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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re	:	
	:	**Chapter 11**
AMBAC FINANCIAL GROUP, INC.,	:	
	:	**Case No. 10-15973 (SCC)**
Debtor.	:	

DEBTOR'S MEMORANDUM (I) IN SUPPORT OF CONFIRMATION OF THIRD AMENDED PLAN OF REORGANIZATION OF AMBAC FINANCIAL GROUP, INC. AND (II) IN RESPONSE TO OBJECTIONS THERETO

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Ambac Financial Group, Inc., as debtor and debtor in possession in the above-captioned case (the "Debtor," and together with its non-debtor affiliates, "Ambac"), having filed its third amended plan of reorganization on February 24, 2012 [Docket No. 829] (together with the exhibits thereto and as the same may be amended or modified, the "Plan"), respectfully submits this memorandum of law in support of confirmation of the Plan.[1]

PRELIMINARY STATEMENT

As described in the Debtor's Disclosure Statement, the declaration of Stephen M. Ksenak, the Debtor's General Counsel, in support of confirmation of the Plan, filed contemporaneously herewith (the "Ksenak Declaration"), the declaration of C.J. Brown of Blackstone Advisory Partners L.P. ("Blackstone"), the Debtor's financial advisor, in support of confirmation of the Plan, filed contemporaneously herewith (the "Brown Declaration"), and any additional declarations which may be filed in support of confirmation of the Plan, the Plan is the product of substantial arm's length discussions and negotiations which began prior to the commencement of the Debtor's chapter 11 case on November 8, 2010. The Plan represents a global settlement among the Debtor, the Committee, AAC, the Segregated Account, and OCI, as regulator of AAC and Rehabilitator of the Segregated Account (the "Amended Plan Settlement"). As evidenced by the certification of Kurtzman Carson Consultants LLC regarding the tabulation of votes, which shall be filed prior to the Confirmation Hearing (the "Vote Certification"), the Plan is supported by all Classes of Claims entitled to vote to accept or reject the Plan. Additionally, the Plan complies with all applicable provisions of the Bankruptcy Code, the Bankruptcy Rules, and the Local Bankruptcy Rules for the Southern District of New York (the "Local Rules"). Certain parties have filed objections to, responses to, or reservation of

[1] Capitalized terms used but not defined herein have the meanings set forth in the Plan.

rights with respect to the Plan (together, the "Objections"). As described below, however, the Objections have either been resolved or are without merit. Accordingly, the Debtor respectfully requests that the Bankruptcy Court overrule the Objections which have not been resolved and enter the Debtor's proposed Confirmation Order.

BACKGROUND

Following entry of the *Order (i) Approving the Disclosure Statement, (ii) Establishing Solicitation, Voting, and Tabulation Procedures, (iii) Appointing a Voting Agent, and (iv) Scheduling a Confirmation Hearing and Approving the Form and Manner of Notice Thereof* on October 5, 2011 [Docket No. 618] (the "Disclosure Statement Order"), the Debtor solicited votes to accept or reject the Plan from holders of Claims in Classes 3 (Senior Notes Claims), 4 (Subordinated Notes Claims), and 5 (General Unsecured Claims). As noted above and in the Vote Certification, holders of Claims in such Classes overwhelmingly voted to accept the Plan.

On February 24, 2012, the Debtor filed the Plan. Certain revisions were made in the Plan to the definition of "Amended Plan Settlement" to reflect the terms of the amended tax sharing agreement among the Debtor, AAC, and certain of their affiliates, as contemplated by the Mediation Agreement, and to the Plan's injunction, exculpation, and release provisions in response to comments received from certain parties in interest. Additionally, the Plan was modified in contemplation of resolution of the IRS Dispute post-confirmation. As set forth in the Plan, the Debtor, the Committee, AAC, the Segregated Account, OCI, and the Rehabilitator have sent an Offer Letter to the United States Attorney's Office for the Southern District of New York describing terms upon which the parties would agree to settle the IRS Dispute. The Plan provides that it shall become effective once, among other things, an IRS Settlement with terms consistent with those set forth in the Offer Letter has been approved by the United States, the Rehabilitation Court, and the Bankruptcy Court. The Plan further provides that the Confirmation

Order may be vacated, at the IRS's discretion, if the IRS Settlement has not been approved by OCI, the United States, the Rehabilitation Court, the Committee, and the boards of directors of the Debtor and AAC within one year after the Confirmation Date. The Plan also carves the United States out of certain of the Plan's discharge, injunction, exculpation, and release provisions. Further, the Plan includes a Ruling Request Agreement as an exhibit thereto, which provides that (i) the Debtor and the Committee may submit to the IRS a request to issue a private letter ruling that, pursuant to IRC section 382(l)(5)(A), no Ownership Change will be experienced by the Debtor or members of its consolidated tax group as a result of the Debtor's emergence from bankruptcy; and (ii) the Debtor shall execute a power of attorney authorizing the Rehabilitator to represent the Debtor's consolidated tax group before the IRS on all tax matters arising under the Segregated Account's rehabilitation plan.

The foregoing revisions do not constitute material Plan modifications, and therefore do not require, pursuant to Bankruptcy Code section 1127 or Bankruptcy Rule 3019, additional disclosure to holders of Claims and Equity Interests or re-solicitation of votes.

ARGUMENT

This memorandum is divided into two parts. In the first part, the Debtor asserts that the Plan satisfies Bankruptcy Code section 1129 and should be confirmed. In the second part, the Debtor addresses the Objections to confirmation of the Plan.

I. The Plan Should be Confirmed

To confirm the Plan, the Bankruptcy Court must find that the Debtor has satisfied the applicable provisions of Bankruptcy Code section 1129 by a preponderance of the evidence.[2]

[2] *See*, *e.g.*, *In re Bally Total Fitness of Greater N.Y., Inc.,* No. 07-12395, 2007 WL 2779438, at *3 (Bankr. S.D.N.Y. Sept. 17, 2007) ("The Debtors, as proponents of the Plan, have the burden of proving the satisfaction of the elements of Sections 1129(a) and (b) of the Bankruptcy Code by a preponderance of the evidence"); *In re Spiegel, Inc.*, No. 03-11540, 2005 WL 1278094, at *4 (Bankr. S.D.N.Y. May 25, 2005) ("The Debtors, as proponents of the Plan, have met their burden of proving the elements of sections 1129(a) and (b) of the Bankruptcy Code by a preponderance of

The Debtor submits that through this memorandum, the declarations filed contemporaneously herewith, and the evidence proffered and adduced at the Confirmation Hearing, the Debtor will demonstrate, by a preponderance of the evidence, that all applicable subsections of Bankruptcy Code section 1129 are satisfied with respect to the Plan.

A. Section 1129(a)(1): The Plan Complies With All Applicable Provisions of the Bankruptcy Code

Bankruptcy Code section 1129(a)(1) requires that the Plan comply with all applicable provisions of the Bankruptcy Code, including, principally, rules governing the classification of claims and interests and the contents of a plan of reorganization.[3] Accordingly, determining whether the Plan complies with Bankruptcy Code section 1129(a)(1) requires consideration of whether the Plan complies with Bankruptcy Code sections 1122 and 1123.

(1) The Plan Satisfies the Classification Requirements of Sections 1122 and 1123(a)(1)

Bankruptcy Code section 1123(a)(1) provides that "a plan shall … designate, subject to section 1122 of this title, classes of claims, other than claims of a kind specified in section 507(a)(2), 507(a)(3), or 507(a)(8) of this title, and classes of interests." Bankruptcy Code section 1122, in turn, provides as follows:

> (a) Except as provided in subsection (b) of this section, a plan may place a claim or an interest in a particular class only if such claim

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the evidence"); *In re WorldCom, Inc.*, No. 02-13533, 2003 WL 23861928, at *46 (Bankr. S.D.N.Y. Oct. 31, 2003) ("A debtor, as the proponent of the Plan, bears the burden of proof under section 1129 of the Bankruptcy Code. A debtor must meet this burden by a preponderance of the evidence"); *In re Kent Terminal Corp.*, 166 B.R. 555, 561 (Bankr. S.D.N.Y. 1994) ("Notwithstanding this time-sensitive evidentiary burden, the final burden of proof at both the relief from stay and confirmation hearings remains a preponderance of the evidence").

[3] *See Kane v. Johns-Manville Corp.* (*In re Johns-Manville Corp.),* 843 F.2d 636, 648-49 (2d Cir. 1988) (the legislative history "suggest that Congress intended the phrase 'applicable provisions' in [Bankruptcy Code section 1129(a)(1)] to mean provisions of Chapter 11 … such as section 1122"); *In re Drexel Burnham Lambert Group, Inc.,* 138 B.R. 723, 757 (Bankr. S.D.N.Y. 1992) (noting that "[t]he legislative history of § 1129(a)(1) explains that this provision embodies the requirements of §§ 1122 and 1123, respectively, governing classification of claims and the contents of the Plan").

> or interest is substantially similar to the other claims or interests of such class.
>
> (b) A plan may designate a separate class of claims consisting only of every unsecured claim that is less than or reduced to an amount that the court approves as reasonable and necessary for administrative convenience.

As required by Bankruptcy Code section 1123(a)(1), in addition to Administrative Claims, Claims for Accrued Professional Compensation, and Priority Tax Claims, which need not be classified, Article III of the Plan designates seven Classes of Claims and one Class of Equity Interests: Class 1 (Priority Non-Tax Claims), Class 2 (Secured Claims), Class 3 (General Unsecured Claims), Class 4 (Senior Notes Claims), Class 5 (Subordinated Notes Claims), Class 6 (Section 510(b) Claims), Class 7 (Intercompany Claims), and Class 8 (Equity Interests). As required by Bankruptcy Code section 1122(a), each Claim or Equity Interest, as the case may be, in each particular Class, is substantially similar to the other Claims or Equity Interests in such Class. Valid business, factual, and legal reasons exist for classifying the various Claims and Equity Interests created under the Plan and such Classes do not unfairly discriminate between holders of Claims and Equity Interests or prejudice the rights of holders of such Claims and Equity Interests. The classification of Claims and Equity Interests is reasonable and necessary to implement the Plan. The Plan adequately and properly classifies all Claims and Equity Interests and therefore satisfies the requirements of Bankruptcy Code sections 1122 and 1123(a)(1).

(2) <u>The Plan Specifies Unimpaired Classes, as Required by Section 1123(a)(2)</u>

Bankruptcy Code section 1123(a)(2) provides that "a plan shall … specify any class of claims or interests that is not impaired under the plan." Articles III.B.1 and 2 of the Plan identify Classes 1 and 2 as Unimpaired and specify the treatment of such Claims, thereby satisfying the requirements of Bankruptcy Code section 1123(a)(2).

(3) The Plan Specifies Impaired Classes, as Required by Section 1123(a)(3)

Bankruptcy Code section 1123(a)(3) provides that "a plan shall … specify the treatment of any class of claims or interests that is impaired under the plan." Articles III.B.3-8 of the Plan identify Classes 3-8 as Impaired and specify the treatment of such Claims, thereby satisfying the requirements of Bankruptcy Code section 1123(a)(3).

(4) The Plan Does Not Discriminate in a Manner Prohibited by Section 1123(a)(4)

Bankruptcy Code section 1123(a)(4) provides that "a plan shall … provide the same treatment for each claim or interests of a particular class, unless the holder of a particular claim or interest agrees to a less favorable treatment of such particular claim or interest." The Plan provides for the same treatment of each Claim against the Debtor in each respective Class unless the holder of a particular Claim has agreed to less favorable treatment on account of such Claim, thereby satisfying the requirements of Bankruptcy Code section 1123(a)(4).

(5) The Plan Provides Adequate Means for its Implementation, as Required by Section 1123(a)(5)

Bankruptcy Code section 1123(a)(5) provides that "a plan shall … provide adequate means for the plan's implementation." The Plan provides adequate and proper means for its implementation. Article IV of the Plan specifies provisions governing the means for implementing the Plan; Article V of the Plan specifies provisions governing the treatment of the Debtor's executory contracts and unexpired leases; Article VI of the Plan specifies provisions governing the distribution of Cash, New Common Stock, and Warrants pursuant to the Plan; and Article VII of the Plan specifies procedures for resolving contingent, unliquidated, and disputed Claims. Moreover, the Reorganized Debtor will have enough cash on the Effective Date to make all cash payments required to be made pursuant to the Plan. Accordingly, the Plan satisfies the requirements of Bankruptcy Code section 1123(a)(5).

(6) The Plan Provides for the Inclusion in the Debtor's New Certificate of Incorporation of a Provision Prohibiting the Issuance of Non-Voting Equity Securities, as Required by Section 1123(a)(6)

Bankruptcy Code section 1123(a)(6) provides that "a plan shall … provide for the inclusion in the charter of the debtor, if the debtor is a corporation … of a provision prohibiting the issuance of nonvoting equity securities." In accordance with Article IV.B of the Plan, Section 4.01 of the New Certificate of Incorporation does not permit the Reorganized Debtor to issue nonvoting equity securities, to the extent prohibited by Bankruptcy Code section 1123(a)(6), thereby satisfying the requirements of such section.

(7) The Plan's Provisions are Consistent With Public Policy With Respect to the Manner of Selection of any Officer or Director under the Plan and Any Successor to Such Officers and Directors, as Required by Section 1123(a)(7)

Bankruptcy Code section 1123(a)(7) provides that "a plan shall … contain only provisions that are consistent with the interests of creditors and equity security holders and with public policy with respect to the manner of selection of any officer, director, or trustee under the plan and any successor to such officer, director, or trustee." Article IV.K of the Plan sets forth provisions regarding the manner of selection of the New Board that are consistent with the interests of creditors, equity security holders, and public policy, in accordance with Bankruptcy Code section 1123(a)(7). As set forth in the Plan, the New Board shall consist of the Reorganized Debtor's Chief Executive Officer and four additional directors selected by the Informal Group and the Committee. Additionally, Article IV.K of the Plan provides that the Debtor's existing officers shall serve in their current capacities, subject to the ordinary rights and powers of the New Board to remove or replace them.

(8) The Plan Impairs or Leaves Unimpaired Classes of Claims and Equity Interests, as Permitted by Section 1123(b)(1)

Bankruptcy Code section 1123(b)(1) provides that "a plan may … impair or leave unimpaired any class of claims … or of interests." As noted above, Articles III.B.1 and 2 identify Classes 1 and Class 2 as Unimpaired and Articles III.B.3-8 identify Classes 3-8 as Impaired, as permitted by Bankruptcy Code section 1123(b)(1).

(9) The Plan Provides for the Assumption or Rejection of the Debtor's Executory Contracts and Unexpired Leases, as Permitted by Section 1123(b)(2)

Bankruptcy Code section 1123(b)(2) provides that "a plan may … subject to section 365 of this title, provide for the assumption, rejection, or assignment of any executory contract or unexpired lease of the debtor not previously rejected under such section." As permitted by Bankruptcy Code section 1123(b)(2), Article V.A of the Plan provides for the rejection of all of the Debtor's executory contracts and unexpired leases as of the Effective Date, except for any executory contract or unexpired lease that (i) was previously assumed or rejected by the Debtor, (ii) previously expired or terminated pursuant to its terms, (iii) is the subject of a motion to assume or reject filed on or before the Effective Date, or (iv) is identified on the Schedule of Assumed Executory Contracts and Unexpired Leases. Moreover, the Debtor has satisfied the provisions of Bankruptcy Code section 365 with respect to the assumption and rejection of executory contracts and unexpired leases pursuant to the Plan.

(10) The Amended Plan Settlement and the Plan's Injunction, Exculpation, and Release Provisions Should be Approved Pursuant to Bankruptcy Code Section 1123(b)(3)

Bankruptcy Code section 1123(b)(3) provides that "a plan may … provide for – (A) the settlement or adjustment of any claim or interest belonging to the debtor or to the estate; or (B) the retention and enforcement by the debtor, by the trustee, or by a representative of the estate

appointed for such purpose, of any claim or interest." The Plan is premised upon and includes an Amended Plan Settlement, and, in furtherance of the Amended Plan Settlement, seeks to implement injunction, exculpation, and release provisions. As described below, the Amended Plan Settlement and the Plan's injunction, exculpation, and release provisions are fair and equitable and are in the best interests of the Debtor and all parties in interest.

(i) The Amended Plan Settlement Should be Approved

The Plan is premised upon the Amended Plan Settlement. The Debtor pursued the Amended Plan Settlement to reach a consensual resolution of numerous litigable issues in the Debtor's Chapter 11 Case and emerge from bankruptcy as a reorganized company. Approval of the Amended Plan Settlement effectuates the primary policy objectives of chapter 11 by ensuring a "fresh start" for the Reorganized Debtor while treating the Debtor's stakeholders and other parties in interest, including OCI, AAC, and the Segregated Account, fairly. Set forth below is an explanation of the need for the Amended Plan Settlement, a description of its key terms, and a demonstration that the Amended Plan Settlement satisfies the *Iridium* factors used by courts in the Second Circuit to evaluate the appropriateness of proposed settlements.

(a) Formulation of the Global Settlement and the Key Terms of the Amended Plan Settlement

As described in the Disclosure Statement and the Ksenak Declaration, after evaluating the amount and nature of Claims against the Debtor and the sources of distributable value available, the Debtor, the Committee, OCI, Rehabilitator, the Informal Group, and their advisors concluded the only way for the Debtor to emerge from bankruptcy was through a global settlement. As a result, the Debtor engaged OCI in negotiations which ultimately resulted in the

Amended Plan Settlement. The following is a brief summary of the Amended Plan Settlement's key terms:[4]

- Maintenance of NOLs. As of September 30, 2010, the Debtor's consolidated tax group had NOLs of approximately $7.3 billion. Pursuant to the Amended Plan Settlement, the Reorganized Debtor will use its best efforts to preserve the use of Ambac's NOLs for the benefit of the AAC Subgroup, including, but not limited to refraining from taking any action that would result in and taking affirmative steps to avoid a Deconsolidation Event, *i.e.*, an event that would result in AAC not being a wholly-owned subsidiary of the Reorganized Debtor.

- Division of NOLs. Pursuant to the Amended Plan Settlement, the Debtor, AAC, and certain of their affiliates will enter into the Amended TSA. The Amended TSA allocates Ambac's NOLs in a manner agreeable to the Debtor, AAC, the Committee, and OCI.

- Cooperation Agreement Amendment. Pursuant to the Amended Plan Settlement, the Debtor, the Segregated Account, and OCI shall enter into an amendment, which is attached to the Plan as Exhibit B, to that certain Cooperation Agreement between the Segregated Account and AAC, dated as of March 24, 2010. The Cooperation Agreement Amendment affords the Rehabilitator the opportunity to participate in decisions concerning Ambac's future tax positions, the calculation of AAC's loss reserves, whether AAC may accept repayment of any intercompany loan in an amount in excess of $50 million per annum, and changes to AAC's investment policy.

- Cost Allocation Agreement. Pursuant to the Amended Plan Settlement, the Debtor, AAC, the Segregated Account, and OCI will enter into the Cost Allocation Agreement, which is attached to the Plan as Exhibit C. The Cost Allocation Agreement provides that AAC shall pay all of the Reorganized Debtor's reasonable operating expenses annually for five years, subject to a $5 million per annum cap. After five years, AAC shall pay all of the Reorganized Debtor's reasonable operating expenses in arrears, subject to a $4 million per annum cap and the Rehabilitator's approval. Pursuant to the Mediation Agreement, 85% of the reasonable litigation fees and expenses incurred by the Debtor in the IRS Dispute shall be allocated to AAC and 15% shall be allocated to the Debtor.

[4] The following summary of the Amended Plan Settlement is qualified in its entirety by the actual terms of the Amended Plan Settlement. To the extent this summary is inconsistent with the Amended Plan Settlement, the terms of the Amended Plan Settlement shall control in all respects.

- $30 Million Cash Grant, Junior Surplus Notes, and Tolling Payments. Pursuant to the Amended Plan Settlement, AAC shall transfer a $30 million Cash Grant to the Reorganized Debtor, the Segregated Account shall issue $350 million of Junior Surplus Notes to the Reorganized Debtor, and the Debtor expects to receive significant tolling payments from AAC for future use of NOLs (the "Tolling Payments").

- Injunction, Exculpation, and Release Provisions. In accordance with the Mediation Agreement, the Plan includes specified injunction, exculpation, and release provisions, as described in greater detail below.

The settlement process was driven by the fact that the Debtor could not successfully reorganize absent support from OCI. As noted above, OCI serves as AAC's regulator and as Rehabilitator of the Segregated Account. Accordingly, OCI approval is required for AAC or the Segregated Account to enter into any agreement with or make any payment to the Reorganized Debtor. Because the Debtor is a holding company, the Debtor has no real source of income other than payments from affiliates. Thus, without OCI support, the Reorganized Debtor could not enter into the Amended TSA, AAC would not be permitted to pay $30 million in Cash and the Segregated Account would not be permitted to issue $350 million in Junior Surplus Notes to the Reorganized Debtor, the Debtor would not receive any Tolling Payments, and AAC would not be permitted to pay the Reorganized Debtor's operating expenses on an ongoing basis. In practical terms, OCI, through AAC and the Segregated Account, is funding the Plan. In exchange, the Reorganized Debtor will maintain Ambac's NOLs, AAC will be entitled to benefit from Ambac's NOLs pursuant to the Amended TSA, and the parties agreed to the injunction, exculpation, and release provisions set forth in the Plan.

(b) The Amended Plan Settlement Satisfies the *Iridium* Factors

When evaluating plan settlements pursuant to Bankruptcy Code section 1123(b), courts in the Second Circuit consider the standards used in evaluating settlements under Bankruptcy Rule

9019, *i.e.*, the settlement must be "fair and equitable" and in the best interests of the estate.[5] In *In re Iridium Operating LLC*, the Second Circuit set forth the following list of factors for courts to consider in evaluating whether a settlement satisfies such standards:

> (1) the balance between the litigation's possibility of success and the settlement's future benefits; (2) the likelihood of complex and protracted litigation, "with its attendant expense, inconvenience, and delay," including the difficulty in collecting on the judgment; (3) "the paramount interests of the creditors," including each affected class's relative benefits "and the degree to which creditors either do not object to or affirmatively support the proposed settlement;" (4) whether other parties in interest support the settlement; (5) the "competency and experience of counsel" supporting, and "[t]he experience and knowledge of the bankruptcy court judge" reviewing, the settlement; (6) "the nature and breadth of releases to be obtained by officers and directors"; and (7) "the extent to which the settlement is the product of arm's length bargaining."

478 F.3d 452, 462 (2d Cir. 2007) (citing *In re WorldCom, Inc.*, 347 B.R. 123, 137 (Bankr. S.D.N.Y. 2006)). *See also In re Adelphia Commc'ns Corp.*, 368 B.R. 140, 226 (Bankr. S.D.N.Y. 2007) (quoting *In re Texaco Inc.*, 84 B.R. 893, 902 (Bankr. S.D.N.Y. 1988), stating a similar list of seven factors). Application of the foregoing factors to the Amended Plan Settlement confirms that it is fair and equitable and in the best interests of the Debtor and its estate and should be approved.

The Benefits of the Amended Plan Settlement Outweigh the Benefits of Litigating the Issues Resolved by the Same. The Amended Plan Settlement confers substantial benefits on the Debtor. Under the Amended Plan Settlement, the Debtor can benefit from Ambac's NOLs, the Debtor will receive $30 million in Cash, $350 million in Junior Surplus Notes, and Tolling

[5] *See Protective Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson,* 390 U.S. 414, 424 (1968); *In re Best Prods. Co.,* 168 B.R. 35, 50 (Bankr. S.D.N.Y. 1994) ("whether the claim is compromised as part of the plan or pursuant to a separate motion, the standards for approval of the compromise are the same. The settlement must be 'fair and equitable' … and be in the best interest of the estate").

Payments, and AAC will pay a significant portion of the Debtor's operating expenses on an ongoing basis. In light of the benefits of the Amended Plan Settlement, litigating any preference or fraudulent conveyance claims pertaining to the Debtor's prepetition transfer of tax refunds or pursuing claims against and seeking discovery from any of the Released Parties would be counterproductive. Even if the Debtor were ultimately successful in litigating such issues, which is uncertain, delaying confirmation and consummation of the Plan could jeopardize the Debtor's reorganization as the Debtor does not have enough liquidity to sustain a delay in confirmation of the Plan of more than several months. Moreover, the cost of litigating the issues resolved by the Amended Plan Settlement would compound the Debtor's liquidity problems by adding millions of dollars in legal fees and expenses at the Bankruptcy Court level, with the possibility of extended appeals. Even absent the Debtor's liquidity problems, pursuing a strategy of litigating the issues resolved by the Amended Plan Settlement to a conclusion could upset the delicate state of the Debtor's relationships with the Committee, AAC, OCI, and the Rehabilitator, all of whose support is essential to confirm the Plan. And of course, if the Debtor were unsuccessful in litigating such issues, the Debtor's estate would lose the significant value delivered to creditors under the Plan and the Debtor may need to convert its case to one under chapter 7 of the Bankruptcy Code.

Litigation of the Issues Resolved by the Amended Plan Settlement Would be Complex, Protracted, and Expensive. Fully litigating the issues resolved by the Amended Plan Settlement would require the Bankruptcy Court and any appeals court to consider, among other things, whether the Debtor's prepetition transfer of tax refunds to AAC constitutes an avoidable fraudulent or preferential transfer and whether and the extent to which the Debtor has valid claims against any of the Released Parties. To date, no discovery has been conducted in

connection with the foregoing issues and any discovery would likely be complex, protracted, and expensive, without even accounting for the logistics of fully litigating such issues. Further, there can be no assurance that the estate would be able to fund such litigation, given that the Debtor's primary source of income is payments from AAC and AAC would very likely not make such payments if the Debtor or the Committee commenced an action against it. Additionally, absent approval of the Amended Plan Settlement, given the amounts at stake, the Bankruptcy Court's decision in any such avoidance action may be appealed regardless of the outcome.

The Amended Plan Settlement is in the Paramount Interests of Creditors. Confirmation of the Plan and approval of the Amended Plan Settlement would provide significant benefits to the Debtor, its estate, and its creditors. Confirmation of the Plan and approval of the Amended Plan Settlement would result in an immediate improvement to the Debtor's liquidity while also enabling the Debtor to successfully emerge from bankruptcy, and further, would benefit the Debtor's creditors by avoiding the fees and expenses associated with engaging in costly litigation.

The Amended Plan Settlement is Supported by All Key Parties in Interest. Approval of the Amended Plan Settlement and confirmation of the Plan is supported by, among others, the Debtor, the Committee, AAC, OCI, the Rehabilitator, and the Informal Group. Moreover, as evidenced by the Vote Certification, the Debtor's creditors eligible to vote to accept or reject the Plan overwhelmingly support the Amended Plan Settlement.

The Amended Plan Settlement is the Product of Arm's Length Bargaining Among Parties with Experienced and Independent Counsel. As set forth in the Disclosure Statement and the Ksenak Declaration, the Amended Plan Settlement is the product of extensive and protracted arm's length negotiations and was developed and negotiated with the aid of knowledgeable and

competent counsel. Moreover, all parties involved in the negotiation of the Amended Plan Settlement support confirmation of the Plan.

The Injunction, Exculpation, and Release Provisions of the Plan, Which Form an Integral Part of the Amended Plan Settlement, are Proper. The injunction, exculpation, and release provisions of the Plan form an integral part of the Amended Plan Settlement and should be approved for reasons described in the following section.

(ii) The Injunction, Exculpation, and Release Provisions of the Plan Should be Approved

(a) Injunction

Article VIII.B of the Plan (the "Injunction") enjoins Entities that have held, hold, or may hold Claims against, Claims that may result in reimbursement, contribution, or indemnification by the Debtor on account of such Claims (including the ERISA Claims at issue in the ERISA Action), or Equity Interests in the Debtor or the Estate from taking certain actions against the Debtor, the Reorganized Debtor, or the Estate, subject to the proviso that AAC may exercise setoff rights pursuant to the Cost Allocation Agreement. The Injunction is necessary to effectuate the Plan and to protect the Reorganized Debtor from any potential litigation as it implements the Plan following the Effective Date. Any such litigation would hinder the Reorganized Debtor's efforts to effectively fulfill its responsibilities as contemplated by the Plan. To enable the Reorganized Debtor to successfully comply with its obligations under the Plan, the Debtor respectfully requests that the Bankruptcy Court approve the Injunction.

(b) Consensual Release

Article I.A.19.(ix) of the Plan (the "Consensual Release") provides that effective as of the Plan Settlement Closing Date, *i.e.*, the date on which the conditions to consummation of the

Amended Plan Settlement have been waived or satisfied, the "AFGI Interests," *i.e.*, the Debtor and the members of the Committee,

> shall provide an unconditional, full, and complete release of OCI, the Rehabilitator, AAC, and the Segregated Account, and each of their respective current and former members, shareholders, affiliates, officers, directors, employees, and agents … from any and all claims or causes of action of any nature whatsoever that the AFGI Interests … ever had, now has or can, shall, or may have, by reason of any matter … occurring prior to the Plan Settlement Closing Date

and AAC, OCI, the Segregated Account, and the Rehabilitator

> shall provide an unconditional, full, and complete release of the Debtor and the members of the Committee, and each of their current and former members, shareholders, affiliates, officers, directors, employees, and agents … from … any and all claims or causes of action of any nature whatsoever that such parties … ever had, now has or can, shall or may have, by reason of any matter … occurring prior to the Plan Settlement Closing Date.

Each of the Debtor, the Committee, its members, OCI, the Rehabilitator, AAC, and the Segregated Account have agreed to the foregoing Consensual Release, and further, courts routinely allow voluntary third-party releases to be included in a chapter 11 plan.[6] Accordingly, the Debtor respectfully requests that the Bankruptcy Court approve the Consensual Release.

(c) Debtor's General Release

Article VIII.D of the Plan (the "Debtor's General Release") provides that "on and after the Effective Date, the Released Parties shall be released and discharged by the Debtor … from

[6] *See, e.g.*, *Deutsche Bank AG, London Branch v. Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.)* 416 F.3d 136, 142 (2d Cir. 2005) (citing *In re Specialty Equip. Cos.*, 3 F.3d 1043, 1047 (7th Cir. 1993)) ("Nondebtor releases may also be tolerated if the affected creditors consent"); *In re DBSD N. Am., Inc.*, 419 B.R. 179, 218-219 (Bankr. S.D.N.Y. 2009), *aff'd*, No. 09-13061, 2010 WL 1223109 (S.D.N.Y. Mar. 24, 2010), *rev'd on other grounds*, 627 F.3d 496 (2d Cir. 2010) (finding third party release provisions "consensual and within the scope of releases permitted in the Second Circuit"); *Adelphia*, 368 B.R. at 268 (citing *Specialty Equip.*, 3 F.3d at 1047; *Deutsche Bank AG, London Branch v. Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.),* 416 F.3d 136, 142 (2d Cir. 2005)) ("The Seventh Circuit held in *Specialty Equipment* that consensual releases are permissible, and the *Metromedia* court did not quarrel with that view").

any and all Claims and Causes of Action of any nature whatsoever,"[7] subject to the proviso that such release does not apply to (i) bankruptcy crimes or claims arising under agreements entered into in connection with the Amended Plan Settlement, or (ii) any claims arising out of or relating to the Securities Actions (rather, such claims may be released under the Stipulation of Settlement once the Stipulation of Settlement becomes effective and the Stipulation of Settlement 9019 Approval Order becomes a Final Order).

Bankruptcy Code section 1123(b)(3)(A) provides that "a plan may … provide for … the settlement or adjustment of any claim or interest belonging to the debtor or to the estate." Consistent with this, numerous courts have permitted debtors to release claims under a plan provided the grant of such release is a valid exercise of its business judgment.[8] The Debtor's General Release is in the best interests of the Estate and well within the Debtor's business judgment because the Debtor's General Release is an integral part of the negotiated Plan, and the Debtor has considered the value of Claims and Causes of Action against the Released Parties and determined that pursuing such Claims and Causes of Action would not provide sufficient benefit to the Estate considering the likelihood of success on the merits and the cost, expense, and delay

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[7] Article I.A.115 of the Plan defines "Released Parties" as follows:

> [T]he 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).

[8] *See*, *e.g.*, *In re Motors Liquidation Co.*, 447 B.R. 198, 220 (Bankr. S.D.N.Y. 2011) ("Releases by estates involve a give-up of potential rights that are owned by the estate, and are perfectly permissible in a plan, either as parts of plan settlements or otherwise, though the court must satisfy itself (at least if anyone raises the issue) that the give-up is an appropriate exercise of business judgment"); *JPMorgan Chase Bank, N.A. v. Charter Commc'ns Operating, LLC (In re Charter Commc'ns)*, 419 B.R. 221, 257 (Bankr. S.D.N.Y. 2009) ("Debtors are authorized to settle or release their claims in a chapter 11 plan"); *Adelphia*, 368 B.R. at 268 n.289 ("The Debtors have considerable leeway in issuing releases of any claims the Debtors themselves own"); *In re Oneida Ltd.,* 351 B.R. 79, 94 (Bankr. S.D.N.Y. 2006) (noting that a debtor's release of its own claims is permissible).

required to prosecute such Claims or Causes of Action. In particular, the Debtor and the Committee have evaluated potential avoidance actions and/or constructive trust claims the Debtor may have against AAC and any liability AAC may have to the Debtor pertaining to any possible misallocation of up to approximately $38.5 million in tax refunds received by AAC in September of 2009 and February of 2010.

The Debtor believes in its sound business judgment that its Estate is best served by releasing the foregoing potential Causes of Action and all other Causes of Action against the Released Parties in order to attain the tremendous value delivered to holders of Claims under the Plan. Accordingly, the Debtor respectfully requests that the Bankruptcy Court approve the Debtor's General Release.

(d) Holders' General Release

Article VIII.E of the Plan (the "Holders' General Release") provides that "[e]xcept as otherwise provided in Article VIII.H of the Plan [relating to a carve-out from the discharge, injunction, exculpation, and release provisions for the United States] 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 … shall be deemed to have … released and discharged the Released Parties from any and all Claims and Causes of Action of any nature whatsoever … based upon or relating to any act [or] omission … taking place on or prior to the Effective Date and based upon or relating to the Debtor, the Estate, the Reorganized Debtor, [or] the Chapter 11 Case," subject to the proviso that (i) such Holders' General Release does not apply to (a) bankruptcy crimes, (b) claims policyholders or securities holders may have against AAC or the Segregated Account pursuant to their respective policies or securities, (c) the reorganized Debtor's obligations under the Plan or agreements entered into in connection with the Amended Plan Settlement, or (d) any claims

arising out of or relating to the Securities Actions (rather, such claims may be released under the Stipulation of Settlement once the Stipulation of Settlement becomes effective and the Stipulation of Settlement 9019 Approval Order becomes a Final Order); and (ii) One State Street, LLC shall remain entitled to the benefits of its settlement agreement with the Debtor, AAC, and the Segregated Account, approved by the Bankruptcy Court on March 24, 2011 [Docket No. 223].

Although the Holders' General Release is a nonconsensual third party release, it should nevertheless be approved. In *SEC v. Drexel Burnham Lambert Group, Inc. (In re Drexel Burnham Lambert Group, Inc.)*, the Second Circuit held that "a court may enjoin a creditor from suing a third party, provided the injunction plays an important part in the debtors' reorganization plan." 960 F.2d 285, 293 (2d Cir. 1992). The Second Circuit further held in *Metromedia* that "[w]hile none of our cases explains when a nondebtor release is 'important' to a debtor's plan … such a release is proper only in rare cases" where "unusual circumstances render the release important to the success of the plan." 416 F.3d at 141, 143. The *Metromedia* court noted that the determination of whether a nonconsensual third party release is sufficiently important and that unusual circumstances justify the approval of such release "is not a matter of factors and prongs," *Id.* at 142, but did provide a non-exhaustive list of instances where nonconsensual third party releases may be appropriate, including where "the estate received substantial consideration" or "the enjoined claims would indirectly impact the debtor's reorganization 'by way of indemnity or contribution.'" *Id.* (citations omitted).

Bankruptcy Court approval of the Holders' General Release is permissible under applicable law and should be approved. The unique circumstances of the Chapter 11 Case renders the Holders' General Release critical to the Plan's success, the Debtor is unquestionably

receiving substantial consideration in exchange for such release, an identity of interests exists between the Debtor and certain of the Released Parties, and other factors weigh in favor of approving such provisions.

Unique Circumstances of the Chapter 11 Case Justify the Holders' General Release. OCI, which, as noted above, is effectively funding the Plan by authorizing AAC to transfer to the Debtor a $30 million Cash Grant and pay the Reorganized Debtor's reasonable operating expenses for five years (subject to a $5 million cap per annum), authorizing the Segregated Account to issue $350 million of Junior Surplus Notes to the Debtor, and authorizing the Debtor to receive Tolling Payments, required, as a condition of such settlement, that the Plan include the Holders' General Release and the definition for "Released Parties" set forth in the Plan. *See* Mediation Agreement, dated as of September 21, 2011, among the Debtor, AAC, the Segregated Account, the Rehabilitator, OCI, and the Committee, attached to the Disclosure Statement as Exhibit B at § 15 (providing that "releases shall be as set forth in the Bankruptcy Plan").

OCI negotiated for and demanded such broad release provisions for several reasons, as described in the Ksenak Declaration. First, OCI, in its capacities as AAC's regulator and Rehabilitator of the Segregated Account, does not want AAC or its directors, officers, or employees to become bogged down in actions against Released Parties relating to acts or omissions occurring prior to the Effective Date and relating in any manner to the Debtor or its restructuring initiatives. Complying with non-party discovery demands in any one such action would be complex, protracted, and expensive and will require the applicable Released Parties and their respective counsel to expend many hours of preparation time in connection with any depositions taken and the review of what may be millions of pages of documents.

Second, as noted in the Ksenak Declaration, OCI has been involved in Ambac's restructuring initiatives since September 2008. Accordingly, any action against a Released Party relating to Ambac's restructuring or the circumstances and events surrounding such restructuring, in addition to distracting AAC and its directors, officers, and employees, will very likely distract OCI and its employees and representatives as well, given OCI's involvement in Ambac's affairs generally since 2008. In this manner, OCI, in its capacities as AAC's regulator and the Segregated Account's Rehabilitator, may be required to produce many documents and/or have its employees or representatives provide deposition testimony in connection with an action against one or more Released Parties relating to the Debtor or its restructuring initiatives.

Third, substantial overlap exists between the Debtor's current and former directors, officers, and employees, and AAC's current and former directors, officers, and employees. Accordingly, OCI wanted a release for AAC's current and former directors, officers, and employees to the extent any of the Debtor's current and former directors, officers, and employees are being released pursuant to the Plan, in order to avoid any litigation over whether an AAC current or former director, officer, or employee was acting in his or her capacity as such in connection with a particular act or omission that is the subject of a post-Effective Date action, and therefore falls within the scope of any release for the Debtor's current and former directors, officers, and employees.

OCI was in a position to negotiate for the Plan's injunction, exculpation, and release provisions because, in accordance with the Mediation Agreement and with OCI's approval, AAC and the Segregated Account will be funding the Plan. As noted above, pursuant to the Amended Plan Settlement, (i) AAC will transfer to the Debtor a $30 million Cash Grant, (ii) the Segregated Account will issue to the Debtor $350 million in junior surplus notes, (iii) AAC will pay the

reasonable operating expenses of the Debtor or the Reorganized Debtor for five years, subject to a $5 million cap per year, as well as 85% of the costs of the IRS Dispute, and (iv) the Debtor expects to receive Tolling Payments from AAC.

The Released Parties Furnished Substantial Consideration in Exchange for the Holders' General Release. As noted above and in the Ksenak Declaration, OCI, the Rehabilitator, AAC, and the Segregated Account are effectively funding the Plan and are therefore furnishing substantial consideration in exchange for the Holders' General Release. Additionally, the Committee, its members, the Indenture Trustees, and many of the released directors, officers, and employees of the Debtor and AAC provided substantial consideration by participating in the negotiations that enabled the parties to reach the Amended Plan Settlement and formulate the Plan. The support of each of the foregoing parties was necessary to enter into the Mediation Agreement, the Amended TSA, the Cooperation Agreement Amendment, and the Cost Allocation Agreement and for the Reorganized Debtor to receive the Cash Grant, Junior Surplus Notes, operating expense support, and Tolling Payments.

An Identity of Interests Exists Between the Debtor and Certain of the Released Parties. Pursuant to section 145 of the Delaware General Corporation Law, Article VII of the Debtor's certificate of incorporation, and Article IX of the Debtor's by-laws,[9] the Debtor's current and former directors and officers, many of whom are or were directors and/or officers of AAC, have broad common law, statutory, and contractual rights of indemnification from the Debtor. In this manner, any causes of action against the Debtor's or AAC's current or former directors or

[9] Copies of the Debtor's certificate of incorporation and by-laws are attached as exhibits 1 and 3, respectively, to the Declaration of Kevin J. Doyle, attached as Exhibit A to the Debtor's motion for summary judgment in its adversary proceeding against Karthikeyan V. Veera, Adv. Pro. No. 11-01265 [Docket No. 5].

officers may be considered actions against the Debtor's estate.[10] Additionally, as noted in the Ksenak Declaration, the Debtor would be in a position to purchase significantly less tail insurance coverage in connection with its emergence from bankruptcy as a result of the Plan's injunction, exculpation, and release provisions. Further, complying with non-party discovery demands in any one action against Released Parties relating to acts or omissions occurring prior to the Effective Date and relating to the Debtor or its restructuring initiatives would be complex, protracted, and expensive and will require the Debtor and its counsel to expend many hours of preparation time in connection with any depositions taken and the review of what may be millions of pages of documents.

Other Factors Weigh in Favor of Approving the Holders' General Release. The Plan has been overwhelmingly accepted by creditors entitled to vote to accept or reject the Plan. Additionally, the Holders' General Release is fair, equitable, and reasonable. It is the product of good faith and arm's length negotiations in connection with the settlements that are the foundation of the Plan. Because of the Amended Plan Settlement, the Plan provides adequate funding to enable the Reorganized Debtor to fund its post-bankruptcy obligations and ensures a fresh start for the Reorganized Debtor. Such provision is reasonable and consistent with public policy because it protects the integrity of the Plan, insulates the Debtor, the Reorganized Debtor, and the Estate from indirect liability, and includes appropriate carve-outs.

(e) Stipulation of Settlement Release

As set forth in greater detail in the Disclosure Statement, the lead plaintiffs in certain Securities Actions, the Debtor, and the Individual Defendants in such actions entered into a

[10] *See*, *e.g.*, *Charter*, 419 B.R. at 259 ("The indemnification obligations between the Debtors and their directors, officers, agents, and professionals produce an identity of interests between the Debtor and the CII Settlement Claim Parties … This identity of interests supports approving the Third Party Releases"); *Adelphia*, 368 B.R. at 268 ("To the extent that the third party releases are congruent with the indemnification obligations, and the Debtor would be liable for any liability imposed on such persons, third-party releases are acceptable").

Stipulation of Settlement which is intended to, among other things, finally resolve any and all Claims and Causes of Action that were, could have been, or may have been asserted in any of the Securities or Derivative Actions.

Paragraph 35(f) of the Stipulation of Settlement provides that a condition to its effectiveness is entry of an order pursuant to Bankruptcy Rule 9019 or entry of a Confirmation Order approving the releases set forth in Article VIII.F of the Plan (the "Stipulation of Settlement Release"). The Stipulation of Settlement Release provides that "[t]o the fullest extent permitted by applicable law, on the Effective Date," "all Persons or Entities" and "the Debtor, on behalf of itself and (to the fullest extent of its power to do so) all Ambac Entities"

> shall be permanently barred and enjoined from … prosecuting … any and all … Claims … [and] … Causes of Action … against any or all of the Individual Defendants and any and all of the current or former officers, directors, or employees of any Ambac Entity (i) that were, could have been … or might be in the future asserted in any of the Securities … or … Derivative Actions; (ii) in connection with … any action or omission … within the Class Period [defined, with respect to the Securities Actions, as October 19, 2005 through July 18, 2009] or relevant periods specified in any of the Derivative Actions by … any of the current or former officers, directors, or employees of any Ambac Entity relating to any Ambac Entity or in his or her capacity as an officer, director, or employee … or (iii) that … are based upon … any … action, [or] omission … alleged in any of the Securities … or … Derivative Actions or related to any … action, [or] omission alleged in any of the Securities … or … Derivative Actions,

subject to the proviso that such release provision does not apply to ERISA claims asserted by Karthikeyan V. Veera ("Veera"), as plaintiff in a putative class action entitled *Veera v. Ambac Plan Administrative Committee, et al.*, No. 10-cv-4191 (the "Veera Action").

As the Bankruptcy Court is aware, the Police and Fire Retirement System of the City of Detroit (the "PFRS") appealed the Bankruptcy Court's amended order, dated September 13, 2011, approving the Stipulation of Settlement, the Debtor's entry into such stipulation, and the

performance of all of the Debtor's obligations thereunder [Docket No. 558] (the "Stipulation of Settlement 9019 Approval Order"). *See also* Bench Decision Approving Stipulation of Settlement and Insurer Agreement, dated September 23, 2011 [Docket No. 582]. Further, on December 29, 2011, the District Court entered a memorandum and order affirming the Bankruptcy Court's decision regarding the Stipulation of Settlement 9019 Approval Order, *see* Case No. 11-cv-07529 [District Court Docket No. 14], and January 4, 2011, the PFRS appealed the District Court's decision to the Second Circuit [District Court Docket No. 17]. The Stipulation of Settlement 9019 Approval Order explicitly approved the Stipulation of Settlement Release, which has been re-stated in the Plan and Confirmation Order.

The District Court has approved the Stipulation of Settlement as well. *See In re Ambac Financial Group, Inc. Securities Litigation*, Case No. 08-cv-00411 (NRB) (S.D.N.Y. Sept. 28, 2011) [District Court Docket Nos. 143, 145, and 146]. As with the Stipulation of Settlement 9019 Approval Order, the PFRS has appealed the foregoing District Court orders approving the Stipulation of Settlement. *See In re Ambac Financial Group, Inc. Securities Litigation*, Case No. 08-cv-00411 (NRB) (S.D.N.Y. Sept. 28, 2011) [District Court Docket No. 153].

Even absent the prior approvals of the Stipulation of Settlement Release by the Bankruptcy and District Courts (in the Stipulation of Settlement 9019 Approval Order and the above-referenced District Court orders, respectively), Bankruptcy Court approval of the Stipulation of Settlement Release is permissible under applicable law and should be approved for the same reason as the Holders' General Release. Specifically, to the extent that the Stipulation of Settlement Release is a nonconsensual third party release, unique circumstances justify such release, as it was specifically negotiated for by the settling insurers as a condition for entering into the Stipulation of Settlement and such insurers are paying $24.6 million pursuant to the

Stipulation of Settlement to resolve Claims and Causes of Action potentially assertable in the Securities and Derivative Actions. In addition, as with the Holders' General Release, an identity of interests exists between the Debtor and many of the released directors and officers and other factors weigh in favor of approving the Stipulation of Settlement Release.

(f) Exculpation

Article VIII.C of the Plan (the "Exculpation") provides that "[e]xcept as otherwise provided in Article VIII.H of the Plan [relating to a carve-out from the discharge, injunction, exculpation, and release provisions for the United States], none of the Released Parties shall have or incur any liability to any holder of any Claim or Equity Interest for any act or omission in connection with … the Debtor's restructuring," subject to the proviso that such Exculpation does not apply to acts which constitute bankruptcy crimes, fraud, gross negligence, willful misconduct, or misuse of confidential information.

The Exculpation provision is consistent with established Second Circuit precedent and should be approved. Courts evaluate the appropriateness of exculpation provisions based on a number of factors, including whether the Plan was proposed in good faith, whether liability is limited, and whether such provision was necessary for plan negotiations.[11] As noted above, the Bankruptcy Court must find, among other things, that the Plan has been proposed in good faith and not by any means forbidden by law pursuant to Bankruptcy Code section 1129(a)(3). Such a finding would extend to the parties involved in the formulation of the Plan, *i.e.*, the Debtor,

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[11] *See*, *e.g.*, *Oneida*, 351 B.R. at 94 n.22 (approving exculpation provision that covered prepetition lenders, DIP lenders, statutory committees and their members, and the respective affiliates of each over an objection and noting that the language "generally follows the text that has become standard in this district … [and] is sufficiently narrow to be unexceptional"); *Upstream Energy Servs. v. Enron Corp. (In re Enron Corp.)*, 326 B.R. 497, 501, 503 (S.D.N.Y. 2005) (approving an exculpation provision where it was necessary to effectuate the plan and excluded gross negligence and willful misconduct); *Captran Creditors' Trust v. McConnell* (*In re Captran Creditors' Trust),* 128 B.R. 469, 476 (M.D. Fla. 1991) (factors used to evaluate the language of an exculpation provision "include, but are not limited to: how the exculpatory clause limits liability, intent of the parties, and the manner in which the exculpatory clause was made a part of the agreement").

AAC, the Segregated Account, OCI, the Rehabilitator, the Committee and the individual members thereof, and the Informal Group and the individual members thereof. Thus, if the Bankruptcy Court confirms the Plan, cause exists to approve the Exculpation provision. Moreover, it is well established that the liability of statutory committees and their professionals is limited to acts or omissions constituting fraud, gross negligence, or willful misconduct.[12] Further, exculpation for participating in the Plan formulation process is appropriate where negotiations could not have occurred without protection from liability.[13] The Plan would not have materialized if the negotiating parties were not assured they would be protected from liability, other than for fraud, gross negligence, or willful misconduct. Finally, policy considerations weigh heavily in favor of approving the Exculpation provision. Failing to include such provision would chill the critical participation of key creditor groups in the process of trying to formulate and negotiate a consensual Plan. In light of the bankruptcy policy in favor of consensual chapter 11 plans and the negotiations that create them, it stands to reason that exculpation provisions are essential to the process, and thus, the Plan's Exculpation provision should be approved.[14]

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[12] *See In re Calpine Corp.,* No. 05-60200, 2007 WL 4565223, at *10 (Bankr. S.D.N.Y. Dec. 19, 2007) (finding exculpation provisions not relieving any party of liability for gross negligence or willful misconduct finding to be appropriate); *Enron Corp.,* 326 B.R. at 501 (noting that the bankruptcy court had addressed the exculpation provision, finding it appropriate because it excluded gross negligence and willful misconduct); *In re PWS Holding Corp.,* 228 F.3d 224, 246-47 (3d Cir. 2000) (holding that the appropriate standard of liability of a committee under Bankruptcy Code section 1103(c) is "willful misconduct or *ultra vires* acts," and approving an exculpation of the committee and its professionals subject only to liability for willful misconduct or gross negligence).

[13] *See Enron Corp.,* 326 B.R. at 503 (excising similar exculpation provisions would "tend to unravel the entire fabric of the Plan, and would be inequitable to all those who participated in good faith to bring it into fruition"); *In re Winn-Dixie Stores, Inc.,* 356 B.R. 239, 261 (Bankr. M.D. Fla. 2006) (holding exculpation provision appropriate where beneficiaries expected such provision to be included in chapter 11 plan in exchange for participation in the chapter 11 cases); *WorldCom,* 2003 WL 23861928, at *28 (finding exculpation provision appropriate where its inclusion in the plan was vital to the plan's successful negotiation).

[14] *See In re Homestead Partners, Ltd.,* 197 B.R. 706, 710 (Bankr. N.D. Ga. 1996) ("the development of consensual reorganizations lies at the heart of Chapter 11 policy"); *In re Pub. Serv. Co.,* 88 B.R. 521, 539-40 (Bankr. D.N.H. 1988) ("it is a 'strong policy' underlying chapter 11 of the Bankruptcy Code to foster consensual plans"); *In re Jartran, Inc.,* 44 B.R. 331, 363 (Bankr. N.D. Ill. 1984) ("the spirit of Chapter 11 [is] to promote consensual plans").

(11) The Plan Provides for the Cure of Defaults in Accordance With Bankruptcy Code Section 1123(d)

Bankruptcy Code section 1123(d) provides that "if it is proposed in a plan to cure a default the amount necessary to cure the default shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law." Article V.B of the Plan provides for the satisfaction of default Claims associated with each executory contract and unexpired lease to be assumed pursuant to the Plan in accordance with Bankruptcy Code section 365(b)(1). The Cure Claims identified in the Schedule of Assumed Executory Contracts and Leases represent the amount, if any, the Debtor proposes to pay in full and complete satisfaction of such default Claims. Any disputed Cure Claim amount will be determined in accordance with the underlying agreements and applicable law. Accordingly, the Plan complies with Bankruptcy Code section 1123(d).

B. Section 1129(a)(2): The Debtor, as Plan Proponent, has Complied With All Applicable Provisions of the Bankruptcy Code

Section 1129(a)(2) of the Bankruptcy Code requires that the proponent of a chapter 11 plan comply with the applicable provisions of the Bankruptcy Code. The legislative history of Bankruptcy Code section 1129(a)(2) reflects that this provision is intended to encompass the disclosure and solicitation requirements set forth in Bankruptcy Code section 1125 of the Bankruptcy Code and the plan acceptance requirements set forth in Bankruptcy Code section 1126.[15]

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[15] *In re Johns-Manville Corp.,* 68 B.R. 618, 630 (Bankr. S.D.N.Y. 1986), *aff'd in part, rev'd in part on other grounds,* 78 B.R. 407 (S.D.N.Y. 1987), *aff'd*, 843 F.2d at 636 (citations omitted) ("Objections to confirmation raised under § 1129(a)(2) generally involve the alleged failure of the plan proponent to comply with § 1125 and § 1126 of the Code"); *In re Toy & Sports Warehouse, Inc.,* 37 B.R. 141, 149 (Bankr. S.D.N.Y. 1984) (to comply with Bankruptcy Code section 1129(a)(2), "the proponent must comply with the ban on post-petition solicitation of the plan unaccompanied by a written disclosure statement approved by the court in accordance with Code §§ 1125 and 1126"); *see also* H.R. Rep. No. 95-595, at 412 (1977); S. Rep. No. 95-989, at 126 (1978) ("Paragraph (2) [of Bankruptcy Code section 1129(a)] requires that the proponent of the plan comply with the applicable provisions of chapter 11, such as section 1125 regarding disclosure").

The Debtor has complied with the disclosure and solicitation requirements of Bankruptcy Code section 1125. Bankruptcy Code section 1125(b) prohibits the solicitation of votes to accept or reject a plan "unless, at the time of or before such solicitation, there is transmitted to such holder the plan or a summary of the plan, and a written disclosure statement approved, after notice and a hearing, by the court as containing adequate information." The purpose of this section is to ensure that parties in interest are fully informed regarding the condition of the debtor, the means for implementation of the plan, and the treatment of classes of claims and interests, such that they may make an informed decision whether to vote to accept or reject the plan.[16] Before the Debtor began soliciting votes to accept or reject the Plan, the Bankruptcy Court entered the Disclosure Statement Order, which, among other things, approved the Disclosure Statement as containing adequate information and procedures for soliciting and tabulating votes to accept or reject or object to the Plan. The Disclosure Statement Order specifies the solicitation materials the Debtor was required to provide and has provided to holders of Claims and Equity Interests and the timing and method of delivery of such materials. As detailed in the Vote Certification, the Debtor, through its Voting Agent, Kurtzman Carson Consultants LLC, has complied in all respects with the content and delivery requirements set forth in the Disclosure Statement Order.

Further, the Debtor has complied with Bankruptcy Code section 1126. Bankruptcy Code section 1126 provides that only holders of allowed claims and equity interests in impaired classes that will receive or retain property under a plan on account of such claims or equity interests may vote to accept or reject a plan. Under the Plan, Classes 1 and 2 are Unimpaired, and thus,

[16] *See Momentum Mfg. Corp. v. Employee Creditors Comm.* (*In re Momentum Mfg. Corp.*), 25 F.3d 1132, 1136 (2d Cir. 1994) (finding that Bankruptcy Code section 1125 obliges a Debtor to engage in full and fair disclosure that would enable a hypothetical reasonable investor to make an informed judgment about the plan).

pursuant to Bankruptcy Code section 1126(f), holders of Claims in such classes are conclusively presumed to have accepted the Plan and were not entitled to vote to accept or reject the Plan. Classes 6, 7, and 8 are not receiving a distribution under the Plan, and thus, pursuant to Bankruptcy Code section 1126(g), holders of Claims in such classes are deemed to have rejected the Plan. The Debtor solicited votes to accept or reject the Plan from holders of Claims in Classes 3, 4, and 5 in accordance with the procedures set forth in the Disclosure Statement Order and Bankruptcy Code section 1126.

C. Section 1129(a)(3): The Plan Was Proposed in Good Faith and Not by any Means Forbidden by Law

Bankruptcy Code section 1129(a)(3) forbids a bankruptcy court from confirming a plan if it was not proposed in "good faith" or was proposed "by any means forbidden by law." The Second Circuit has construed the good faith standard as requiring a showing that "the plan was proposed with 'honesty and good intentions' and 'with a basis for expecting that the reorganization can be effected.'"[17] Here, the Debtor has proposed the Plan with honesty, good intentions, and a desire to effectuate a full, fair, and feasible restructuring of its liabilities while maximizing value for the benefit of its stakeholders. As described in the Disclosure Statement and the Ksenak Declaration, the Plan is the product of extensive arm's length negotiations among the Debtor, the Committee, OCI, AAC, the Segregated Account, the Rehabilitator, and the Informal Group. These negotiations were difficult and, at times, contentious, and the Plan and Amended Plan Settlement reflect a series of compromises that represent a good faith effort to provide the highest available recoveries to the various stakeholders under the totality of the circumstances. Indeed, throughout the Chapter 11 Case, the Debtor (including its officers and

[17] *Johns-Manville Corp.,* 843 F.2d at 649 (citations omitted); *Texaco,* 84 B.R. at 907 (citations omitted) (in a chapter 11 reorganization, "a plan is considered proposed in good faith if there is a likelihood that the plan will achieve a result consistent with the standards prescribed under the Code").

directors) has upheld its fiduciary duties to stakeholders and protected the interests of all constituents with an even hand. Accordingly, the Debtor submits that the Plan was proposed in good faith and not by any means forbidden by law.

D. Section 1129(a)(4): The Plan Provides That Payments Made or to be Made by the Debtor for Services or Costs and Expenses are Subject to Bankruptcy Court Approval as Reasonable

Bankruptcy Code section 1129(a)(4) provides that certain professional fees and expenses paid by the plan proponent, the debtor, or person issuing securities or acquiring property under the plan be approved by or subject to bankruptcy court approval as reasonable. Here, all payments made or to be made by the Debtor for services or for costs or expenses in connection with the Chapter 11 Case prior to the Effective Date, including all Claims for Accrued Professional Compensation, Indenture Trustee Fees, and Informal Group Fees, will have been approved by, or are subject to approval of the Bankruptcy Court, as reasonable. In particular, Article II.C of the Plan provides for the payment of only allowed Claims for Accrued Professional Compensation and Article II.F of the Plan provides that the Debtor and the Committee shall have the opportunity to object to the Indenture Trustee Fees and/or the Informal Group Fees, and following the filing of an objection the Debtor will not be required to pay any such fees unless and until such objection is resolved or the Bankruptcy Court enters an order providing for payment of the disputed portion. Because Accrued Professional Compensation Claims must be allowed by the Bankruptcy Court and Claims for Indenture Trustee Fees and Informal Group Fees are subject to Bankruptcy Court approval as reasonable, the Plan complies with the requirements of Bankruptcy Code section 1129(a)(4).

E. Section 1129(a)(5): The Plan Provides for Disclosure of Post-Reorganization Directors and Officers and Their Appointment is Consistent With Public Policy

Bankruptcy Code section 1129(a)(5) requires that (i) the proponent of a plan disclose the identity and affiliations of the proposed officers and directors of the reorganized debtor; (ii) the appointment or continuance of such directors and officers is consistent with the interests of creditors and equity security holders and with public policy; and (iii) the proponent of a plan has disclosed the identity and nature of compensation of any insiders to be employed or retained. As noted in the Ksenak Declaration, the following individuals will serve as members of the initial board of directors of the Reorganized Debtor: Diana Adams (the Debtor's President and Chief Executive Officer), Charles Lemonides, Victor E. Mandel, Jeffrey Stein, and Nader Tavakoli. Pursuant to Article IV.K of the Plan, the Debtor's existing officers shall remain in place as officers of the Reorganized Debtor. The only such officers who participate in the management of the Debtor, and therefore are considered insiders of the Debtor under Bankruptcy Code section 101(31)(B), are Diana Adams, Robert B. Eisman (Senior Managing Director, Chief Accounting Officer, and Controller), myself, Michael Reilly (Senior Managing Director), and David Trick (Senior Managing Director, Chief Financial Officer, and Treasurer). The foregoing officers are currently employed and compensated by AAC. In accordance with intercompany cost allocation procedures, the Debtor reimburses AAC for each individual's time that is spent on matters relating to the Debtor. In addition to an annual salary, these individuals are eligible for a bonus, both of which are paid by AAC, subject to intercompany cost allocation procedures. In accordance with the Cost Allocation Agreement, this compensation structure is expected to continue following the Effective Date, as noted in the Ksenak Declaration. The appointment or continuance of the Reorganized Debtor's directors and officers is consistent with the interests of

creditors and equity security holders and in accord with public policy. Accordingly, the Debtor submits it has satisfied the requirements of Bankruptcy Code section 1129(a)(5).

F. Section 1129(a)(6): The Plan Does Not Require Governmental Approval of Rate Changes

Bankruptcy Code section 1129(a)(6) permits confirmation of a plan only if any regulatory commission that will have jurisdiction over the debtor after confirmation has approved any rate changes provided for in the plan. The Plan does not provide for any rate changes and no party has argued otherwise, and thus, Bankruptcy Code section 1129(a)(6) is inapplicable here.

G. Section 1129(a)(7): The Plan is in the Best Interests of Holders of Claims and Equity Interests

The "best interests test" of Bankruptcy Code section 1129(a)(7) requires that, with respect to each impaired class, each holder of a claim or interest in such class has either accepted the plan or will receive or retain property having a present value, as of the effective date of the plan, of not less than what such holder would receive if the debtor were liquidated under chapter 7 of the Bankruptcy Code at that time. In other words, the best interests test is satisfied where the estimated recoveries for impaired creditors in a hypothetical chapter 7 liquidation are less than or equal to the estimated recoveries for a holder of an impaired claim or interest under the debtor's plan that rejects the plan.

A chapter 7 liquidation of the Debtor would result in the elimination of substantial value being delivered to creditors under the Plan. Specifically, Ambac's NOLs would not be preserved, the Debtor would not receive $30 million in cash from AAC, $350 million in Junior Surplus Notes from the Segregated Account or any Tolling Payments from AAC, the Debtor would lose all benefits associated with the Cost Allocation Agreement and Mediation Agreement, and the Debtor would incur additional costs in connection with consummating a sale of its ownership interest in AAC. Moreover, a chapter 7 trustee would need to satisfy or resolve

the IRS's priority claims before making a distribution to holders of Claims and Equity Interests. The following table provides an overview of recoveries to holders of Claims and Equity Interests under the liquidation analysis attached to the Disclosure Statement as Exhibit D:

Class	Estimated Recovery under the Plan	Estimated Recovery in a Chapter 7 Liquidation
Class 1 - Priority Non-Tax Claims	100%	100%
Class 2 - Secured Claims	100%	100%
Class 3 - General Unsecured Claims	8.5% - 13.2%	1.8% - 2.3%
Class 4 - Senior Notes Claims	11.4% - 17.6%	2.4% - 3.1%
Class 5 - Subordinated Notes Claims	.5% - .8%	0%
Class 6 - Section 510(b) Claims	0%	0%
Class 7 - Intercompany Claims	0%	0%
Class 8 - Equity Interests	0%	0%

The liquidation analysis and the Brown Declaration plainly establish that all holders of Claims or Equity Interests will receive or retain property valued, as of the Effective Date, at an amount greater than or equal to the value of what they would receive if the Debtor were liquidated under chapter 7. Accordingly, the Debtor submits the Plan satisfies the requirements of Bankruptcy Code section 1129(a)(7).

H. Section 1129(a)(8): Acceptance by Impaired Classes

Bankruptcy Code section 1129(a)(8) requires that each class of claims or interests must either accept the plan or be unimpaired thereby. As noted above and in the Vote Certification, Classes 1 and 2 are deemed to accept the Plan pursuant to Bankruptcy Code section 1126(f) and Classes 3, 4, and 5 voted overwhelmingly to accept the Plan. Accordingly, Bankruptcy Code section 1129(a)(8) has been satisfied with respect to Classes 1 through 5. Classes 6 through 8 are

conclusively presumed to have rejected the Plan pursuant to Bankruptcy Code section 1126(g), and thus, Bankruptcy Code section 1129(a)(8) has not been satisfied with respect to such Classes. Nevertheless, as discussed more fully below, the Debtor meets the requirements of Bankruptcy Code section 1129(b) to "cram down" those Classes of claims that are deemed to have rejected the Plan.

I. Section 1129(a)(9): The Plan Complies With Statutorily-Mandated Treatment of Administrative and Priority Tax Claims

Bankruptcy Code section 1129(a)(9) requires that entities holding allowed claims entitled to priority under Bankruptcy Code section 507 receive specified treatment under the plan. In accordance with Bankruptcy Code section 1129(a)(9)(A) and (B), Articles II.A and III.B.1 of the Plan provide that all Allowed Administrative Claims under Bankruptcy Code section 503(b) and all Allowed Non-Tax Priority Claims under Bankruptcy Code section 507(a) will be paid in full in Cash on the later of the Effective Date, the date such Claim becomes allowed, or as soon as practicable thereafter.[18] Further, Article II.D of the Plan provides that Allowed Priority Tax Claims shall be provided treatment in a manner consistent with Bankruptcy Code section 1129(a)(9)(C). Based upon the foregoing, the Plan satisfies the requirements of Bankruptcy Code section 1129(a)(9).

J. Section 1129(a)(10): At Least One Class of Impaired Claims Has Accepted the Plan

Bankruptcy Code section 1129(a)(10) requires the affirmative acceptance of the Plan by at least one class of impaired claims determined without including any acceptance of the plan by an insider. As set forth in the Vote Certification, Classes 3, 4, and 5, which are Impaired under

[18] Allowed Administrative Claims relating to ordinary course of business transactions may be paid in full on the date such claims become due and payable by their terms or as soon as practicable thereafter and Allowed Administrative Claims relating to Accrued Professional Compensation will be paid in full on the date on which an order allowing such claims is entered or as soon as practicable thereafter.

the Plan, voted to accept the Plan. Those Classes qualify as Impaired but accepting Classes, and thus, the requirements of Bankruptcy Code section 1129(a)(10) have been satisfied.

K. Section 1129(a)(11): The Plan is Not Likely to be Followed by Liquidation or the Need for Further Financial Reorganization

Bankruptcy Code section 1129(a)(11) requires that, as a condition precedent to confirmation, the Bankruptcy Court determine that the Plan is feasible, *i.e.*, "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further reorganization, of the debtor … unless such liquidation or reorganization is proposed in the plan." The Bankruptcy Code's feasibility test requires that the Bankruptcy Court determine whether the Plan is workable and has a reasonable likelihood of success.[19] In determining whether a plan is workable, courts have considered the following factors: (i) the adequacy of the capital structure, (ii) the earning power of the business, (iii) economic conditions, (iv) the ability of management and the probability of continuation of the same management, and (v) any other related matters which will determine the prospects of a sufficiently successful operation to enable performance of the provisions of the plan.[20]

For purposes of determining whether the Plan satisfies the above-referenced feasibility standards, the Debtor has analyzed its ability to fulfill its obligations under the Plan. As part of this analysis, the Debtor prepared projections of its financial performance which are included in Article VI.C of the Disclosure Statement. The projections are premised on certain assumptions,

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[19] *See United States v. Energy Res. Co., Inc.*, 495 U.S. 545, 549 (1990); *Johns-Manville Corp.*, 843 F.2d at 649 ("the feasibility standard is whether the plan offers a reasonable assurance of success. Success need not be guaranteed"); *In re One Times Square Assocs. Ltd. P'ship*, 159 B.R. 695, 709 (Bankr. S.D.N.Y. 1993) (quoting *Collier on Bankruptcy* 1129.02[11] at 1129-54 (15th ed. 1992)) ("It is not necessary that the success be guaranteed, but only that the plan present a workable scheme of reorganization and operation from which there may be a reasonable expectation of success").

[20] *See Worldcom*, 2003 WL 23861928, at *58 (citations omitted); *Texaco*, 84 B.R. at 910-11; *In re Prudential Energy Co.,* 58 B.R. 857, 862-63 (Bankr. S.D.N.Y. 1986); *see also Teamsters Nat'l Freight Indus. Negotiating Comm. v. U.S. Truck Co.* (*In re U.S. Truck Co.),* 800 F.2d 581, 589 (6th Cir. 1986).

including general business and economic conditions, reorganization assumptions, operating and financial assumptions, and market conditions. Based upon such projections and other information in the Disclosure Statement, the Debtor anticipates that its cash on hand upon emergence and following the Plan Settlement Effective Date will provide sufficient liquidity to make all required payments under the Plan and to satisfy working capital requirements on a going-forward basis.

Based upon the foregoing and the Brown Declaration, the Plan is feasible and there is a reasonable likelihood that the Reorganized Debtor will meet its financial obligations under the Plan in the ordinary course of business and confirmation of the Plan is not likely to be followed by the liquidation or need for further financial reorganization of the Reorganized Debtor. Therefore, the Plan satisfies the Bankruptcy Code's feasibility standard.

L. Section 1129(a)(12): All Statutory Fees Have Been or Will Be Paid

Bankruptcy Code section 1129(a)(12) requires the payment of "[a]ll fees payable under section 1930 of title 28, as determined by the court at the hearing on confirmation of the plan." Further, Bankruptcy Code section 507(a)(2) provides that "any fees and charges assessed against the estate under [section 1930 of] chapter 123 of title 28" are afforded priority as administrative claims. In accordance with the foregoing sections, Article II.E of the Plan provides that all such fees and charges payable will be paid in cash on the Effective Date and thereafter as may be required. Accordingly, the Plan satisfies the requirements of Bankruptcy Code section 1129(a)(12).

M. Sections 1129(a)(13)-(16) are Inapplicable

Bankruptcy Code sections 1129(a)(13) (requiring that a plan provide for retiree benefits at levels established pursuant to Bankruptcy Code section 1114), (14) (requiring that a debtor pay domestic support obligations if required to do so by a judicial or administrative order or by

statute), (15) (imposing requirements upon individual debtors), and (16) (imposing requirements upon debtors that are corporations or trusts that are not moneyed, business, or commercial corporations or trusts) are inapplicable because the Debtor does not believe there are any existing retiree benefits that require funding by the Reorganized Debtor, the Debtor is not required by a judicial or administrative order or by statute to pay any domestic support obligations, the Debtor is not an individual, and the Debtor is a moneyed, business, or commercial corporation. Therefore, these sections are inapplicable to the Chapter 11 Case.

N. Section 1129(b): The Plan Satisfies the Bankruptcy Code's "Cram Down" Requirements

Bankruptcy Code section 1129(b) provides a mechanism for confirmation of a plan in circumstances where the plan has not been accepted by all impaired classes of claims and equity interests. This section provides, in relevant part:

> Notwithstanding section 510(a) of this title, if all of the applicable requirements of [Bankruptcy Code section 1129(a)] other than [Bankruptcy Code section 1129(a)(8)'s requirement that a plan be accepted by all impaired classes] are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.

By its express terms, Bankruptcy Code section 1129(b) is only applicable to a class of creditors that rejects a plan. Accordingly, a dissenting creditor in an accepting class lacks standing to object to the Plan on the basis of unfair discrimination or absolute priority.[21] As each

[21] *See Johns-Manville Corp.*, 843 F.2d at 650 (refusing to consider objection of dissenting creditor in accepting class because 1129(b) did not need to be satisfied as to an accepting class); *In re Jersey City Med. Ctr.*, 817 F.2d 1055, 1062 (3d Cir. 1987) (overruling cramdown objection because objecting party was a member of an accepting class and therefore Bankruptcy Code section 1129(b)(1) afforded no protection to such party); *In re United Marine Inc.*, 197 B.R. 942, 948 (Bankr. S.D. Fla. 1996) (overruling absolute priority objection of a dissenting creditor in an accepting class because "the absolute priority rule only applies in the context of cramdown of an impaired *rejecting* class").

class of creditors entitled to vote accepted the Plan by overwhelming majorities, cramdown is only relevant to those Classes of Claims and Equity Interests that are deemed to have rejected the Plan, *i.e.*, Classes 6 through 8. The Plan may be confirmed as to each of these classes pursuant to Bankruptcy Code section 1129(b)'s cramdown provisions.

(1) The Plan Does Not Discriminate Unfairly

Bankruptcy Code section 1129(b)(1) does not prohibit discrimination between classes. Rather, it prohibits discrimination that is unfair. Pursuant to Bankruptcy Code section 1129(b), a plan unfairly discriminates where similarly situated classes are treated differently without a reasonable basis for the disparate treatment.[22] As between two classes of claims or interests, there is no unfair discrimination if (i) the classes are comprised of dissimilar claims or interests or (ii) taking into account the particular facts and circumstances of the case, there is a reasonable basis for such disparate treatment.[23] The Debtor's Plan does not "discriminate unfairly" with respect to any Class deemed to reject the Plan. The Plan's treatment of Class 6 Section 510(b) Claims is based upon the statutory mandates of Bankruptcy Code sections 510(b). To comply with Bankruptcy Code section 1129(a)(1), which requires that the Plan comply with the applicable provisions of the Bankruptcy Code, section 510 must be enforced. Accordingly, Class 6 is not similarly situated to other Classes and the disparate treatment of such Class in comparison to Classes 3 and 4, which are not subordinated by statute, is not unfair. Additionally, the Plan does not discriminate unfairly with respect to Class 7 because there are no Claims in

[22] *See*, *e.g.*, *WorldCom*, 2003 WL 23861928, at *59 (citing *In re Buttonwood Partners, Ltd.*, 111 B.R. 57, 63 (Bankr. S.D.N.Y. 1990)) ("a plan unfairly discriminates where similarly situated classes are treated differently without a reasonable basis for the disparate treatment … Thus, if under the facts and circumstances of a particular case, there is a reasonable basis for disparate treatment of two similarly situated classes of claims … or equity interests … there is no unfair discrimination").

[23] *See*, *e.g.*, *Johns-Manville Corp.*, 68 B.R. at 636 ("the interests of … Class 8 … are not similar or comparable to those of any other class. Thus, this court finds no unfair discrimination").

Class 7. Finally, the Plan does not discriminate unfairly with respect to Class 8 because Equity Interests are classified together and afforded the same treatment under the Plan.

(2) The Plan is Fair and Equitable

Bankruptcy Code sections 1129(b)(2)(B)(ii) and (b)(2)(C)(ii) provide that a plan is "fair and equitable" with respect to a class of impaired unsecured claims or interests if under the plan no holder of any junior claim or interest will receive or retain property under the plan on account of such junior claim or interest. Distributions under the Plan are made in the order of priority proscribed by the Bankruptcy Code and in accordance with the absolute priority rule. Pursuant to the Plan, holders of Claims in Class 6 are receiving treatment consistent with that required by Bankruptcy Code sections 510(b) and Class 7 Intercompany Claims and Class 8 Equity Interests are being cancelled under the Plan. Further, in determining whether a plan is "fair and equitable," courts consider additional factors, such as whether holders of claims senior to the claims of a dissenting class are receiving more than 100% of the value of their claims.[24] Under the Plan, no holder of an Allowed Claim will receive consideration in excess of its entitlements under the Bankruptcy Code.

II. **Response to Objections**

The Objections which have not been resolved are limited in scope, raising two general arguments: (i) the Debtor undervalued its enterprise and liquidation value, and as a result, the Debtor has not satisfied the best interests test, complied with the absolute priority rule, or proposed the Plan in good faith; and (ii) the Holders' General Release is not in accord with the Second Circuit's *Metromedia* decision.

[24] *See*, *e.g.*, *United Sav. Ass'n v. Timbers of Inwood Forest Assocs. (In re Timbers of Inwood Forest Assocs.)*, 793 F.2d 1380, 1410 (5th Cir. 1986), *aff'd on reh'g*, 808 F.2d 363 (5th Cir. 1987), *aff'd*, 484 U.S. 365 (1988) (citations omitted) ("[n]o class may be paid more than in full").

A. The Debtor Has Not Undervalued its Enterprise or Liquidation Values

An ad hoc group of equity security holders [Docket No. 849] (the "Equity Group") and various individual shareholders[25] have filed Objections (respectively, the "Equity Group Objection" and the "Individual Shareholder Objections," and together, the "Shareholder Objections") which assert that (i) Blackstone's valuation does not accurately reflect the Debtor's enterprise or liquidation values; (ii) Blackstone undervalued "put-back" claims asserted by AAC in certain actions (such claims, together with similar or potential claims, the "Put-Back Claims"); (iii) AAC's loss reserves were increased for the purpose of minimizing the perceived value of the Debtor's ownership interest in AAC; and (iv) Blackstone's valuation is stale and does not reflect any improvement in economic and other market conditions.

The Shareholder Objections assert that, as a result: (i) the best interests test has not been satisfied because creditors would receive a greater recovery in a liquidation of the Debtor's ownership interest in AAC than they will receive under the Plan; (ii) the Plan is not fair and equitable, as required by Bankruptcy Code section 1129(b), because creditors will be receiving more than the allowed amount of their respective claims pursuant to the Plan; and (iii) the Debtor has not acted in good faith in connection with assessing its enterprise and/or liquidation values, and therefore, has not proposed the Plan in good faith. As described below, however, the Debtor

[25] *See* Objections of Wolfgang Drogis [Docket Nos. 607, 608, and 652], Frederick Sam [Docket Nos. 628, 770, 826, and 830], Edward F. Hosinger [Docket No. 832], Thomas W. Barrett [Docket No. 836] (joining in Mrs. Sam's Objection at Docket No. 826), Wanson F. Silva [Docket No. 837], Bradley A. Sparks [Docket No. 838], Carlos Castillo [Docket No. 839], Scott E. Wilbur [Docket No. 840], Marcelo Fabian Roitman [Docket No. 841], Raju Porandla [Docket No. 844], Neelima Vojjala [Docket No. 845], Sven Preut [Docket No. 846], Scott E. Wilbur [Docket No. 847], James P. Knipp [Docket No. 848], and Thomas W. Barrett [Docket No. 852]. The foregoing objections, in addition to requesting that the Bankruptcy Court deny confirmation of the Plan, request the appointment of a trustee pursuant to Bankruptcy Code section 1104. The appointment of a trustee is plainly unwarranted, given that the Individual Shareholder Objections have failed to demonstrate that the Debtor has acted with less than good faith, as described below, let alone demonstrated that the Debtor engaged in fraud, dishonesty, incompetence, or gross management. Another shareholder alleges that the Debtor failed to provide adequate disclosure concerning the methodology employed in valuing its interests in AAC. *See* Objection of Wanson Silva [Docket No. 688].

properly assessed its enterprise and liquidation values, and thus, all of the Shareholder Objections lack merit and should be overruled.

(1) The Equity Group's "Preliminary Analysis" is Inadmissible

The Equity Group asserts, based upon the "preliminary analysis" of its financial advisor, NHB Advisors, Inc., that the Debtor's enterprise and liquidation values have been undervalued and fail to take into account "several billion dollars of accretive value." Equity Group Objection at ¶15. The Equity Group further requests, given such preliminary analysis, that the Bankruptcy Court either deny confirmation of the Plan or postpone the confirmation hearing. Equity Group Objection at ¶¶22-23. However, the Bankruptcy Court cannot consider the Equity Group Objection to the extent it relies upon expert testimony, as the Equity Group Objection is not accompanied by an expert statement or report or otherwise supported by admissible expert valuation testimony. Contemporaneously herewith, the Debtor has filed a motion to strike the Equity Group Objection to the extent it relies upon such testimony. Nevertheless, out of an abundance of caution, the Debtor responds to the Equity Group Objection below.

(2) Blackstone Properly Assessed the Debtor's Enterprise and Liquidation Values

(i) Enterprise Value

As noted in the Brown Declaration, Blackstone's enterprise valuation includes the tangible sources of value stemming from the Amended Plan Settlement as well as the Debtor's cash position and residual interest in AAC. Further, as noted in the Brown Declaration, Blackstone's valuation of the Debtor's ownership interest in AAC is based primarily on AAC's ability to pay dividends to the Debtor. AAC's ability to pay such dividends, in turn, has been significantly restricted as a result of the deterioration of AAC's financial condition and the establishment of the Segregated Account. AAC's ability to pay dividends has also been

restricted by the terms of the CDS Settlement Agreement, dated as of June 7, 2010, pursuant to which AAC paid certain credit default swap counterparties $2.6 billion in cash and $2 billion in surplus notes of AAC in exchange for the termination of certain obligations. Further, AAC's ability to pay dividends to the Debtor is restricted by certain terms of its approximately $660 million in auction market preferred shares ("AMPS").

Additionally, as noted in the Brown Declaration, although the Segregated Account's rehabilitation plan has been confirmed by the Circuit Court of Dane County, Wisconsin, such plan has not yet become effective and substantial revisions may be made thereto. All dividend payments by AAC to the Debtor must be approved by OCI and it is unlikely that OCI will permit AAC to pay dividends to the Debtor unless and until OCI is satisfied that AAC and the Segregated Account will be able to pay all current and future policy claims, surplus notes, and other obligations. Given the magnitude and timing of projected loss defaults, such clarity may not be known for an extended period of time, perhaps decades.

Moreover, AAC's most recent statutory filing for the period ending December 31, 2011 reports AAC as having policyholder surplus of approximately $495 million (*see* http://www.ambac.com/investor_statutory.asp), which includes $2 billion of surplus notes of AAC issued pursuant to the CDS Settlement Agreement and approximately $660 million of AMPS, among other obligations. These notes and the AMPS are obligations of AAC and it would have to be made clear that these obligations will be able to be paid or settled in full with their holders along with all policyholders and other obligations before the Debtor could realize residual equity value in AAC. Accordingly, the ability of the Debtor's creditors or shareholders to achieve a recovery beyond that provided for under the Plan based upon AAC's future residual equity value is highly unlikely.

In practical terms, AAC's main assets are future installment premiums, the holdings in its investment portfolio, and litigation recoveries, whereas AAC's liabilities include payment of all current and future policy claims, surplus notes, and its AMPS. In order for there to be residual equity value available at AAC, all of AAC's liabilities, including surplus notes, AMPS, and all other obligations must first be paid in full.

(ii) Liquidation Value

As noted in the Brown Declaration, to the extent there is any value at AAC for the Debtor, this value may only be realized through the payment of ordinary or extraordinary dividends by AAC to the Debtor or as residual equity value once it becomes clear that all current and future policy claims, surplus notes, and the AMPS can be paid in full. Further, all dividend payments by AAC to the Debtor must be approved by OCI and, as noted in the Brown Declaration, it is unlikely that OCI will permit AAC to pay dividends to the Debtor unless and until OCI is satisfied that AAC and the Segregated Account will be able to pay in full all current and future policy claims, surplus notes, and other obligations. Given the magnitude and timing of projected loss defaults, such clarity may not be known for an extended period of time, perhaps decades. In light of the foregoing, no reasonable investor would purchase the Debtor's ownership interest in AAC. In a chapter 7 liquidation, the likelihood of finding an investor to purchase AAC's equity would be even lower, given that such liquidation would result in the effective loss of all of Ambac's NOLs, *i.e.*, Ambac's NOLs would have no value in a liquidation scenario.

(3) Blackstone Properly Valued the Put-Back Claims

The Equity Group Objection and certain Individual Shareholder Objections assert that the Disclosure Statement undervalues the Debtor's expected recoveries from AAC's Put-Back Claims at $2.6 billion.

As of September 30, 2011, the date the Disclosure Statement was filed, $2.6 billion represented the Debtor's best good faith estimate of recoveries AAC was likely to receive from the Put-Back Claims, an estimate which has not changed materially enough, as of December 31, 2011, to require revision to the estimated enterprise or liquidation values. This estimate was formulated in accordance with a detailed protocol prepared by the Debtor in consultation with Patterson Belknap Webb & Tyler LLP, AAC's counsel in connection with the Put-Back Claims. In connection with its review of the Debtor's quarterly financial results, KPMG LLP, the Debtor's independent auditor, audited the assumptions utilized and the computations made in determining such expected recoveries. The $2.6 billion figure takes into account the risks associated with litigating the Put-Back Claims and the potential difficulties associated with collecting large judgments.

Moreover, as noted in the Brown Declaration, Blackstone's valuation analysis includes $1 billion of incremental value resulting from an assumption that various value creation initiatives can be implemented. While the Debtor believes these value creation initiatives are likely to be achieved, there is no certainty that they can be achieved.

(4) AAC's Loss Reserves Were Properly Calculated

The Equity Group Objection asserts that its financial advisor "notes that AAC may have excessively reserved for losses associated with its U.S. Public Finance Accounts." Equity Group Objection at ¶15. Similarly, several Individual Shareholder Objections assert that AAC increased its loss reserves to manipulate the perceived value of the Debtor's ownership interest in AAC and hide $3.2 billion AAC allegedly received from Takefuji Corp. *See*, *e.g.*, Objection of Frederick Sam [Docket No. 826] and Edward F. Hosinger [Docket No. 832] ("the Debtor has steadily increased their loss reserves to huge amounts … the same amount AAC received … from Takefuji").

As noted in the Brown Declaration, the Debtor disclosed in its public filings that it utilizes a blend of the results of an internal roll-rate model, a licensed Monte Carlo model, and licensed statistical regression model to project residential mortgage-backed securities ("RMBS") losses and establish RMBS loss reserves. Any increase in RMBS loss reserves is primarily as a result of expected losses within these models.

Moreover, as noted in the Brown Declaration, allegations that the Debtor increased its loss reserves to hide $3.2 billion AAC allegedly received from Takefuji Corp. are false. AAC did not directly receive any funds from Takefuji Corp. Funds were paid by Takefuji to Aleutian Investments LLC, an entity created in connection with an Ambac-sponsored medium-term note program, and were used to satisfy Aleutian's payment obligations. Thus, the funds paid by Takefuji did not directly benefit AAC via cash or other incremental value.

Additionally, the Equity Group Objection asserts that AAC's projected losses and loss reserves fail to incorporate recent market improvements. The Equity Group Objection cites recent purchases of distressed assets, default rates that "suggest that pricing could be at least 65% of par," peak default rates having already occurred, improved economic and housing market conditions, and recent recoveries on student loans as reasons why AAC's projected losses are essentially too high. Equity Group Objection at ¶13. However, there are two main problems with the Equity Group's approach.

First, the Equity Group Objection makes these claims by providing statistics associated with general pools of assets including subprime, RMBS, and student loans. As noted in the Brown Declaration, these statistics fail to accurately reflect the performance of the underlying portfolio of AAC-specific exposures, which is a very large and complex portfolio and is not represented by general and high-level statistics.

Second, the Equity Group Objection uses its claims that economic and housing conditions have improved and that peak default rates have already occurred to make the logical leap that AAC's projected losses must, therefore, be overstated, without having any knowledge of the assumptions underlying AAC's loss projections. As noted above, however, AAC utilizes the results of various models to project losses and establish loss reserves for RMBS exposures. These models take into account a variety of assumptions regarding macro-economic conditions and projected default rates, including many of those cited in the Equity Group Objection. AAC's loss projections are the result of third-party modeling and third-party assumptions and are representative of the expected losses of the specific policies included in AAC's portfolio.

(5) Nothing has Changed Materially Since Blackstone Performed its Valuation That Would Significantly Increase the Debtor's Enterprise or Liquidation Values or Otherwise Permit a Recovery for Existing Shareholders

While Blackstone has not formally updated its valuation or liquidation analysis, Blackstone has maintained an ongoing dialogue with the Debtor regarding AAC's business operations. Based on discussions with management and Blackstone's review of updated financials, nothing has changed materially since Blackstone performed its initial valuation that would significantly increase the enterprise or liquidation values of the Debtor or permit a recovery to holders of its Equity Interests. As discussed in the Disclosure Statement, two of the most significant factors that impact the value of AAC include general and Segregated Account losses and the Put-Back Claims. Based on the most recent statutory filing for the period ending December 31, 2011, AAC's loss reserves have increased to approximately $3.1 billion during 2011 as a result of an increased number of defaulted credits added to the loss reserves – a condition not indicative of a scenario as favorable as depicted in the Equity Group Objection. Moreover, expected nominal future cash flow losses as of September 30, 2011, as projected by a

third-party retained by AAC, have not moved materially enough for Blackstone to believe a change to its valuation is warranted. Finally, as noted in the Brown Declaration, the value of the Put-Back Claims has not changed materially enough as of December 31, 2011 to require revision to the estimated enterprise or liquidation values. As a result, it is not necessary for Blackstone to revise its valuation or liquidation analysis.

As noted in the Brown Declaration, Blackstone's valuation reflects certain additional value creation initiatives. Specifically, Blackstone's valuation analysis reflects approximately $1 billion of incremental value above that which is reflected in AAC's statutory financial statements. Moreover, Blackstone projected, based on discussions with management, that this value would flow to AAC primarily in the near term, which could have a very significant impact on AAC's value from a present value perspective.

B. Objections Alleging the Plan is Un-confirmable on Account of the Holders' General Release Should be Overruled

Veera filed an objection to confirmation of the Plan [Docket No. 842] (the "Veera Objection") asserting that the Holders' General Release set forth in Article VIII.E of the Plan does not pass muster under *Metromedia*. The Equity Group objects to the Plan for similar reasons. *See* Equity Group Objection at ¶¶8-9. Veera asserts "there are no unusual or rare circumstances that would justify the broad releases proposed in the Plan." *See* Veera Objection at 7. Specifically, Veera (i) points out that the Released Parties, which include certain defendants in the ERISA Action, have not furnished any consideration in exchange for the Holders' General Release and (ii) alleges that no identity of interests exists between the Debtor and the Released Parties which are defendants in the Veera Action, as the Debtor's General Release allegedly relieves the Debtor of its indemnification obligations. *See* Veera Objection at 9-11.

The Debtor presented its case as to why the Holders' General Release passes muster under *Metromedia* above and in the Ksenak Declaration and such arguments need not be repeated here. *See*, *supra*, at 18-23. As noted above, unique circumstances exist justifying the Holders' General Release because OCI – not the Released Parties which are defendants in the Veera Action – negotiated for and demanded the Holders' General Release and is funding the Plan through AAC and the Segregated Account pursuant to the Amended Plan Settlement. Moreover, contrary to Veera's assertion otherwise, an identity of interests exists between the Debtor and certain of the Released Parties. Further, other factors weigh in favor of approving the Holders' General Release (as noted above, creditors overwhelmingly voted to accept the Plan, the Holders' General Release is the product of good faith and arm's length negotiations, and the Holders' General Release is consistent with public policy).

Notably, the cases relied upon by *Veera* in support of his argument that unique circumstances do not exist under *Metromedia* actually support approval of the Holders' General Release. Veera relies heavily upon *In re Karta Corp.*, 342 B.R. 45 (S.D.N.Y. 2006). In *Karta*, the issue before the District Court was whether certain releases against non-debtors passed muster under *Metromedia*. As *Veera* points out, the District Court held "the mere fact of financial contribution by a non-debtor cannot be enough to trigger the right to a *Metromedia/Drexel* release of non-debtor claims." *Id.* at 55. However, the District Court nevertheless approved the releases in *Karta*, finding that significant non-debtor financial contributions plus other unusual factors rendered the situation sufficiently unique:

> And because of the unique character of the Cartalemi empire (with a different corporation or partnership owning different assets that are used to run a single integrated enterprise) and the unique circumstance that prevented the business' management from putting KI into bankruptcy, such releases … are exactly the sort of releases that should be sanctioned under *Metromedia / Drexel*.

> Additionally, there is another uniqueness factor in this particular case: the involvement of the City of Peekskill in this bankruptcy and the relationship of the reorganization of this business to the development of the Peekskill waterfront.

Id. at 56. As in *Karta*, the Debtor relies upon its non-debtor affiliates, including AAC, to run its business; the Debtor could not place AAC into bankruptcy because AAC, a domestic insurance company, is ineligible to be a debtor under Bankruptcy Code section 109(b); and, as noted in the Ksenak Declaration, OCI has been intimately involved in the Debtor's restructuring efforts. In light of the foregoing, the factors which render *Karta* unique necessarily render the Debtor's case unique as well.

In approving the releases in question the *Karta* court relied upon *Rosenberg v. XO Commc'ns, Inc. (In re XO Commc'ns, Inc.)*, 330 B.R. 394 (Bankr. S.D.N.Y. 2005). In *XO Commc'ns*, the Bankruptcy Court approved a nonconsensual third-party release notwithstanding the fact that certain released parties did not furnish consideration in exchange. Specifically, the Bankruptcy Court held:

> The absence of consideration by Defendants is not fatal to their release … in that the record of a finding of unique circumstances is clearly supported by the confirmation record. The substantial consideration provided … by the Senior Secured Lenders, the identity of interest present as a result of indemnification/contribution exposure of the Debtor, and the necessity of the satisfaction of the Litigation Condition to the Plan process [a condition that certain threatened or pending litigation against the Debtor, its investors, and certain directors and officers be resolved], all form the basis of a finding fully consistent with *Metromedia* … Therefore, the Court finds that the confirmation record supports the unique circumstances necessary … for allowing the nondebtor releases.

Id. at 439-40. As in *XO Commc'ns*, unique circumstances exist which justify the Holders' General Release under *Metromedia*, notwithstanding the fact that the released directors, officers, and employees are not furnishing consideration in exchange for such release. Specifically, OCI,

though AAC and the Segregated Account, is furnishing substantial consideration. Moreover, as noted above, OCI's contribution was made in contemplation of the resolution of any and all litigation relating to the Debtor or the Debtor's restructuring which may implicate OCI, the Rehabilitator, the Segregated Account, AAC, or its current and former directors and officers. Further, as in *XO Commc'ns*, an identity of interests exists between the Debtor and certain of the released individuals.

Veera's assertion that no identity of interests exists between the Debtor and the released directors and officers on account of the Debtor's General Release is plainly untrue, given the Debtor's indemnification obligations. The Debtor's General Release releases claims by the Debtor against the Released Parties, not the other way around. Although such release does not relieve the Debtor of its indemnification obligations, the Holders' General Release will, as a practical matter, substantially limit the Debtor's exposure to future indemnification claims. Veera argues that even if an identity of interests exists, this is not enough to justify the Holders' General Release, relying upon *In re Saint Vincent's Catholic Medical Centers of NY*, 417 B.R. 688, 696 (S.D.N.Y. 2009). However, *Saint Vincent's* does not stand for this proposition. Rather, the *Saint Vincent's* court held nonconsensual third party releases could not be approved absent "findings that discharging the liability of third-party Covered Persons would be important to the Plan." *Id*. More significantly, the Debtor is not relying solely upon the identity of interests between it and the Released Parties in seeking approval of the Holders' General Release. Rather, unique circumstances exist in this case because OCI negotiated for and demanded the Holders' General Release, an identity of interests exists between the Debtor and certain Released Parties, and other factors weigh in favor of approving the Holders' General Release, as described above.

Veera also asserts that the Holders' General Release is inconsistent with the Stipulation of Settlement Release, which explicitly carves out the Veera Action from its scope, and therefore, the Holders' General Release should also be modified to carve out the Veera Action. However, this argument fails to consider that the Holders' General Release and the Stipulation of Settlement Release serve entirely different purposes. The Stipulation of Settlement Release is intended to resolve any and all Claims and Causes of Action that were, could have been, or may have been asserted in the Securities or Derivative Actions. The Stipulation of Settlement Release carved out the Veera Action from its scope because the directors' and officers' insurance carriers paying $24.6 million in connection with the Stipulation of Settlement do not care whether the Veera Action proceeds. The Holders' General Release does not carve out the Veera Action from its scope because OCI conditioned its funding of the Plan on Bankruptcy Court approval of a release of all current and former directors, officers, and employees of the Debtor and AAC, for reasons described above.

Veera asserts Article XII.O of the Plan, which provides that the Stipulation of Settlement and the Stipulation of Settlement 9019 Approval Order shall control in the event such documents conflict with the Plan, should be interpreted as overriding the Holders' General Release to the extent such release purports to release the Veera Action because the Stipulation of Settlement Release carves out the Veera Action. *See* Veera Objection at 12. Veera's proposed interpretation, however, is plainly inconsistent with the terms of the Plan. While the Stipulation of Settlement Release was designed to be consistent with the Stipulation of Settlement and the Stipulation of Settlement 9019 Approval Order, the Holders' General Release has nothing to do with such documents. Therefore, the Stipulation of Settlement and the Stipulation of Settlement

9019 Approval Order cannot reasonably be interpreted as being "inconsistent" with the Holders' General Release for the purposes of Article XII.O of the Plan.

For the foregoing reasons, Veera's and the Equity Group's Objections to the Holders' General Release should be overruled. Additionally, the Debtor respectfully requests that the Bankruptcy Court reject Veera's proposed interpretation of Article XII.O of the Plan.

C. Other Arguments Raised in the Individual Shareholder Objections Should be Overruled

The Individual Shareholder Objections raise three additional arguments. First, such Objections allege that the Debtor stopped presenting adjusted book value in its operating supplement to mask AAC's true value. As described in the Brown Declaration, however, the Debtor stopped disclosing adjusted book value – which it was never required to do – as the measure became less relevant as losses continued to increase and AAC stopped writing new business.

Second, such Objections allege OCI is pressuring the Debtor to reduce the apparent value of AAC and that the Debtor is conflicted because it needs OCI's approval to confirm its Plan. This is plainly untrue. As evidenced by the Ksenak Declaration and the record of the Chapter 11 Case, the Plan is the result of months of extensive, good-faith, arms' length negotiations among numerous parties other than OCI and the Rehabilitator, *i.e.*, AAC, the Committee, the Informal Group, and the IRS. The Plan reflects the views of all of these parties.

Third, such Objections argue that the Debtor should not be rushing to confirm the Plan as there is no real risk that the Debtor will have to convert its case to one under chapter 7. As noted in the *Affidavit of C.J. Brown in Support of Debtor's Motion for Entry of an Order Extending its Exclusive Period for Soliciting Votes to Accept or Reject a Chapter 11 Plan*, filed on October 24, 2011 [Docket No. 657], the Debtor's cash burn rate is and has been approximately $2.5 to $4.5

million per month (net of reimbursement from AAC for 85% of legal fees related to the IRS Dispute), comprised primarily of legal and other professional expenses. As noted in the Debtor's monthly operating report for the period ending November 30, 2011 [Docket No. 754], the Debtor had less than $30 million in unrestricted cash and cash equivalents and $2.5 million in restricted cash and cash equivalents. Absent confirmation of the Plan and receipt of the $30 million Cash Grant pursuant to the Amended Plan Settlement or the receipt of other funds from AAC, there is no doubt that the Debtor will eventually burn through its available cash.

D. Additional Objections

Attached hereto as Exhibit A is a summary of the other Objections that have been filed and their current status. The Debtor reserves the right to supplement this response or otherwise introduce further evidence in support of confirmation of its Plan.

CONCLUSION

The Plan complies with all applicable requirements of Bankruptcy Code section 1129 and should therefore be confirmed.

Dated: March 6, 2012
New York, New York

Respectfully Submitted,

/s/ Peter A. Ivanick

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EXHIBIT A

(Additional Objections)

Objecting Party	Status / Response
Frederick Sam [Docket No. 687]. Mrs. Sam asserts the Debtor failed to provide adequate notice of the hearing in respect of the deadline for objecting to the Debtor's motion for entry of the Disclosure Statement Order (the "Disclosure Statement Objection Deadline") and the hearing in respect of such motion (the "Disclosure Statement Hearing") because the Disclosure Statement ultimately approved by the Bankruptcy Court was filed after the Disclosure Statement Objection Deadline and five days before the Disclosure Statement Hearing.	The Debtor respectfully refers the Bankruptcy Court to the *Debtor's Objection to Wanson F. Silva's Motion for an Order Overturning the Disclosure Statement Order* and the *Joinder of the Official Committee of Unsecured Creditors to the Debtor's Objection to Wanson F. Silva's Motion for an Order Overturning the Disclosure Statement Order*, both of which were filed February 7, 2012 [Docket Nos. 802 and 803] and address a substantially similar argument raised by a different shareholder.
Thomas Barrett [Docket No. 682]. Mr. Barrett asserts that the Debtor should not have commenced its Chapter 11 Case in response to the IRS's information document request, that the IRS Dispute should have been resolved outside of bankruptcy, that the Debtor has enough cash on hand to remain solvent for the next 3-5 years, and that as a result, the Bankruptcy Court should deny confirmation of the Plan.	Mr. Barrett's Objection does not assert that the Plan cannot be confirmed. To the extent Mr. Barrett's Objection is considered an Objection to confirmation of the Plan on the grounds that the Plan does not satisfy the best interests of creditors test, the Debtor respectfully refers the Court its response to similar Individual Shareholder Objections in its memorandum in support of confirmation of the Plan.
Bank of America, N.A., Wells Fargo Bank, N.A., Wilmington Trust Company, and Wilmington Trust FSB, each as trustee and in similar capacities for certain securities issued in connection with the rehabilitation of the Segregated Account [Docket Nos. 804-806]; Deutsche Bank National Trust Company and Deutsche Bank Trust Company Americas [Docket Nos. 812-13] (collectively, the "Trustees").	The Trustees have informed the Debtor that they object to the inclusion of the phrase "the rehabilitation of the Segregated Account" in the Plan's Exculpation provision. The Debtor intends to work with the Trustees to resolve their objection prior to the Confirmation Hearing.
Broadbill Investment Partners, L.P. and Broadbill Investment Corporation (together, "Broadbill") [Docket No. 831].	This Objection has been resolved, provided the language described in the Objection and which has been incorporated into Article VIII.E of the Plan remains in the Plan, as confirmed, and the Plan is not further amended in a manner that adversely affects Broadbill's rights.
Public School Teachers' Pension and Retirement Fund of Chicago, Arkansas Teachers' Retirement System, Public Employees' Retirement System of Mississippi, and Painting Industry Insurance and Annuity Funds [Docket No. 833].	This Objection has been resolved.