equity interests, Veera and the members of the putative class are not entitled to vote on the Plan and are otherwise deemed to reject its terms.

The Debtor may argue – as it has consistently stated throughout these bankruptcy proceedings – that AAC's insistence on broad non-debtor releases is necessary for the Debtor's reorganization. This, however, is exactly the type of abuse that the Second Circuit warned against in *Metromedia*. *Metromedia*, 416 F.3d at 142; *see also Karta*, 342 B.R. at 54 (noting that "Anyone can devise a plan that involves contributions from non-debtors who (not surprisingly) would condition their participation on being shielded from *their* creditors. And just as every unhappy family is unhappy in its own way … every multi-debtor corporate bankruptcy can come up with some aspect of its situation that seems to it, and to its creditors, to be 'unique.' ").

Moreover, even if AAC's contribution is essential in Ambac's reorganization efforts and a release of claims against AAC comports with *Metromedia*, no justification exists for extending

these releases to the Non-Debtor ERISA Defendants in the *ERISA Action* who have not made any meaningful financial contributions to the Debtor's reorganization.

Neither the Plan nor the Disclosure Statement provides any justification for the non-debtor releases. Moreover, the releases improperly provide blanket immunity to non-debtors against any and all claims arising prior to the Effective Date. Specifically, the releases include all claims "of any nature whatsoever, including any derivative Claims asserted by or on behalf of the Debtor, that such entity would have been legally entitled to assert based upon or relating to any act, omission, transaction, event, or other occurrence taking place on or prior to the Effective Date and based upon or related to the Debtor, the Estate, the Reorganized Debtor, the Chapter 11 Case, or the preparation, negotiation or implementation of the Plan or Disclosure Statement." Plan, VIII.E. Thus, under *Metromedia* and *Karta*, the Court should reject the Debtor's proposed blanket release of the Non-Debtor ERISA Defendants.

2. The Release Provision is Inconsistent with the Remaining Provisions of the Plan with Respect to the *ERISA Action*

Under the Plan's own terms, the *ERISA Action* should be excluded from the Release provisions. Outside of the *Definitions* section, the *ERISA Action* is expressly mentioned in only one section of the Plan: Article VIII.F.3. That section provides that "the injunctions and releases set forth in Article VIII.F of the Plan and in the Stipulation of Settlement 9010 Approval Order do not release and/or bar the ERISA claims at issue in the ERISA Action…" or the Securities Settlement Agreement.

This carve-out of the *ERISA Action* from the release provisions of the Securities Settlement Agreement – the settlement entered into by the parties to the *Securities Action* – is of course the result of Veera's objection and subsequent negotiations with the parties to the *Securities Action* (including the Debtor) in May of 2011. *See supra*, ¶9. It is illogical to suppose

that all of the parties involved in negotiating the scope of the release in the *Securities Action*, including the Debtor, worked cooperatively to exempt the *ERISA Action* from the release of the Stipulation and Settlement only to later release those claims through the terms of the Plan.

In any event, pursuant to the Conflicts section of the Plan at Article XII.O, to the extent that the Plan's releases are inconsistent with the terms of the Stipulation of Settlement or the Stipulation of Settlement 9019 Approval Order, "the terms of such [the Securities Settlement Agreement] shall control." In other words, applying the Plan's Releases in Article I.A.115 and Article VIII to the *ERISA Action* is inconsistent with the terms of the settlement in the *Securities Action* and therefore prohibited under the Plan.

CONCLUSION

For the reasons set forth above, the Court should reject the proposed non-debtor releases set forth in Article I.A.115 and Article VIII of the Third Amended Plan of Reorganization or, alternatively, modify the provisions to specifically exclude Veera and the *ERISA Action* from the release.

Dated: March 2, 2012

Respectfully submitted,

/s/ Stephen J. Fearon, Jr.

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