

**IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF PUERTO RICO**

LEX CLAIMS, LLC, et al.,

Plaintiffs,

v.

THE COMMONWEALTH OF PUERTO RICO, et al.,

Defendants.

Case No. 3:16-cv-02374 (FAB)

**REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF AMBAC  
ASSURANCE CORPORATION'S MOTION FOR LEAVE TO INTERVENE AND IN  
SUPPORT OF THE PROMESA STAY**

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## INTRODUCTION

Plaintiffs' Opposition<sup>1</sup> to Ambac's Motion to Intervene does not dispute that Ambac satisfies the tests for both intervention as of right and permissive intervention. *See* Fed. R. Civ. P. 24(a)-(b). Nor could it: As the insurer of more than \$800 million in COFINA bonds (and direct owner of more),<sup>2</sup> Ambac clearly has a significant interest in the SUT securing the COFINA bonds that Plaintiffs seek to misappropriate. It is equally clear that the Court's disposition of Plaintiffs' COFINA Claims may impair Ambac's ability to protect its interests; that the named Defendants—most of whom will suffer no direct harm if Plaintiffs prevail—do not adequately represent Ambac's interests; and that Ambac's defenses to the COFINA Claims cut to the core issue presented by the Second Amended Complaint ("SAC")—whether the Commonwealth's transfer of the SUT to COFINA in 2006 violated the Puerto Rico Constitution.

Instead, Plaintiffs mount two procedural challenges to the Motion to Intervene, each of which is without merit. First, Plaintiffs argue that Ambac has failed to satisfy Rule 24(c) because an answer was not attached to the Motion to Intervene. Although this is wrong—particularly considering that the COFINA Claims were not yet operative when Ambac moved to intervene—the Court need not decide that issue because, in light of the filing of the SAC (Dkt. Nos. 76, 78), Ambac has attached hereto a proposed Answer-in-Intervention. (*See* Ex. A.)

Second, Plaintiffs argue that only the trustee for the COFINA bonds may intervene. This, too, is wrong. Both the text of the "no-action" provision in the COFINA bond resolution (the "Resolution") and the case law construing similar provisions relate only to creditors

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<sup>1</sup> Ambac's Motion for Leave to Intervene and in Support of the PROMESA Stay (Dkt. No. 55) is denoted herein as the "Motion to Intervene." Plaintiffs' Opposition to the Motion to Intervene (Dkt. No. 93) is denoted herein as the "Opposition" or "Opp'n." All other capitalized terms are as defined in the Motion to Intervene.

<sup>2</sup> Ambac sought to intervene in its capacity as insurer, rather than bondholder, for the common sense reason that its financial exposure as insurer dwarfs its exposure as bondholder. Nevertheless, should the Court deem the distinction significant, Ambac currently owns COFINA bonds with a market value of approximately \$29.5 million.

affirmatively instituting legal proceedings (typically against the issuer), *not* a creditor seeking to intervene as a defendant to protect against a third party's attack on pledged collateral. Plaintiffs have not cited a single case—and Ambac's research has not uncovered one—in which a court found such intervention to be impermissible due to a no-action provision.

Having failed to establish a bar to the Motion to Intervene under Rule 24(c) or the Resolution, Plaintiffs advance an interpretation of PROMESA that would read the stay out of existence. Plaintiffs argue that the COFINA Claims could not have been commenced prior to PROMESA's enactment, and therefore are not stayed, because they arise under Section 303(3) of PROMESA. This argument is contradicted by PROMESA itself, as claims under Section 407—the sole provision creating a private right of action to challenge post-PROMESA transfers—are *expressly* subject to the stay. In any event, if repackaging constitutional challenges to executive orders as Section 303(3) claims were enough to evade the stay, then *every single creditor lawsuit challenging executive orders issued by the Commonwealth could be revived through Section 303(3)*, including the numerous consolidated cases in which the Court recently affirmed the stay. This is not the result intended by Congress, and would lead to the very wave of litigation this Court has warned about in applying the stay. *See Brigade Leveraged Capital Structures Fund v. García-Padilla*, Civ. No. 16-1610 (D.P.R.) (Dkt. No. 140) (the "Brigade Order"), at 40-42.

Plaintiffs further argue that the COFINA Claims are not stayed because they purportedly challenge post-PROMESA conduct—*i.e.*, the June 30 Executive Order—and seek an order declaring the June 30 Executive Order preempted under PROMESA. This argument is belied by the fact that an order invalidating the June 30 Executive Order would have *no effect whatsoever* on the transfer of the SUT to COFINA. The SUT was transferred to COFINA by COFINA's enabling legislation, not the June 30 Executive Order. This fact is not lost on Plaintiffs, who,

instead of requesting nullification of the June 30 Executive Order, seek an order modifying it by directing the SUT to the Commonwealth—a modification that would itself violate PROMESA by transferring assets outside the ordinary course. The COFINA Claims aim to invalidate the COFINA structure and the 2006 statute establishing it; they do *not* arise under PROMESA.

Although Ambac trades from time to time in Puerto Rico securities, including COFINA bonds (*see supra* at 1 n.2), Ambac is differently situated from the other putative intervenors in this action by virtue of its diverse, long-term commitment to Puerto Rico’s financial recovery—a commitment reflected in its insurance of many billions of dollars in principal and interest payments through 2054. In keeping with this commitment, Ambac has supported the PROMESA stay in each case to which it is a party,<sup>3</sup> cognizant that the stay provides a critical opportunity for the Oversight Board to facilitate desperately needed fiscal reforms. As this Court noted in *Brigade*, intervening orders by this Court on constitutional questions have the potential to be rendered moot by the Oversight Board. Here, too, principles of constitutional avoidance counsel against adjudication of the COFINA Claims before it is necessary to decide them.

## ARGUMENT

### I. Ambac Has Satisfied the Pleading Requirement of Rule 24(c).

As noted, Plaintiffs’ contention that the Motion to Intervene should be denied as procedurally defective, however erroneous,<sup>4</sup> is now moot. (Opp’n at 6-7.) Even under the strict interpretation of Rule 24(c) advanced by Plaintiffs, Ambac has satisfied the pleading requirement by attaching hereto a proposed Answer-in-Intervention. (*See Ex. A.*)

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<sup>3</sup> *See Assured Guar. Corp. v. García-Padilla*, Civ. No. 16-1037 (D.P.R.) (Dkt. No. 64) (acquiescing to PROMESA stay while reserving right to move to lift the stay should circumstances warrant); *Ambac Assurance Corp. v. Puerto Rico Highways and Transp. Auth.*, Civ. No. 16-1893 (D.P.R.) (Dkt. No. 64) (same).

<sup>4</sup> Plaintiffs claim that Rule 24(c) can be satisfied only through attachment of one of the documents listed in Rule 7(a). Numerous courts have found otherwise. *See, e.g., City Of Bangor v. Citizens Commc’ns Co.*, 532 F.3d 70, 83-84, 95 & n.11 (1st Cir. 2008); *Piambino v. Bailey*, 757 F.2d 1112, 1121 (11th Cir. 1985).

## II. There Is No Contractual Impediment to Ambac’s Intervention as a Defendant.

**Subrogation Principles.** Plaintiffs argue that Ambac is barred from intervening because it has not paid a claim under the applicable financial guaranty insurance policy (the “Ambac Insurance Policy”). (Opp’n at 7.) This argument mischaracterizes the Ambac Insurance Policy.

First, the Court need not address whether Ambac in its capacity as insurer must be subrogated to the rights of the bondholders before intervening, because Ambac is also a direct holder of COFINA bonds. Second, it is untrue that the Ambac Insurance Policy provides that Ambac may participate in litigation only upon the payment of a claim; the subrogation provision in that Policy merely provides that, *if* a claim is paid, Ambac will be subrogated to the rights of the bondholders. (See Dkt. No. 93-1, at Ex. B, at 12.) Nothing in the subrogation provision limits any other rights Ambac may have under applicable law, including Rule 24.<sup>5</sup> In any event, Plaintiffs’ claim that Ambac lacks any “legally cognizable interest in this litigation” (Opp’n at 7) is untenable—setting aside the millions of dollars of principal and interest payments Ambac may be liable for if COFINA is deprived of its sole revenue stream, Ambac enjoys numerous rights relating to COFINA that have nothing to do with payment defaults or subrogation—*e.g.*, consent rights, information rights, and the right to direct an accounting—reflecting its status as a key COFINA stakeholder. (See Dkt. No. 93-1, at Ex. B, at 9-10, ¶¶ (b), (c), (e), (f).)

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<sup>5</sup> Nor does this Court’s decision in *Assured Guaranty Corporation v. Commonwealth of Puerto Rico*, Civ. No. 16-2384 (Dkt. No. 59) (Nov. 2, 2016), affect the intervention analysis. There, the question was whether the insurer had suffered injury-in-fact under Article III such that it could sue as a plaintiff; the Court found that it had not because it had not yet paid out on a claim. *Id.* at 12-13. Although the First Circuit has not decided the issue, *see Mangual v. Rotger-Sabat*, 317 F.3d 45, 61 & n.5 (1st Cir. 2003), the Article III standing requirement should not apply to a request for intervention as a defendant, which turns on whether the intervenor claims an interest in property that is the subject of the action where the court’s disposition of the dispute will impair or impede the intervenor’s ability to protect that interest. Consistent with this distinction, Plaintiffs only challenge Ambac’s “contractual authority” to intervene, not its “standing” to do so. (See Opp’n at 7.) In any event, “in the ordinary case, an applicant who satisfies the ‘interest’ requirement of the intervention rule is almost always going to have a sufficient stake in the controversy to satisfy Article III as well.” *Cotter v. Mass. Ass’n of Minority Law Enforcement Officers*, 219 F.3d 31, 34 (1st Cir. 2000) (quoting *Transamerica Ins. Co v. South*, 125 F.3d 392, 396 n.4 (7th Cir. 1997)). That is the case here, as Ambac clearly would have standing both as an insurer and a direct holder of COFINA bonds.

***The No-Action Provision.*** Plaintiffs cite language from the COFINA bonds and the Resolution that, they claim, prevents Ambac from intervening in this action. (Opp’n at 10.) None of the provisions relied upon by Plaintiffs applies to Ambac’s request to intervene.

First, Plaintiffs point to disclosures on the COFINA bonds stating that bondholders lack the right “to enforce the provisions of this Resolution, to institute action to enforce the provisions of the Resolution or to institute, appear in or defend any suit or other proceeding ***with respect thereto.***” (Dkt. No. 93-1 at Ex. A, at 2 (emphasis added).) As an initial matter, the disclosures on the COFINA bonds are merely descriptive of the terms of the Resolution. But even if this were the operative language, Plaintiffs ignore the words “with respect thereto,” which refers to the Resolution. That is, any limitation on bondholders’ ability to “appear in or defend” suits is only with respect to the “provisions of the Resolution.” (*Id.*) Here, Plaintiffs do not allege that any of the parties to the Resolution are failing to comply with their obligations thereunder. Thus, the disclosures in the COFINA bonds relied upon by Plaintiffs simply do not apply.

Second, Plaintiffs cite portions of Section 1106 of the Resolution—the actual no-action provision—which purportedly provide that a bondholder may not “institute [a] suit . . . or other proceeding” unless it meets certain prerequisites. (Opp’n at 10.) Plaintiffs’ selective quotation, however, is misleading. The complete relevant language provides: “No owner of any Bond shall have any right to institute any suit, action, mandamus or other proceeding in equity or at law ***hereunder***, or for the protection or enforcement of any right ***under this Resolution***, unless . . . .” (Dkt. No. 93-2 at 76 (emphasis added).) Again, Ambac’s Motion to Intervene is unrelated to the Resolution; it seeks to defend Ambac’s collateral from constitutional attack by Plaintiffs.

Further, the no-action language cited by Plaintiffs also provides that bondholders shall not institute litigation unless holders of at least 25% of the COFINA bonds “have given to the

Trustee written notice of the Event of Default or breach of duty on account of which such suit, action or proceeding is to be taken.” (*Id.*) Where, as here, bondholders do not seek to remedy such a breach, but rather seek to defend against a third party’s claims, the no-action provision by its terms does not apply. Indeed, in the absence of such a breach, there is no mechanism for compelling the COFINA trustee to litigate, leaving COFINA’s bondholders entirely defenseless were they not free to intervene on their own.

Finally, although unmentioned by Plaintiffs, Section 1106 of the Resolution further provides that bondholders lack the right “to enforce any right hereunder or under law with respect to the Bonds.” (*Id.* at 77.) Certain decisions have found similar no-action language to apply to claims other than those arising under the bond indenture. *See, e.g., Lange v. Citibank, N.A.*, 2002 WL 2005728, at \*5-6 (Del. Ch. Aug. 13, 2002); *Feldbaum v. McCrory Corp.*, 1992 WL 119095, at \*5 (Del. Ch. June 2, 1992). In each of these cases, however, the bondholders were enforcing rights by **asserting** common-law or statutory claims as plaintiffs, not by intervening to defend against an action that might affect their interests.

Here, Ambac is not seeking “to enforce any right . . . with respect to the Bonds.” *See* Black’s Law Dictionary 596 (8th ed. 2004) (defining “enforce” to mean “[t]o give force or effect to (a law, etc.); to compel obedience to”). Ambac does not seek to intervene in this action to compel compliance by the Commonwealth or COFINA with their respective obligations, but rather to **prevent** a judicial order that would cause them to violate those obligations. Nothing in the Resolution’s no-action provision or the case law construing similar provisions bars such intervention. To the contrary, a recent decision in Detroit’s bankruptcy proceedings permitted it. *See City of Detroit, Mich. v. Detroit Gen. Ret. Sys. Serv. Corp. (In re City of Detroit, Mich.)*, No. 13-53846, Adv. No. 14-04112 (Dkt. No. 73), slip op. at 12-13 (Bankr. E.D. Mich. June 30, 2014)

(attached hereto as Ex. B) (no-action clause was “intended to prevent certificate holders from instituting proceedings against others[,]” not from “defend[ing] against the action brought by the City that may affect their legal and pecuniary interests”).

Unsurprisingly, Ambac has not located a single decision in which a court found a no-action provision precluded a creditor from intervening as a defendant in a third-party attack on the intervenor’s collateral. As the court stated in *Feldbaum* (applying New York law), “[t]he primary purpose of a no-action clause is . . . to protect issuers from the expense involved in defending lawsuits that are either frivolous or otherwise not in the economic interest of the corporation and its creditors.” 1992 WL 119095, at \*6. If anything, Ambac is *minimizing* the expense caused by Plaintiffs’ collateral attack on COFINA, and it is clearly in the economic interest of COFINA and its creditors to preserve COFINA’s sole revenue stream. For this reason as well, the Resolution’s no-action provision does not apply to the Motion to Intervene.

### **III. The COFINA Claims Should Be Stayed.**

*Arising Under PROMESA.* Plaintiffs argue that a claim arising under PROMESA is necessarily exempt from the stay. (Opp’n at 11-12.) This argument is contradicted by Section 407 of PROMESA—the sole provision creating a private right of action for challenging transfers by the Commonwealth. Section 407(b) provides that such claims can be brought only “after the expiration or lifting of the stay of Section 405.” Thus, Section 407 reflects Congress’s determination that private challenges to post-PROMESA transfers are subject to the stay. By contrast, Section 303 does not provide a private right of action at all, much less a means to evade Section 407’s prescription that challenges to post-PROMESA transfers are stayed.<sup>6</sup>

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<sup>6</sup> Nor do Sections 204(c)(3) and 207 authorize a private right of action. Section 204(c)(3) provides only that certain laws “may be subject to review and rescission by the Oversight Board,” while Section 207 provides for Oversight Board approval of any debt transactions by the Commonwealth. Thus, Sections 204(c)(3) and 207 reinforce the fact that the sole private right of action created by PROMESA arises under Section 407.

Plaintiffs’ contention that any challenge to an executive order advanced under Section 303(3) is not stayed would read the stay out of existence. If Plaintiffs were correct, then virtually every creditor lawsuit that has been stayed could immediately be resuscitated by refiling constitutional claims as Section 303(3) claims. At least nine of the creditor lawsuits pending before this Court challenge as unlawful various executive orders issued by the Governor.<sup>7</sup> On Plaintiffs’ reading, so long as these plaintiffs use the magic words “unlawful executive orders” and “303(3),” the stay is inapplicable. Not only does this reading exalt form over substance, it threatens to unleash the very “cascade” of litigation this Court recently warned about. *See* Brigade Order at 40-42 (noting risk of “provoking a massive ‘wave of litigation’ by other creditors who are eager to obtain relief outside the PROMESA process”). Even plaintiffs (such as Ambac) who believe that the stay should be given a chance to foster necessary reforms could find themselves compelled to revive their claims if the COFINA Claims were allowed to proceed, lest they find themselves unfairly disadvantaged.<sup>8</sup>

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<sup>7</sup> *See Assured Guar. Corp. v. García-Padilla*, Civ. No. 16-1037 (D.P.R.) (filed Jan. 7, 2016) (challenging Executive Orders 2015-46 and 2015-49); *Fin. Guar. Ins. Corp. v. García-Padilla*, Civ. No. 16-1095 (D.P.R.) (filed Jan. 19, 2016) (challenging Executive Orders 2015-46 and 2015-49); *Nat’l Pub. Fin. Corp. v. García-Padilla*, Civ. No. 16-2101 (D.P.R.) (filed June 15, 2016) (challenging Executive Orders 2016-10, 2016-14, and 2016-18); *Trigo-Gonzalez v. García-Padilla*, Civ. No. 16-2257 (D.P.R.) (filed June 30, 2016) (challenging Executive Orders 2016-10, 2016-14, and 2016-2027); *Peaje Investments LLC v. García-Padilla*, Civ. No. 16-2365 (D.P.R.) (filed July 18, 2016) (challenging Executive Orders 2015-46, 2015-49, 2016-18, 2016-30, and 2016-31); *Assured Guar. Corp. v. Commonwealth of Puerto Rico*, Civ. No. 16-2384 (D.P.R.) (filed July 21, 2016) (challenging Executive Orders 2016-18, 2016-30, and 2016-31); *U.S. Bank Trust Nat’l Ass’n v. Commonwealth of Puerto Rico*, Civ. No. 16-2510 (D.P.R.) (filed Aug. 19, 2016) (challenging Executive Order 2016-31); *Altair Global Credit Opportunities Fund (A) L.L.C. v. García-Padilla*, Civ. No. 16-2696 (D.P.R.) (filed Sept. 21, 2016) (challenging Executive Order 2016-31); and *Scotiabank de Puerto Rico v. García-Padilla*, Civ. No. 16-2736 (D.P.R.) (filed Sept. 28, 2016) (challenging Executive Order 2016-30).

<sup>8</sup> Plaintiffs’ policy argument that immediate adjudication of the COFINA Claims would “promote voluntary negotiations with the Commonwealth” proves too much. (Opp’n at 12.) By that logic, resolution of numerous important legal questions—including Ambac’s constitutional challenge to the Governor’s “clawback” orders—should likewise promote negotiations. *See Assured Guar. Corp. v. García-Padilla*, Civ. No. 16-1037 (D.P.R.). Plaintiffs offer no reason why COFINA should be treated differently, nor is there any evidence that Congress intended such preferential treatment. Indeed, it would be manifestly unfair—and thus counterproductive to the negotiating environment—for the Court to resolve certain legal issues while delaying the resolution of others.

**Post-PROMESA Conduct.** Plaintiffs further contend that, although the COFINA Claims “implicate[] the constitutional validity of the Commonwealth’s assignment of SUT revenues to COFINA,” the COFINA Claims nonetheless challenge post-PROMESA conduct because “the legal injury plaintiffs seek to remedy here stems from [the June 30] Executive Order.” (Opp’n at 12.) If that were true, however, then the invalidation of the June 30 Executive Order should remedy the injury. But a declaratory judgment invalidating the June 30 Executive Order would have *no effect whatsoever* on the transfer of the SUT to COFINA for the simple reason that it is not the cause of that transfer. It was another government act entirely—COFINA’s 2006 enabling legislation—that transferred the SUT to COFINA. Thus, even if the June 30 Executive Order were struck down, the flow of SUT revenues to COFINA would continue unabated.

It is for this reason that Plaintiffs seek more than invalidation of the June 30 Executive Order; they also seek a declaration that the SUT proceeds are “available revenues” under the Puerto Rico Constitution and that GO debt must be paid in advance of COFINA debt, as well as an injunction prohibiting the transfer of the SUT to COFINA and directing the SUT to the Commonwealth Treasury. (SAC, Prayer for Relief, at 67-68.) Of course, there is no basis for the Court to award such relief unless the legislation requiring the transfers at issue is also declared invalid. Thus, it is disingenuous<sup>9</sup> for Plaintiffs to contend that the target of the COFINA Claims is limited to the June 30 Executive Order; they plainly seek a much bigger

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<sup>9</sup> Plaintiffs complain that Ambac is “recharacteriz[ing] plaintiffs’ claim under PROMESA as something else—namely, a challenge under the Puerto Rico Constitution to Act No. 56, the legislation that purported to assign SUT revenues to COFINA in 2007.” (Opp’n at 3.) But as Plaintiffs stated forthrightly in their Opposition to COFINA Senior Bondholders’ Motion for Leave to Intervene, “plaintiffs have alleged that Act No. 56—the Commonwealth statute purporting to assign SUT revenues to COFINA—is inconsistent with the Puerto Rico Constitution.” (Dkt. No. 87, at 12; *see also id.* at 13 (“[W]hether the Commonwealth has validly assigned SUT revenues to COFINA and insulated them from the Constitutional Debt’s constitutional lien and first-priority claim is a highly dubious proposition *that is directly at issue in this case.*”) (emphasis added).) That Plaintiffs decided to remove these statements from their Opposition to Ambac’s Motion to Intervene—which is for the most part identical to their opposition to the COFINA senior bondholders’ intervention motion—does not make the candor any less noteworthy.

prize—the invalidation of the COFINA structure itself—which can be accomplished only by striking down the decade-old statute establishing that structure. Indisputably, these attacks on the COFINA structure could have been brought long before PROMESA was enacted.<sup>10</sup>

Finally, even if the stay were deemed inapplicable, the canon of constitutional avoidance would counsel against adjudication of the COFINA Claims at this time. Plaintiffs openly acknowledge that the COFINA Claims “implicate the constitutional validity of the Commonwealth’s assignment of SUT revenues to COFINA.” (Opp’n at 12.) As in *Brigade*, “the passage of PROMESA and the establishment of the Oversight Board creates the distinct possibility that any ruling by the Court regarding the constitutionality of the Moratorium Act and its related Executive Orders”—including the June 30 Executive Order—“will become moot.” *Brigade* Order at 48. Thus, here as in *Brigade*, the Court should “avoid reaching constitutional questions in advance of the necessity of deciding them.” *Id.* at 49 (quoting *Lyng v. Nw. Indian Cemetery Protective Ass’n*, 485 U.S. 439, 445 (1988)).<sup>11</sup>

### CONCLUSION

For the foregoing reasons, Ambac respectfully requests that the Court enter an Order (a) granting Ambac leave to intervene as a defendant in this action, and (b) declaring that the COFINA Claims are stayed by PROMESA.

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<sup>10</sup> Plaintiffs suggest that the COFINA Claims could not have been commenced prior to PROMESA’s enactment because Plaintiffs would have lacked standing before the June 30 Executive Order imposed a moratorium on payment of GO debt. (Opp’n at 14 n.11.) This Court has already found otherwise. *See Peaje Investments LLC v. García-Padilla*, Civ. No. 16-2365 (D.P.R.) (Dkt. No. 74) (bondholders of Puerto Rico Highways and Transportation Authority have standing to move to lift stay despite lack of actual payment default or likely payment default during pendency of stay).

<sup>11</sup> Relatedly, Plaintiffs’ improper attempt to litigate the merits of their COFINA Claims in the context of an intervention motion—before the Court has ruled on whether the COFINA Claims may be prosecuted at this time—should also be rejected. (*See* Opp’n at 12-14.) As noted in the Motion to Intervene (at 5 n.3), should it prove necessary, Ambac will address in detail the merits of the COFINA Claims at the procedurally appropriate time, including by way of a motion under Rule 12.

**RESPECTFULLY SUBMITTED.**

In San Juan, Puerto Rico, this 29th day of November, 2016.

FERRAIUOLI LLC

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**EXHIBIT A**

**PROPOSED ANSWER-IN-INTERVENTION**

**IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF PUERTO RICO**

LEX CLAIMS, LLC, et al.,

Plaintiffs,

v.

THE COMMONWEALTH OF PUERTO RICO, et al.,

Defendants,

AMBAC ASSURANCE CORPORATION,

Proposed Intervenor-Defendant.

Case No. 3:16-cv-02374 (FAB)

**PROPOSED INTERVENOR-DEFENDANT’S ANSWER AND AFFIRMATIVE  
DEFENSES TO SECOND AMENDED COMPLAINT**

Proposed Intervenor-Defendant Ambac Assurance Corporation (“Ambac”), by and through its attorneys, Ferraiuoli LLC and Milbank, Tweed, Hadley & McCloy LLP, hereby answers and responds to Plaintiffs’ Second Amended Complaint (“SAC”). Any allegation in the SAC that is not expressly admitted is denied.

1. Ambac states that Paragraph 1 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required. Ambac respectfully refers the Court to Section 204 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

2. Ambac states that Paragraph 2 sets forth legal conclusions to which no response is required, and denies all allegations in Paragraph 2 that relate to COFINA, any bonds issued by COFINA, any holders of bonds issues by COFINA, the Puerto Rico’s sales and use tax (“SUT”) revenues allocated to COFINA, and COFINA’s right to such SUT revenues. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations of Paragraph 2.

3. Ambac states that Paragraph 3 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 204 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

4. Ambac states that Paragraph 4 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 207 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

5. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 5 concerning Plaintiffs' beneficial ownership of bonds, and otherwise states that Paragraph 5 sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to Sections 204 and 207 of PROMESA and Article VI of the Puerto Rico Constitution, which speak for themselves, regarding their complete and accurate contents.

6. Ambac states that Paragraph 6 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI, Section 8 of the Puerto Rico Constitution and Exhibit A to the SAC, which speak for themselves, regarding their complete and accurate contents.

7. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 7, and respectfully refers the Court to Exhibits B and C to the SAC, which speak for themselves, regarding their complete and accurate contents.

8. Ambac states that Paragraph 8 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 204(c)(3) of PROMESA, which speaks for itself, regarding its complete and accurate contents.

9. Ambac admits that the Executive Order was issued, but states that the remainder of Paragraph 9 sets forth legal conclusions to which no response is required. Ambac respectfully

refers the Court to Exhibits D and E to the SAC, which speak for themselves, regarding their complete and accurate contents.

10. Ambac admits that Puerto Rico enacted a budget for Fiscal Year 2017, but states that the remainder of Paragraph 10 sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Fiscal Year 2017 budget, which speaks for itself, regarding its complete and accurate contents.

11. Ambac states that Paragraph 11 sets forth legal conclusions to which no response is required, and otherwise lacks knowledge or information sufficient to form a belief as to the truth of the allegations set forth in Paragraph 11.

12. Ambac states that Paragraph 12 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Sections 204(c)(3) and 207 of PROMESA, which speak for themselves, regarding their complete and accurate contents.

13. Ambac states that Paragraph 13 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required. Ambac respectfully refers the Court to Section 303 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

14. Ambac states that Paragraph 14 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Sections 5(19), 5(20), and 303(3) of PROMESA, which speak for themselves, regarding their complete and accurate contents

15. Ambac denies the third sentence of Paragraph 15, and otherwise states that Paragraph 15 sets forth legal conclusions to which no response is required.

16. Ambac states that Paragraph 16 sets forth legal conclusions to which no response is required.

17. Ambac admits that Governor Padilla issued the Executive Order, but lacks knowledge or information sufficient to form a belief as to the truth of when the Executive Order was issued. Ambac states that the remaining allegations set forth legal conclusions to which no response is required, and respectfully refers the Court to the Executive Order, which speaks for itself, regarding its complete and accurate contents.

18. Ambac denies the allegations of Paragraph 18.

19. Ambac states that Paragraph 19 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution and cited laws, which speak for themselves, regarding their complete and accurate contents.

20. Ambac states that Paragraph 20 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 303(3) of PROMESA, the Executive Order, and Puerto Rico Constitution, which speak for themselves, regarding their complete and accurate contents.

21. Ambac states that Paragraph 21 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 303(1) of PROMESA, which speaks for itself, regarding its complete and accurate contents.

22. Paragraph 22 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required.

23. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 23.

24. Ambac admits the allegations of Paragraph 24.

25. Ambac admits the allegations of Paragraph 25, except for Footnote 1, which sets forth legal conclusions to which no response is required.

26. Ambac admits the allegations of Paragraph 26.

27. Ambac admits the allegations of the first sentence of Paragraph 27, but states that the remainder of Paragraph 27 sets forth legal conclusions to which no response is required.

28. Ambac denies the allegations of Paragraph 28.

29. Ambac admits the allegations of Paragraph 29.

30. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 30.

31. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the first sentence of Paragraph 31, but admits the allegations in the second sentence of Paragraph 31.

32. Ambac denies the allegations of Paragraph 32.

33. Ambac states that Paragraph 33 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required. Ambac respectfully refers the Court to PROMESA, the United States and Puerto Rico Constitutions, and the U.S. Code, which speak for themselves, regarding their complete and accurate contents.

34. Ambac states that Paragraph 34 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 106(a) of PROMESA, which speaks for itself, regarding its complete and accurate contents.

35. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 35.

36. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 36.

37. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 37.

38. Ambac admits that Congress passed PROMESA and that PROMESA was signed into law on June 30, 2016. Ambac states that Paragraph 38 constitutes a characterization of the action, and otherwise sets forth legal conclusions, to which no response is required, and respectfully refers the Court to PROMESA and the Bankruptcy Code, which speak for themselves, regarding their complete and accurate contents.

39. Ambac states that Paragraph 39 sets forth legal conclusions to which no response is required, and respectfully refers the Court to PROMESA, which speaks for itself, regarding its complete and accurate contents.

40. Ambac admits the allegations in the first three sentences of Paragraph 40, but states that the fourth sentence of Paragraph 40 sets forth legal conclusions to which no response is required. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the fifth and six sentences of Paragraph 40.

41. Ambac states that Paragraph 41 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

42. Ambac states that Paragraph 42 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

43. Ambac states that Paragraph 43 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

44. Ambac states that Paragraph 44 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

45. Ambac states that Paragraph 45 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

46. Ambac states that Paragraph 46 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

47. Ambac states that Paragraph 47 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 301 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

48. Ambac states that Paragraph 48 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required.

49. Ambac states that Paragraph 49 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 204 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

50. Ambac states that Paragraph 50 sets forth legal conclusions to which no response is required, and respectfully refers the Court to PROMESA and Article VI of the Puerto Rico Constitution, which speak for themselves, regarding their complete and accurate contents.

51. Ambac states that Paragraph 51 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 204 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

52. Ambac states that Paragraph 52 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 207 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

53. Ambac states that Paragraph 53 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 303 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

54. Ambac states that Paragraph 54 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 303 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

55. Ambac states that Paragraph 55 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 303 of PROMESA and the Executive Order, which speak for themselves, regarding their complete and accurate contents.

56. Ambac states that Paragraph 56 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 303 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

57. Ambac states that Paragraph 57 sets forth legal conclusions to which no response is required, and respectfully refers the Court to PROMESA and the Bankruptcy Code, which speak for themselves, regarding their complete and accurate contents

58. Ambac states that Paragraph 58 sets forth legal conclusions to which no response is required, and respectfully refers the Court to PROMESA, which speaks for itself, regarding its complete and accurate contents.

59. Ambac states that Paragraph 59 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents

60. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the first and second sentences of Paragraph 60. Ambac states that the third sentence of Paragraph 60 sets forth legal conclusions to which no response is required.

61. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the first, second, and third sentences of Paragraph 61. Ambac states that the first and fourth sentences of Paragraph 60 set forth legal conclusions to which no response is required.

62. Ambac states that the first sentence of Paragraph 62 sets forth legal conclusions to which no response is required, and otherwise lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 62.

63. Ambac states that Paragraph 63 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution and the referenced Official Statement, which speak for themselves, regarding their complete and accurate contents.

64. Ambac states that Paragraph 64 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Public Law 600, the cited Message from the President of the United States, and the Joint Resolution, which speak for themselves, regarding their complete and accurate contents.

65. Ambac states that Paragraph 65 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution and Pub. L. No. 87-121, 75 Stat. 245 (1961), which speak for themselves, regarding their complete and accurate contents.

66. Ambac states that Paragraph 65 sets forth legal conclusions to which no response is required, and respectfully refers the Court to P.R. Laws Ann. tit. 23, § 104(c) and PROMESA, which speak for themselves, regarding their complete and accurate contents.

67. Ambac states that Paragraph 67 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

68. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the first and second sentences of Paragraph 68, and respectfully refers the Court to Exhibits B and C to the SAC, which speak for themselves, regarding their complete and accurate contents. Ambac states that the first and third sentences of Paragraph 68 set forth legal conclusions to which no response is required.

69. Ambac states that Paragraph 69 sets forth legal conclusions to which no response is required.

70. Ambac states that Paragraph 70 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

71. Ambac states that Paragraph 71 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

72. Ambac states that Paragraph 72 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

73. Ambac states that Paragraph 73 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution, PROMESA, and P.R. Laws Ann. tit. 23, § 104(c), which speak for themselves, regarding their complete and accurate contents.

74. Ambac states that the first and fourth sentences of Paragraph 74 set forth legal conclusions to which no response is required, and respectfully refers the Court to Section 204 of PROMESA, which speaks for itself, regarding its complete and accurate contents. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the

second and third sentences of Paragraph 74, and to the extent they set forth legal conclusions, no response is required.

75. Ambac admits that Governor Padilla issued the Executive Order, but lacks knowledge or information sufficient to form a belief as to the truth of when the Executive Order was issued. Ambac respectfully refers the Court to such Executive Order, which speaks for itself, regarding its complete and accurate contents. Ambac states that the remainder of Paragraph 75 sets forth legal conclusions to which no response is required.

76. Ambac states that Paragraph 76 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act and Executive Order, which speak for themselves, regarding their complete and accurate contents.

77. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations concerning the existence of money available to Puerto Rico on July 1, 2016, and the purposes for which such money could or should have been used. Ambac respectfully refers the Court to Exhibit D, which speaks for itself, regarding its complete and accurate contents, and states that the remainder of Paragraph 77 sets forth legal conclusions to which no response is required.

78. Ambac states that the fifth sentence of Paragraph 78 sets forth legal conclusions to which no response is required. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations of Paragraph 78, and respectfully refers the Court to Exhibits D and F to the SAC, which speak for themselves, regarding their complete and accurate contents.

79. Ambac states that the third and fourth sentences of Paragraph 79 set forth legal conclusions to which no response is required, and that Ambac lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations of Paragraph 79. Ambac

respectfully refers the Court to the Puerto Rico Constitution, P.R. Laws Ann. tit. 23, § 104(c), and Section 204 of PROMESA, which speak for themselves, regarding their complete and accurate contents.

80. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 80, and respectfully refers the Court to the Fiscal Year 2016 budget and P.R. Laws Ann. tit. 23, § 104(d)(1), which speak for themselves, regarding their complete and accurate contents.

81. Ambac states that Paragraph 81 sets forth legal conclusions to which no response is required. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the second sentence of Paragraph 81, and respectfully refers the Court to Section 204(c)(3) of PROMESA and the Fiscal Year 2017 budget, which speak for themselves, regarding their complete and accurate contents.

82. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 82, except to the extent Paragraph 82 sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Fiscal Year 2017 Budget, which speaks for itself, regarding its complete and accurate contents.

83. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 83, except to the extent Paragraph 83 sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

84. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 84, and respectfully refers the Court to the Fiscal Year 2017 budget, which speaks for itself, regarding its complete and accurate contents.

85. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of the first sentence of Paragraph 85, and states that the remaining allegations set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Puerto Rico Constitution and laws, which speak for themselves, regarding their complete and accurate contents.

86. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 86, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Fiscal Year 2017 budget, PROMESA, the Puerto Rico Constitution and related laws of Puerto Rico, which speak for themselves, regarding their complete and accurate contents.

87. Ambac states that Paragraph 87 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution, PROMESA, and Act No. 74-2016, which speak for themselves, regarding their complete and accurate contents.

88. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of the Paragraph 88, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Puerto Rico Constitution and Act No. 74-2016, which speak for themselves, regarding their complete and accurate contents.

89. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of the Paragraph 89. Ambac respectfully refers the Court to Act No. 74-2016, which speaks for itself, regarding its complete and accurate contents.

90. Ambac states that Paragraph 90 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution, PROMESA, and Act No. 74-2016, which speak for themselves, regarding their complete and accurate contents.

91. Ambac admits that the Governor promulgated the Executive Order, but otherwise lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations of Paragraph 91. Ambac respectfully refers the Court to Exhibit E, which speaks for itself, regarding its complete and accurate contents.

92. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the first sentence of Paragraph 92, and respectfully refers the Court to Exhibit C, which speaks for itself, regarding its complete and accurate contents. Ambac denies the allegations in the second sentence of Paragraph 92, and respectfully refers the Court to the Executive Order, which speaks for itself, regarding its complete and accurate contents. Ambac admits the allegations in the third sentence of Paragraph 92. Ambac denies the fourth sentence of Paragraph 92. Ambac states that the fifth sentence of Paragraph 92 sets forth legal conclusions to which no response is required, and otherwise denies the allegations of the fifth sentence of Paragraph 92.

93. Ambac states that Paragraph 93 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the cited Puerto Rico laws, which speak for themselves, regarding their complete and accurate contents.

94. Ambac denies the allegations of Paragraph 94.

95. Ambac states that Paragraph 95 sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Puerto Rico Constitution and Act No. 56-2007, which speak for themselves, regarding their complete and accurate contents.

96. Ambac states that Paragraph 96 sets forth legal conclusions to which no response is required, and Ambac lacks knowledge or information sufficient to form a belief as to the total amount of COFINA debt issued or currently outstanding.

97. Ambac denies the allegations in the first sentence of Paragraph 97. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations of Paragraph 97, and respectfully refers the Court to the cited Official Statement, which speaks for itself, regarding its complete and accurate contents.

98. Ambac states that Paragraph 98 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution and Act No. 56-2007, which speak for themselves, regarding their complete and accurate contents.

99. Ambac states that Paragraph 99 sets forth legal conclusions to which no response is required.

100. Ambac states that Paragraph 100, including Footnotes 2-4, sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the cited Puerto Rico laws, Official Statement, and Distribution of Monthly Collection, which speak for themselves, regarding their complete and accurate contents.

101. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 101, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the cited Puerto Rico laws, which speak for themselves, regarding their complete and accurate contents.

102. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 102, except to the extent that they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Puerto Rico Constitution and the cited Puerto Rico law, which speak for themselves, regarding their complete and accurate contents.

103. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 103, except to the extent that they set forth legal conclusions to

which no response is required. Ambac respectfully refers the Court to the cited Puerto Rico laws, which speak for themselves, regarding their complete and accurate contents.

104. Ambac states that Paragraph 104 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution and Puerto Rico laws, which speak for themselves, regarding their complete and accurate contents.

105. Ambac denies the allegations in the first four sentences of Paragraph 105, and states that the last sentence sets forth legal conclusions to which no response is required.

106. Ambac states that Paragraph 106 sets forth legal conclusions to which no response is required, and respectfully refers the Court to COFINA's enabling statutes, which speak for themselves, regarding their complete and accurate contents.

107. Ambac states that Paragraph 107 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

108. Ambac states that Paragraph 108 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Executive Order and Article VI of the Puerto Rico Constitution, which speak for themselves, regarding their complete and accurate contents.

109. Ambac states that Paragraph 109 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Executive Order and the Puerto Rico Constitution, which speak for themselves, regarding their complete and accurate contents.

110. Ambac states that Paragraph 110 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Executive Order, the Puerto Rico Constitution, and Section 303 of PROMESA, which speak for themselves, regarding their complete and accurate contents.

111. Ambac states that Paragraph 111 sets forth legal conclusions to which no response is required.

112. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 112, and respectfully refers the Court to the 2014 GO Bond Resolution, which speaks for itself, regarding its complete and accurate contents.

113. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 113, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the 2014 GO Bond Resolution, which speaks for itself, regarding its complete and accurate contents

114. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 114, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the 2014 GO Bond Resolution, which speaks for itself, regarding its complete and accurate contents.

115. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 115, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the 2014 GO Bond Resolution, which speaks for itself, regarding its complete and accurate contents.

116. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 116, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the 2014 GO Bond Resolution, which speaks for itself, regarding its complete and accurate contents.

117. Ambac states that Paragraph 117 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the 2014 GO Bond Resolution and prior

GO Bond Resolutions, which speak for themselves, regarding their complete and accurate contents.

118. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 118, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the 2012 GO Bonds and the 2012 GO Bond Resolution, which speak for themselves, regarding their complete and accurate contents.

119. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 119, except to the extent they set forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the 2012 and 2014 GO Bond Resolutions, and P.R. Laws Ann. tit. 13, § 41, which speak for themselves, regarding their complete and accurate contents.

120. Ambac states that Paragraph 120 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Series 2006 PRIFA Special Tax Revenue Bonds Official Statement, which speaks for itself, regarding its complete and accurate contents.

121. Ambac states that Paragraph 121 sets forth legal conclusions to which no response is required.

122. Ambac states that Paragraph 122 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act and Executive Order, which speak for themselves, regarding their complete and accurate contents.

123. Ambac states that Paragraph 123 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act and Executive Order, which speak for themselves, regarding their complete and accurate contents.

124. Ambac states that Paragraph 124 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act and Executive Order, which speak for themselves, regarding their complete and accurate contents.

125. Ambac states that Paragraph 125 sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Moratorium Act and Executive Order, which speak for themselves, regarding their complete and accurate contents.

**Plaintiffs' First Cause of Action**

126. Ambac repeats its responses and answers to Paragraphs 1-125 above.

127. Ambac states that Paragraph 127 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required. Ambac respectfully refers the Court to the Declaratory Judgment Act, and Sections 204 and 207 of PROMESA, which speak for themselves, regarding their complete and accurate contents.

128. Ambac states that Paragraph 128 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 204 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

129. Ambac states that Paragraph 129 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 207 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

130. Ambac states that Paragraph 130 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution and Sections 204 and 207 of PROMESA, which speak for themselves, regarding their complete and accurate contents.

131. Ambac states that Paragraph 131 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 204 of PROMESA, which

speaks for itself, regarding its complete and accurate contents. To the extent a response is required, Ambac denies the allegations of Paragraph 131.

132. Ambac states that Paragraph 132 sets forth legal conclusions to which no response is required, except to the extent that the second sentence constitutes a characterization of the action to which no response is required. Ambac respectfully refers the Court to PROMESA and the Puerto Rico Constitution and laws, which speak for themselves, regarding their complete and accurate contents.

133. Ambac denies the second sentence of Paragraph 133, and states that the remaining allegations of Paragraph 133, including all its subparts, constitute a characterization of the action to which no response is required.

134. Ambac states that Paragraph 134 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required.

**Plaintiffs' Second Cause of Action**

135. Ambac repeats its responses and answers to Paragraphs 1-134 above.

136. Paragraph 136 constitutes a characterization of the action to which no response is required.

137. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 137.

138. Ambac states that Paragraph 138 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 138.

139. Ambac states that Paragraph 139 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 139.

140. Ambac states that Paragraph 140 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 140.

141. Ambac states that Paragraph 141 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 141.

142. Ambac states that Paragraph 142 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 142.

143. Ambac states that Paragraph 143 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 143.

144. Ambac states that Paragraph 144 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 144.

**Plaintiffs' Third Cause of Action**

145. Ambac repeats its responses and answers to Paragraphs 1-144 above.

146. Ambac states that the first two sentences of Paragraph 146 set forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act and 11 U.S.C. 109, which speak for themselves, regarding their complete and accurate contents. Ambac lacks knowledge or information sufficient to form a belief as to the remainder of the allegations in Paragraph 146.

147. Ambac states that Paragraph 147 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act and Section 303 of PROMESA, which speak for themselves, regarding their complete and accurate contents.

148. Ambac states that Paragraph 148 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Section 303 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

149. Ambac states that Paragraph 149 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act, which speaks for itself, regarding its complete and accurate contents.

150. Ambac states that Paragraph 150 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 150.

**Plaintiffs' Fourth Cause of Action**

151. Ambac repeats its responses and answers to Paragraphs 1-150 above.

152. Ambac states that Paragraph 152 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

153. Ambac states that Paragraph 153 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 153.

154. Ambac states that Paragraph 154 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution, the Executive Order, and the Moratorium Act, which speak for themselves, regarding their complete and accurate contents.

155. Ambac states that Paragraph 155 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

156. Ambac states that Paragraph 156 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 156.

157. Ambac states that Paragraph 157 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution and Moratorium Act, which speak for themselves, regarding their complete and accurate contents.

**Plaintiffs' Fifth Cause of Action**

158. Ambac repeats its responses and answers to Paragraphs 1-157 above.

159. Ambac states that Paragraph 159 sets forth legal conclusions to which no response is required, and respectfully refers the Court to Article VI of the Puerto Rico Constitution, which speaks for itself, regarding its complete and accurate contents.

160. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 160, and respectfully refers the Court to Act No. 56-2007, which speaks for itself, regarding its complete and accurate contents.

161. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the first two sentences of Paragraph 161. Ambac states that the third sentence of Paragraph 161 sets forth a legal conclusion to which no response is required. To the extent a response is required, Ambac denies the allegations in the third sentence of Paragraph 161.

162. Ambac states that Paragraph 162 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 162.

**Plaintiffs' Sixth Cause of Action**

163. Ambac repeats its responses and answers to Paragraphs 1-162 above.

164. Ambac states that Paragraph 164 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the United States and Puerto Rico Constitutions, and the case cited in Paragraph 164, regarding their complete and accurate contents. To the extent a response is required, Ambac denies the allegations of Paragraph 164.

165. Ambac states that the first three sentences of Paragraph 165 set forth legal conclusions to which no response is required, and respectfully refers the Court to the Moratorium Act, the Executive Order, and the Puerto Rico Constitution, which speak for themselves, regarding their complete and accurate contents. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations of Paragraph 165.

166. Ambac states that Paragraph 166 sets forth legal conclusions to which no response is required, and Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 166.

167. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 167, except with respect to Footnote 5, which sets forth legal conclusions to which no response is required. Ambac respectfully refers the Court to the Press Release, which speaks for itself, regarding its complete and accurate contents.

168. Ambac denies the allegations in the first, second, fourth, and sixth sentences of Paragraph 168, and lacks knowledge or information sufficient to form a belief as to the truth of

the allegations in the third and fifth sentences. Ambac respectfully refers the Court to the cited Distribution of Monthly Collection, Press Releases, and United States and Puerto Rico Constitutions, which speaks for themselves, regarding their complete and accurate contents.

169. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 169, and respectfully refers the Court refer to the Fiscal Year 2017 budget and cited KPMG report, which speak for themselves, regarding their complete and accurate contents.

170. Ambac denies the allegations of Paragraph 170.

171. Ambac denies the allegations of Paragraph 171.

172. Ambac states that Paragraph 172 sets forth legal conclusions to which no response is required. To the extent a response is required, Ambac denies the allegations of Paragraph 172.

**Plaintiffs' Seventh Cause of Action**

173. Ambac repeats its responses and answers to Paragraphs 1-172 above.

174. Ambac states that Paragraph 174 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico and United States Constitutions, which speak for themselves, regarding their complete and accurate contents.

**Plaintiffs' Eighth Cause of Action**

175. Ambac repeats its responses and answers to Paragraphs 1-174 above.

176. Ambac states that Paragraph 176 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the United States Constitution, which speaks for itself, regarding its complete and accurate contents.

177. Ambac states that Paragraph 177 sets forth legal conclusions to which no response is required, except to the extent that Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations regarding Plaintiffs' ownership of bonds.

178. Ambac states that Paragraph 178 sets forth legal conclusions to which no response is required, except to the extent Ambac lacks knowledge or information sufficient to form a belief as to the truth regarding Plaintiffs' ownership of bonds and expectations related thereto. Ambac respectfully refers the Court to the United States and Puerto Rico Constitutions, which speak for themselves, regarding their complete and accurate contents.

179. Ambac states that Paragraph 179 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the Puerto Rico Constitution, the Executive Order, and the Moratorium Act, which speak for themselves, regarding their complete and accurate contents.

180. Ambac states that Paragraph 180 sets forth legal conclusions to which no response is required.

**Plaintiffs' Ninth Cause of Action**

181. Ambac repeats its responses and answers to Paragraphs 1-180 above.

182. Ambac states that Paragraph 182 sets forth legal conclusions to which no response is required, and respectfully refers the Court to the United States and Puerto Rico Constitutions, which speak for themselves, regarding their complete and accurate contents.

**Plaintiffs' Tenth Cause of Action**

183. Ambac repeats its responses and answers to Paragraphs 1-182 above.

184. Ambac does not seek to intervene with respect to Plaintiffs' Tenth Cause of Action. Accordingly, Ambac has no obligation to respond to the allegations of Paragraph 184.

185. Ambac does not seek to intervene with respect to Plaintiffs' Tenth Cause of Action. Accordingly, Ambac has no obligation to respond to the allegations of Paragraph 185.

**Plaintiffs' Eleventh Cause of Action**

186. Ambac repeats its responses and answers to Paragraphs 1-185 above.

187. Ambac does not seek to intervene with respect to Plaintiffs' Eleventh Cause of Action. Accordingly, Ambac has no obligation to respond to the allegations of Paragraph 187.

188. Ambac does not seek to intervene with respect to Plaintiffs' Eleventh Cause of Action. Accordingly, Ambac has no obligation to respond to the allegations of Paragraph 188.

189. Ambac does not seek to intervene with respect to Plaintiffs' Eleventh Cause of Action. Accordingly, Ambac has no obligation to respond to the allegations of Paragraph 189.

190. Ambac does not seek to intervene with respect to Plaintiffs' Eleventh Cause of Action. Accordingly, Ambac has no obligation to respond to the allegations of Paragraph 190.

**Plaintiffs' Twelfth Cause of Action**

191. Ambac repeats its responses and answers to Paragraphs 1-190 above.

192. Ambac states that Paragraph 192 sets forth legal conclusions to which no response is required, and respectfully refers the Court to 42 U.S.C. § 1983, which speaks for itself, regarding its complete and accurate contents.

193. Ambac states that Paragraph 193 sets forth legal conclusions to which no response is required, and Ambac respectfully refers the Court to the United States and Puerto Rico Constitutions, PROMESA and other the laws of the United States, Puerto Rico statutes, ordinances, regulations, customs and usages of the Commonwealth, which speak for themselves, regarding their complete and accurate contents.

**Plaintiffs' Thirteenth Cause of Action**

194. Ambac repeats its responses and answers to Paragraphs 1-193 above.

195. Ambac states that Paragraph 195 constitutes a characterization of the action, and/or sets forth legal conclusions, to which no response is required.

196. Ambac states that Paragraph 196 purports to state legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

197. Ambac states that Paragraph 197 purports to state legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

198. Ambac lacks knowledge or information sufficient to form a belief as to the truth of the allegations of Paragraph 198 concerning Plaintiffs' interests. Ambac states that the remaining allegations of Paragraph 198 set forth legal conclusions to which no response is required, and respectfully refers the Court to Section 405 of PROMESA, which speaks for itself, regarding its complete and accurate contents.

199. Ambac states that Paragraph 199 constitutes a characterization of the action, and/or purports to state legal conclusions, to which no response is required.

Ambac further denies every allegation not specifically admitted or otherwise responded to above, including every heading and subheading to the extent they contain substantive allegations. With respect to Plaintiffs Prayer for Relief, Ambac denies that Plaintiffs are entitled to any relief or to a judgment in their favor.

#### **AFFIRMATIVE DEFENSES**

Ambac asserts the following affirmative defenses and reserves the right to assert others when and if they become appropriate, known, or available in this action. The statement of any affirmative defense below does not assume the burden of proof as to which applicable law places the burden on Plaintiffs:

**First Affirmative Defense**

Plaintiffs fail to state a claim upon which relief can be granted.

**Second Affirmative Defense**

Plaintiffs lack standing because they have not suffered irreparable harm.

**Third Affirmative Defense**

Plaintiffs' claims are time-barred by statutes of limitation and/or the doctrine of laches.

**Fourth Affirmative Defense**

Plaintiffs' claims are barred by the doctrine of estoppel.

**Fifth Affirmative Defense**

Plaintiffs' claims are barred by the doctrines of waiver, release, acquiescence, or ratification.

**Sixth Affirmative Defense**

Plaintiffs' claims are barred by the doctrine of unclean hands.

**Seventh Affirmative Defense**

Plaintiffs' claims are barred by the doctrine of marshaling.

**Eighth Affirmative Defense**

Plaintiffs are not entitled to equitable relief because they have an adequate remedy at law.

**Ninth Affirmative Defense**

Plaintiffs' claims are barred because they failed to mitigate their harm.

**Tenth Affirmative Defense**

Plaintiffs' claims are barred because they are contrary to public policy.

\* \* \*

WHEREFORE, Ambac demands judgment dismissing the SAC and this action with prejudice, and awarding such other and further relief as the Court deems just and proper.

**RESPECTFULLY SUBMITTED.**

In San Juan, Puerto Rico, this [\_\_] day of [\_\_\_\_\_], 2016.

FERRAIUOLI LLC

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**EXHIBIT B**

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF MICHIGAN  
SOUTHERN DIVISION

In re:  
City of Detroit, Michigan,  
Debtor.

Chapter 9  
Case No. 13-53846  
Hon. Steven W. Rhodes

\_\_\_\_\_  
City of Detroit, Michigan,  
Plaintiff,

v.

Adv. Pro. No. 14-04112

Detroit General Retirement System Service  
Corporation, et al.,  
Defendants.  
\_\_\_\_\_

**Opinion and Order**  
**(1) Denying Motion to Dismiss Filed by Defendants**  
**Detroit General Retirement System Service Corporation and**  
**Detroit Police and Fire Retirement System Service Corporation**  
**and**  
**(2) Granting Motions to Intervene with Limitations**

Defendants Detroit General Retirement System Service Corporation and Detroit Police and Fire Retirement Systems Service Corporation (collectively, the “Service Corporations”) have filed a motion to dismiss the claims against them in this adversary proceeding.<sup>1</sup> The City filed a response in opposition to the motion.

<sup>1</sup> The Court notes that there is a discrepancy between the relief sought in the original motion (dismissal of the adversary proceeding in its entirety) and the relief requested in subsequent pleadings (dismissal of the claims against the Service Corporations only). *See* Reply in Support of Service Corporations’ Motion to Dismiss, § III at 8 (Dkt. #54); Service Corporations’ Supplemental Brief in Support of Motion to Dismiss at 5. (Dkt. #67) The Court assumes that the relief requested is for dismissal of the claims against the Service Corporations only and this opinion addresses that request.

In addition, Financial Guaranty Insurance Company (“FGIC”) and certain COPs Holders<sup>2</sup> (collectively, the “Intervenors”) have filed motions to intervene, which the City also opposes.

For the reasons stated below, the motion to dismiss is denied and the motions to intervene are granted with limitations.

### **I. Introduction**

By 2005, the City had fallen behind in its constitutional and statutory requirements to make contributions to its two pension systems. At the time, the City did not have sufficient resources to fully fund the pension systems, and the amounts it needed to borrow would have exceeded the debt limits imposed on the City by the Home Rule City Act (“HRCA”), M.C.L. § 117.1.

In an attempt to meet its funding obligations without violating the HRCA, the City entered into a series of complex financial transactions. First, the City created the Service Corporations and entered into contracts with them in which the City agreed to make payments to the Service Corporations (the “City Payments”), for the service of helping the City with its funding obligations to the pension funds (the “Service Contracts”). The Service Corporations then created the defendant Detroit Retirement Systems Funding Trust 2005 and the defendant Detroit Retirement Systems Funding Trust 2006 (collectively, the “Funding Trusts”) to sell certificates of participation (“COPs”) in the City’s payment obligations to the Service Corporations. The proceeds from the sale of the COPs were remitted by the Funding Trusts to the Service Corporations, which in turn remitted the funds to the pension systems to satisfy the unfunded pension obligations of the City. Finally, the Service Corporations assigned their rights to receive the City Payments to the Funding Trusts, which used the payments to pay the COPs

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<sup>2</sup> The COPs Holders joining in the motion to intervene are listed in the Joint Motion of Certificate Holders to Intervene. (Dkt. #12)

Holders the interest and principal they were due. For purposes of this opinion, the Court will refer to the above described transactions collectively as the “COPs Transaction.”

By creating this structure, the City could characterize the payments it made as contractual obligations under the Service Contracts rather than debt service, which would have violated the debt limitations in the HRCA. According to the City, the current outstanding amount owed to COPs Holders is estimated to be approximately \$1.45 billion.

In order to make the COPs marketable to investors, the City sought out monoline insurers, including FGIC, to issue policies guaranteeing the scheduled payments of principal and interest on certain of the COPs. Immediately before filing its petition for relief under chapter 9 of the bankruptcy code, the City stopped making the payments it owed under the Service Contracts, including those that came due on June 17, 2013, September 16, 2013, and December 16, 2013. FGIC has made payments to the COPs Holders under the insurance policies it issued for the amounts that are due and owing by the City.

On January 31, 2014, the City filed this adversary proceeding against the Service Corporations and the Funding Trusts seeking a declaratory judgment that the Service Contracts are void *ab initio* and related injunctive relief.

## **II. The Motion to Dismiss**

### **A.**

The Service Corporations bring their motion to dismiss under Fed. R. Civ. P. 12(b)(1) and 12(b)(6), which are incorporated into bankruptcy adversary proceedings by Fed. R. Bankr. P. 7012(b). In deciding a motion to dismiss, the Court must accept the plaintiff’s allegations as true, and construe the complaint in the light most favorable to the plaintiff. *Davis v. Malatinsky*, No. 12-13761, 2013 WL 6008612, \*2-3 (E.D. Mich. Nov. 13, 2013) (A motion under Rule

12(b)(1) “challenges the court’s subject matter jurisdiction by attacking the claim on its face, in which case all factual allegations of the Plaintiff must be considered as true . . . .”) (citing *DLX, Inc. v. Ky.*, 381 F.3d 511, 516 (6th Cir. 2004));<sup>3</sup> *Benzon v. Morgan Stanley Distribs., Inc.*, 420 F.3d 598, 605 (6th Cir. 2005) (A court considering a 12(b)(6) motion must accept all allegations as true and construe the complaint in the light most favorable to the plaintiff.). Only if the complaint’s factual allegations raise a right to relief above a speculative level will it survive a motion to dismiss. *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 555 (2007); *see also Ashcroft v. Iqbal*, 556 U.S. 662, 663-64 (2009).

In the complaint, the City seeks a declaratory judgment that the Service Contracts are void *ab initio* because they are illegal under Michigan law. The City argues that the Service Contracts are not future service contracts at all but rather a means for the City to create debt that was not authorized under the HRCRA and other state laws. To that end, the City argues that the Service Corporations are shell entities created for the sham purpose of entering into the Service Contracts so that the City’s payments could be characterized as payments for future services by the Service Corporations rather than for debt service.

The Service Corporations argue that the claims asserted against them should be dismissed because the Court does not have subject matter jurisdiction and the City has failed to state a claim against the Service Corporations. They contend that if the City’s allegations are taken as true, the Service Corporations are “shams” and “mere alter-egos” of the City. If the Service Corporations are merely “alter egos” of the City, the Service Corporations claim, then there are

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<sup>3</sup> The Court notes that the cases addressing dismissal under Rule 12(b)(1) identify two separate grounds for dismissal: a facial attack on the pleadings or an attack on the factual basis for jurisdiction which would require the Court to weigh the evidence. *See Malatinsky*, 2013 WL 6008612, at \*2. The Service Corporations assert that their motion to dismiss constitutes a facial attack on the pleadings. Service Corporations’ Supplemental Brief at 1 n.1. (Dkt. #67)

no truly adverse parties here and no “case or controversy” as required for subject matter jurisdiction under Article III of the U.S. Constitution and the Declaratory Judgment Act, 28 U.S.C. § 2201(a). Further, the Service Corporations argue that because they assigned their right to receive the City Payments to the Funding Trusts, they have no interest in the dispute and so there can be no substantial controversy between the City and the Service Corporations.

The City argues that the Service Corporations are necessary parties and inherently adverse to it because they are the counterparties to the Service Contracts. The City further states that it seeks a declaratory judgment that the Service Contracts are void because they are not actually future services contracts but rather a means of obtaining debt in contravention of the HRCA, a declaration, the City contends, that does not rest upon a finding that the Service Corporations are shams.

**B.**

For the reasons set forth below, the Court finds that the motion to dismiss the claims against the Service Corporations must be denied.

The Article III requirement of a “case or controversy” for subject matter jurisdiction has its roots in the need to limit judicial power to “the right to determine actual controversies arising between adverse litigants.” *Muskrat v. United States*, 219 U.S. 346, 361 (1911). The purpose of this limitation is to ensure that the “clash of adverse parties sharpens the presentation of issues upon which the court so largely depends for illumination of difficult . . . questions.” *GTE Sylvania v. Consumers Union of the United States, Inc.*, 445 U.S. 375, 382-3 (1980) (internal quotations omitted).

This adversary proceeding most certainly involves a case or controversy as contemplated by Article III of the U.S. Constitution and the Declaratory Judgment Act, 28 U.S.C. § 2201(a).

The COPs Transaction resulted in an enormous financial obligation for the City and that obligation was a significant factor in later forcing the City into bankruptcy. As part of its restructuring efforts, the City is now attempting to invalidate the COPs Transaction in an effort to relieve itself of that burden.

On the other hand, there are many stakeholders in the COPs Transaction whose substantial pecuniary interest could be severely impaired if the City's obligations under the COPs Transaction are invalidated. Indeed, Wilmington Trust, the trustee of the Funding Trusts (the "Trustee") has filed a lengthy answer to the complaint asserting significant affirmative defenses and counterclaims.

In addition, as noted above, other parties to the COPs Transaction have moved to intervene in this litigation with proposed answers that would vigorously challenge the City's allegations.

Undoubtedly, the parties on either side of this litigation have significant and adverse interests in its outcome such that the issues will be fully presented for the Court to decide. *See GTE Sylvania*, 445 U.S. at 382-3.

Accordingly, this adversary proceeding clearly involves a case or controversy such that the Court has subject matter jurisdiction over the action. The remaining question is whether the City has stated a claim against the Service Corporations.

The fundamental question at issue in this adversary proceeding is the validity of the COPs Transaction. The COPs Transaction is structured such that the only direct contractual obligation the City has is the City Payments due under the Service Contracts. Thus, the Service Contracts are arguably the most important component of the COPs Transaction. Assuming that the allegations in the complaint are true, the Service Corporations are the only counterparties to

the Service Contracts; indeed they are the only parties with whom the City has a direct contractual relationship in the entire framework of the COPs Transaction.<sup>4</sup> Likewise, the Service Corporations have the only direct contractual relationship with the Funding Trusts and the Trustee. In order for the Court to resolve all of the issues relating to the validity of the COPs Transaction, the Service Corporations must be included. In other words, dismissing the Service Corporations may leave the Court unable to accord complete relief among the remaining parties because there is no direct contractual relationship between them.

At this stage in the proceedings, the record does not establish that the Service Corporations have no remaining interest in the Service Contracts. The complaint alleges that the Service Corporations assigned their right to receive the City Payments to the Funding Trusts; however, nowhere in the complaint does the City allege that the Service Corporations assigned *all* of their rights, interests and obligations to the Funding Trusts such that the Court could reasonably consider the Funding Trusts to have displaced the Service Corporations as counterparties to the Service Contracts. *See, e.g., Macomb Interceptor Drain Drainage Dist. v. Kilpatrick*, 896 F. Supp. 2d 650, 658 (E.D. Mich. 2012) (an assignment of a contract right is a contract between the assignor and the assignee); *Keyes v. Scharer*, 165 N.W.2d 498, 501 (Mich. Ct. App. 1969) (assignment of rights does not automatically include assumption of duties). For example, there are several duties of the Service Corporations under the Service Contracts to make payments to third parties, such as insurers, that were not assumed by the Funding Trusts. *See* GRS Service Contract 2005, General Terms and Conditions, §9.09 (May 25, 2005), attached as Exhibit C to the Complaint. In addition, Section 9.10 of the General Terms and Conditions

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<sup>4</sup> The Court notes that the City did assume direct contractual obligations with other entities related to swap agreements designed to hedge against interest rate changes on the payments due to COPs Holders. However, those agreements are not at issue here.

explicitly states that the only permitted assignment under the Service Contracts is that of the right to receive the City Payments specifically. The Court simply cannot conclude, based on the pleadings, that the assignment of the right to receive the City Payments alone requires the conclusion that the Service Corporations have no continuing interest in the Service Contracts or in this adversary proceeding.

Finally, the Court rejects the Service Corporations' argument that the Court lacks subject matter jurisdiction over them, or that the City has failed to state a claim against them because they and the City are the same entity and the City "cannot sue itself." The cases cited by the Service Corporations for this proposition either deal with the same person or entity appearing on both sides of the action, *see Globe & Rutgers Fire Ins. Co. v. Hines*, 273 F. 774, 777-84 (2d Cir. 1921) (insurance company subrogated to owner of plaintiff railroad cannot sue same entity as owner of defendant railroad); *Allen v. Evans*, 64 P. 414, 415 (Ariz. 1901) (representative of one estate cannot sue himself as representative of another estate); *Tate v. Tate*, 227 S.W.2d 50, 52 (Tenn. 1950) (sister of incompetent person cannot sue herself as guardian of incompetent person's estate for support), or address concerns about conflicts of interest, *see Chadd v. Delavan Industries, Inc.*, No. 86-74241, 1987 U.S. Dist. LEXIS 15758, at \*5 (E.D. Mich. May 19, 1987) (subsidiary of defendant is not permitted to intervene as plaintiff where the "intervenor would have an interest in both sides of the tort action"); *Harrison v. Ford Motor Co.*, 122 N.W.2d 680, 681-82 (Mich. 1963) (insurance company is not permitted to intervene as plaintiff when it also insured the defendant).

These concerns are not present here. While the City does allege that the Service Corporations were created for the unlawful purpose of enabling the City to avoid debt limitations imposed by state law, nowhere in the pleadings does the City allege that the Service

Corporations are not distinct and separate legal entities. Further, the Service Corporations have engaged their own independent legal counsel who have filed pleadings and appeared in court for them. For these reasons, the City and the Service Corporations cannot be considered the same entity.

Further, nothing here suggests the same kind of conflict of interest that warranted dismissal in the cases cited by the Service Corporations.

For these reasons, the motion to dismiss the claims against the Service Corporations must be denied.

### **III. The Motions to Intervene**

#### **A.**

The Intervenors argue that they have a right to intervene in this adversary proceeding under Fed. R. Civ. P. 24(a)(2),<sup>5</sup> made applicable to bankruptcy adversary proceedings by Bankruptcy Rule 7024. Rule 24(a)(2) provides in pertinent part:

On timely motion, the court must permit anyone to intervene who . . . claims an interest relating to the property or transaction that is the subject of the action, and is so situated that disposing of the action may as a practical matter impair or impede the movant's ability to protect its interest, unless existing parties adequately represent that interest.

In the Sixth Circuit, intervention under Rule 24(a)(2) is appropriate where:

(1) the motion to intervene is timely; (2) the proposed intervenors have a significant legal interest in the subject matter of the pending litigation; (3) the disposition of the action may impair or impede the proposed intervenors' ability to protect their legal interest; and

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<sup>5</sup> The Intervenors also claim a right to intervene under Fed. R. Civ. P. 24(a)(1) and Section 1109(b) of the Bankruptcy Code. The Court notes that there is a split in the decisions of the courts of appeals on whether 11 U.S.C. § 1109(b) applies in adversary proceedings and the Sixth Circuit has not ruled on this issue. Because the motions should be granted under Rule 24(a)(2), it is not necessary to address the arguments under Rule 24(a)(1) and Section 1109(b) at this time.

(4) the parties to the litigation cannot adequately protect the proposed intervenors' interests.

*Jansen v. City of Cincinnati*, 904 F.2d 336, 340 (6th Cir. 1990). Further, courts in the Sixth Circuit construe these elements broadly in favor of intervention. *Stupak-Thrall v. Glickman*, 226 F.3d 467, 472 (6th Cir. 2000); *Purnell v. Akron*, 925 F.2d 941, 950 (6th Cir. 1991).

**B.**

The Court finds that the motions meet the requirements of intervention as a matter of right under Rule 24(a)(2). Accordingly, the motions are granted, subject to the limitations set forth below.

Specifically, the Court finds as follows:

(1) The motions are timely. They were filed on the same day the Funding Trusts filed their answer to the complaint and the case is clearly in its initial stages. *See Michigan State AFL-CIO v. Miller*, 103 F.3d 1240, 1245 (6th Cir. 1997).

(2) The Intervenor has a significant legal interest in the subject matter of this adversary proceeding. The certificates held by the COPs Holders have a combined value of close to \$1 billion, with each certificate evidencing an individual undivided proportionate legal interest in the right to receive certain payments made by the City under the Service Contracts. FGIC, as an insurer of the COPs, has already made payments under its insurance policies to the COPs Holders and thus has become subrogated to the rights of the COPs Holders to the extent of those payments. Further, FGIC is an express third-party beneficiary under the Service Contracts and could incur further significant financial obligations to the COPs Holders if the Service Contracts are declared void.

(3) The disposition of this action may impair or impede the Intervenor's ability to protect their legal interests. As the court in *Miller* pointed out, an intervenor need only show that

impairment of its legal interest is possible if intervention is denied and that this burden is minimal. *Id.* at 1247. The Intervenor has met that burden here. If the Court were to declare that the Service Contracts are void *ab initio* and the City has no duty to make payments under them, the Intervenor may be precluded from re-litigating that issue in later proceedings to determine their own rights and obligations under the same and related transactional documents. Indeed, in response to these motions to intervene, the City argues that, under Michigan law, bondholders have no right to restitution when they hold debt that was unlawfully issued. City of Detroit's Opposition to Motions to Intervene, at 21 n.8. (Dkt. #19) So, if intervention in this adversary proceeding is denied, the Intervenor could lose rights based on findings in an action in which they were not permitted to take part. This is exactly the type of concern that warrants intervention. *See Smith v. Nitschke (In re Nitschke)*, Bankr. No. 05-74861, Adv. No. 06-3131, 2008 WL 141510, at \*2-3 (Bankr. N.D. Ohio Jan. 11, 2008) (finding insurer could intervene in adversary proceeding because of potential collateral estoppel effect in later proceedings).

(4) The parties to the litigation cannot adequately protect the Intervenor's interests. The City argues that the Trustee, who is also the Contract Administrator under the Contract Administration Agreement ("CAA"), can adequately represent the parties without their intervention. Indeed, the City argues that the Trustee is the only party entitled to defend this action based on the limitations of the so-called "no-action" clause contained in Section 6.8 of the CAA.

The Intervenor's burden of showing inadequate representation is minimal. *Grutter v. Bollinger*, 188 F.3d 394, 400 (6th Cir. 1999). "The proposed intervenors need show only that there is a *potential* for inadequate representation." *Id.* (citing *Trbovich v. United Mine Workers*,

404 U.S. 528, 538 n.10 (1972); *Linton v. Comm'r of Health & Env't*, 973 F.2d 1311, 1319 (6th Cir. 1992)).

The Court finds that the Intervenorors have met that burden here. As the Intervenorors point out, the Trustee's pecuniary interest in the Service Contracts is limited to its general corporate expenses. This is in sharp contrast to the \$1 billion that the Intervenorors have at stake. Further, the Intervenorors suggest that they have defenses unique to them which the Trustee would not be capable of raising. As the Court in *Miller* found, it can be "enough to show that the existing party who purports to seek the same outcome will not make all of the prospective intervenor's arguments." 103 F.3d at 1247. Consequently, the Court finds that the Intervenorors have met the minimal burden of showing that the existing parties may not adequately represent their interests.

Furthermore, the Court concludes that the "no-action" clause in the CAA does not bar the Intervenorors from intervening in this action. The "no-action" clause specifically does not apply to FGIC as an insurer and third party beneficiary under the Service Contracts. CAA § 6.8 ("No *Certificateholder* shall have any right to institute any proceeding . . .") (emphasis added).

Further, by the plain language of the "no-action" clause, it is intended to prevent certificate holders from instituting proceedings against others. Indeed, in each of the cases cited by the City, the "no-action" clause was used to justify dismissing a plaintiff-certificate holder's case against a defendant. It is clear that these types of clauses are intended to prevent individual or small groups of certificate holders from initiating piecemeal, harassing or redundant litigation. *See e.g., Cent. States Life Ins. Co. v. Kopljar Co.*, 80 F.2d 754, 758 (8th Cir. 1935) ("If . . . every holder of a bond or bonds were free to sue at will for himself and for others similarly situated, the resulting harassment and litigation would be not only burdensome but intolerable."); *Feldbaum v. McCrory Corp.*, No. 11866, 1992 WL 119095, at \*6 (Del. Ch. June 2, 1992)

