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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

In the Matter of the Rehabilitation of FINANCIAL GUARANTY INSURANCE COMPANY	Index No. 401265/2012 Doris Ling-Cohan, J. Motion Sequence No. 4 **AMENDED OBJECTIONS**

The Bank of New York Mellon and The Bank of New York Mellon Trust Company, N.A. (collectively, the "Trustee") states that its amended objections, as set forth more fully in the accompanying memorandum of law (the "Trustee's Memo"), are to the following sections of the Proposed Plan:

Plan Section	Grounds for Objection
3.5	Improperly seeks to re-write Transaction Documents to which FGIC is not a party. See Trustee's Memo at 7-15.
3.7(b)	Improperly requires the Trustee to act in the absence of reasonable assurance that FGIC will be able to satisfy its indemnification obligations. See Trustee's Memo at 19-20.
4.6	Improperly shifts payment of attorneys' fees in the absence of contract. See Trustee's Memo at 20.
4.9	Improperly grants FGIC set-off rights while stripping policy-holders of their set-off rights. See Trustee's Memo at 15-16.
7.5(b)	Improperly requires the Trustee to act in the absence of reasonable assurance that FGIC will be able to satisfy its indemnification obligations. See Trustee's Memo at 19-20.
7.8(c)	Improperly restrains the Trustees from exercising their legally-mandated set-off rights. See Trustee's Memo at 15-19.
7.8(e)	Improperly seeks to re-write Transaction Documents to which FGIC is not a party. See Trustee's Memo at 7-15.
Exhibit B Restructured Policy Terms 1.4.A[1]	Improperly adjusts Claimholders' rights to payment based on recoveries from third-parties. See Trustee's Memo at 21-23.

[1] Joining in the objection asserted in the Objection of Certain Jefferson County Warrantholders to Plan of Rehabilitation dated November 19, 2013 pp. 20 et seq., not limited to the Jefferson County Policies and Jefferson County Indenture as defined therein.

Dated: New York, New York
January 22, 2013

Respectfully submitted,

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

In the Matter of the Rehabilitation of FINANCIAL GUARANTY INSURANCE COMPANY	Index No. 401265/2012 Doris Ling-Cohan, J. Motion Sequence No. 4

MEMORANDUM OF LAW IN SUPPORT OF AMENDED OBJECTIONS OF THE BANK OF NEW YORK MELLON AND THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., AS TRUSTEE TO THE PROPOSED PLAN OF REHABILITATION

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Introduction

The Bank of New York Mellon and The Bank of New York Mellon Trust Company, N.A., each in its capacity as indenture trustee (collectively, the "Trustee") under indentures pursuant to which bonds[1] were issued and are outstanding that are insured by financial guaranty insurance policies issued by Financial Guaranty Insurance Company ("FGIC") or FGIC Credit Products, LLC ("FGIC CP"), respectfully submit this memorandum of law in support of its Amended Objections dated January 22, 2013 (the "Amended Objections") to the First Amended Plan of Rehabilitation dated December 12, 2012 (the "Proposed Plan")[2] filed by Benjamin Lawsky, Superintendent of Financial Services of the State of New York (the "Superintendent") as the court appointed rehabilitator (the "Rehabilitator") of FGIC. The Trustee incorporates the previously filed affidavits of Gerard F. Facendola and Bridget Schessler both sworn to June 22, 2012, and the affidavit of Gerard F. Facendola sworn to November 19, 2012 (the "Facendola November Aff.") in support of the Amended Objections.

Preliminary Statement

The Trustee acts as trustee in thousands of transactions. Pursuant to the governing documents (the "Transaction Documents"), FGIC has issued policies (the "Policies") insuring bonds issued in approximately 700 of these transactions (the "Insured Bonds"). The Policies insure against possible payment shortfalls on the Insured Bonds. Over the life of these transactions, FGIC has been paid substantial policy premium payments in exchange for FGIC's commitment to pay claims (the "Claims") arising under the Insured Bonds.

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[1] References to indenture trustee, indenture and bonds should be read to include all similar transactions involving municipal, corporate and asset-backed securities where the role of the Trustee may be titled as a fiscal agent or other designation. The governing instrument may have different designations and the securities may be referred to as notes or by other designations.

[2] Capitalized terms used without definition are used as they are defined in the Proposed Plan.

Pursuant to the terms of the Proposed Plan, the Rehabilitator seeks to dramatically and inequitably alter the terms of these transactions. The Proposed Plan far exceeds the jurisdiction of this Court and scope of the Rehabilitator's authority, by unilaterally amending, and in many cases eviscerating, the terms contained in the Transaction Documents, including agreements other than Policies and agreements to which FGIC is not even a party. Further, the Proposed Plan improperly and wrongfully strips holders of Claims (the "Claimholders") of their common-law rights of recoupment and setoff. The Proposed Plan also fails to provide adequate indemnity to the Trustee, which is particularly significant in light of the potential exposure to substantial expense and liability. The Proposed Plan improperly seeks to shift the payment of attorneys' fees in claims disputes in the absence of contract in violation of the "American Rule." Finally, the Proposed Plan violates the "made whole" doctrine by attempting to permit FGIC as an insurer to rely on equitable subrogation rights to compete with the Claimholders for recoveries from available sources of payment before the insured obligations are paid in full. For each of these reasons and as set forth more fully below and as set forth in the Amended Objections filed by the other trustee banks and certain Jefferson County Warrantholders,[3] the Proposed Plan must be substantially modified before it may be approved.

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[3] The Trustee reserved the right to join in the Objections filed by the other trustee banks in its initial objections filed November 19, 2012, and on December 11, 2012, the Trustee filed with this Court a formal Joinder of The Bank of New York Mellon and The Bank of New York Mellon Trust Company N.A., as Trustee to (I) Objections of Trustees Deutsche Bank National Trust Company and Deutsche Bank Trust Company Americas to the Proposed Plan of Rehabilitation of Financial Guaranty Insurance Corporation, (II) The Objection of U.S. Bank National Association and U.S. Bank Trust National Association, Each in its Capacity as Trustee, to the Plan of Rehabilitation Dated September 27, 2012, and (III) Objection to the Proposed Plan of Rehabilitation of Wells Fargo Bank, N.A., in its Capacity as Trustee for Certain RMBS Certificateholders and Noteholders for Such Trusts and Transactions. The Trustee also joins in the Amended Objection of Aurelius Capital Management, LP to the Proposed Plan of Rehabilitation, filed January 22, 2013, and the objection asserted in the Objection of Certain Jefferson County Warrantholders to the Plan of Rehabilitation, dated November 19, 2012, (the "Jefferson County Warrantholders' Objection") at p. 21 et seq., based on principals of equitable subrogation and not limited to the Jefferson County Plan and the Jefferson County Indenture as defined therein.

FACTS

On November 24, 2009, the New York Department of Insurance (now known as the New York Department of Financial Service, "NYDFS") entered an Order pursuant to Section 1310 of the New York Insurance Law ("NYIL") (as modified by the Supplemental Order dated March 25, 2010, the "1310 Order") requiring FGIC to suspend paying any and all claims and prohibiting FGIC from writing any new policies effective November 24, 2009. That same day, FGIC issued a press release stating that, as a result of the issuance of the 1310 Order, "FGIC will immediately suspend all claims payments." The press release further provided that until "FGIC achieves compliance with such requirement, the 1310 Order prohibits FGIC from writing any new policies and requires FGIC, as of November 24, 2009, to suspend paying any and all claims and to otherwise operate in the ordinary course and as necessary to effectuate the Surplus Restoration Plan."

FGIC's failure to pay Claims was a default of FGIC's obligations under the Policies. Independently, FGIC's announcement that it would suspend payment of Claims was and is an anticipatory breach under the Policies and applicable Transaction Documents. As a result, Claimholders, including the Trustee, were entitled to exercise common law and contractual rights of recoupment or setoff against premium payments and reimbursements[4] to FGIC. The failure to pay Claims (and, typically, insolvency and becoming subject to a rehabilitation proceeding) as well as its announced suspension to pay Claims or otherwise provide adequate assurance of performance constituted a defined "Insurer Default."[5] An Insurer Default, by the terms of the

[4] As a financial guaranty insurer, to the extent that it pays Claims, FGIC has rights to recover the amounts that it pays on Claims through reimbursement and subrogation as detailed in the Transaction Documents or rights of equitable subrogation.

[5] The Transaction Documents on any particular transaction may use some other defined term such as "Series Enhancer Default" or reach the same result through other drafting conventions or applicable law, including the

Transaction Documents resulted in a loss of FGIC's "Control Rights." FGIC's Control Rights included, among other things, the right, subject to conditions, to direct the Trustee to take action under the Transaction Documents. An Insurer Default also resulted in the reordering of the priorities of distributions of funds under certain Transaction Documents to eliminate or subordinate the distributions made to FGIC because of its failure or prospective failure to fund payments to the investors through payments on policy Claims. FGIC's position in the waterfall and its Control Rights derive from its promise to pay the principal of and interest on the Insured Bonds if there are insufficient funds otherwise available. When an Insurer Default has occurred, i.e., FGIC has failed to pay Claims or by its insolvency or filing or becoming subject to a rehabilitation proceeding showing that it will be unable to pay Claims in full, the cash flows are adjusted to account for FGIC's failure to pay Claims, such as, for example, the cessation of premium payments for insurance coverage that FGIC is no longer supplying or reimbursements for Claims.

On June 11, 2012, the Superintendent filed his Verified Petition for Order of Rehabilitation in this Court. On June 28, 2012, this Court entered the Order of Rehabilitation. On September 27, 2012 this Court entered a scheduling order (the "Scheduling Order") setting forth a briefing schedule with respect to the approval of the Proposed Plan. That same day, the Rehabilitator filed the Proposed Plan, a Disclosure Statement regarding the Proposed Plan ("Disclosure Statement"), an Affirmation in Support of Plan Approval, a Proposed Plan Approval Order, a Novation Agreement, and a Form of Notice of Plan Approval Hearing. On October 25, 2012, the Rehabilitator filed its Memorandum of Law in Support of Approval of Plan of Rehabilitation For Financial Guaranty Corporation (the "Rehabilitator's Memo"). On

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concept of anticipatory breach under Policies and applicable Transaction Documents and FGIC's failure to provide adequate assurance of performance.

November 19, 2012, the Trustee filed its initial Objections to the Proposed Plan of Rehabilitation. On December 12, 2012, the Rehabilitator filed the Omnibus Reply Memorandum of Law in Further Support of Approval of First Amended Plan of Rehabilitation for Financial Guaranty Insurance Company (the "Reply") along with the amended Proposed Plan. The Proposed Plan as amended addressed some, but not all of the Trustee's Objections. On December 18, 2012, this Court held a status conference regarding the Objections that had been resolved and the Objections that remained outstanding. On December 19, 2012, this Court entered a new scheduling order fixing January 28 and 29, 2013, as the dates for the Proposed Plan approval hearing and requiring the objecting parties to file amended papers on January 22, 2013, addressing their remaining Objections. On January 15, 2013, at the Discovery Conference, the Court indicated that the amended objections could not address points raised in the Rehabilitator's Reply. The Trustee reserves the right to address any point raised in the Rehabilitator's Reply at the hearing on approval of the Proposed Plan, and in any post-hearing briefing.

OBJECTIONS

The Trustee objects to those portions of the Proposed Plan that exceed the power of this court, are unfair and inequitable, do not meet the "best interests of creditors" test, work an unnecessary hardship on Claimholders and constitute an abuse of the Rehabilitator's discretion. The Proposed Plan impermissibly seeks to modify Claimholders' bargained-for contractual rights under contracts which are not subject to adjustment in a rehabilitation proceeding and others to which FGIC is not a party. This exceeds the power of this Court, constitutes a clear abuse of discretion, is inequitable to Claimholders, and must be modified. Specifically, the Proposed Plan seeks to disregard FGIC's payment defaults and its announced suspension of all Claims payments, rewrite the Transaction Documents, reverse allocations of funds made pursuant the terms of the Transaction Documents, and restore to FGIC Control Rights in contravention of the Transaction Documents and applicable law. The Proposed Plan also wrongfully strips the Claimholders of their common law and statutory rights of recoupment and setoff contrary to the express terms of the NYIL and contrary to New York case law. The Proposed Plan contains arbitrary provisions that expose the Trustee to liability by requiring the Trustee to act without adequate indemnification and shift liability for attorneys' fees not provided for by contract or applicable law. Finally, the Proposed Plan contains provisions not provided for in the Transaction Documents and contrary to applicable law giving FGIC rights to share in recoveries before Claimholders are paid in full. Accordingly, approval of the Proposed Plan should be denied unless it is modified to adequately address the objections identified in the Amended Objections.

STANDARD

The standard for approval of the Rehabilitator's application for approval of the Proposed Plan is elaborated in the January 22, 2013, letter brief from James Gadsden of Cater Ledyard & Milburn LLP, attorneys for the Trustee, submitted pursuant to the Court's request at the January 15, 2013, discovery conference. A plan of rehabilitation must be consistent with the law and must equitably apportion loss. See In re Frontier Ins. Co., 36 Misc. 3d 529, 542 (Sup. Ct. Albany Co. 2012) ("[A] plan of rehabilitation cannot be approved where it is inconsistent with the law."); Grode v. Mut. Fire, Marine, & Inland Ins. Co., 572 A.2d 798, 804 (Pa. Commw. Ct. 1990) (the court must act as a "check on potential discretionary abuse to insure equitable apportionment of loss"). Thus, a plan of rehabilitation must not only comply with legal and constitutional precepts it must also be fair and equitable to all interested parties. Carpenter v. Pac. Mut. Life Ins. Co. of Cal., 10 Cal. 2d 307, 317 (1937), aff'd sub nom. Neblett v. Carpenter, 305 U.S. 297 (1938). Courts defer to a rehabilitator's business judgment exercised within legal parameters, but must disapprove actions by a rehabilitator that are "arbitrary, capricious or an abuse of discretion." Callon Petroleum Co. v. Superintendent of Ins. of State, 53 A.D.3d 845, 845 (3d Dep't 2008); Mills v. Florida Asset Fin. Corp., 31 A.D.3d 849, 850 (3d Dep't 2006).

While "[t]he courts will generally defer to the rehabilitator's business judgment" (Callon, 53 A.D.3d at 845; Mills, 31 A.D.3d at 850), the scope of this Court's jurisdiction over parties or contracts other than an insurer's policies and the determination of what are permissible terms of a plan of rehabilitation are not business decisions, but matters of law for the Court.

ARGUMENT

POINT I.

SECTIONS 3.5 AND 7.8 OF THE PROPOSED PLAN ARE UNFAIR, INEQUITABLE AND A VIOLATION OF THE REHABILITATOR'S DISCRETION AND THUS MUST BE MODIFIED

Section 3.5 of the Proposed Plan provides that FGIC shall be deemed not to have defaulted under any FGIC Contract or Transaction Documents.[6] Section 7.8 enjoins all parties from exercising any contractual rights, including Control Rights, they would otherwise have as a result of FGIC's defaults.[7]

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6 In relevant part, Section 3.5 provides:

> upon the Effective Date, any default, event of default or other event or circumstance relating to the FGIC Parties then existing (or that would exist with the passing of time or the giving of notice or both) under any FGIC Contract or Transaction Document as a result of (whether directly or indirectly) the Rehabilitation or the Rehabilitation Circumstances shall be deemed not to have occurred (including, for the avoidance of doubt any default, Event of Default or other event or circumstance relating to the FGIC Parties then existing (or that would exist with the passing of time or the giving of notice or both) due to a lack of payment or performance of or by the FGIC Parties under any FGIC Contract or Transaction Document).

7 In relevant part, Section 7.8(e)(i) provides:

> except as expressly provided by Section 3.7 hereof, exercising or taking any action to exercise, including by asserting any defense based on the Rehabilitation or the occurrence or existence of any of the Rehabilitation Circumstances, any approval, consent, direction, determination, appointment, request, voting, veto, waiver or other right that the FGIC Parties have (through the right to direct or grant or withhold consent with respect to such

As a consequence of FGIC's defaults, during the three years since it stopped paying Claims, distributions of funds under Transaction Documents have been made based on the bargained-for revised distribution priorities applicable after an Insurer Default.[8] The BFC Ajax CDO Ltd. Indenture[9] is illustrative. The Priority of Payments in Section 11.01(a) makes payment to FGIC as "Credit Enhancer"[10] in the fourth priority, but only "so long as no Credit Enhancer Default[11] has occurred and is continuing."[12] Under such a waterfall, the available funds are distributed to the investors in the Insured Bonds and other parties contractually entitled

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exercise or otherwise) (or that the FGIC Parties would have but for the Rehabilitation or the occurrence or existence of any of the Rehabilitation Circumstances) under or with respect to any FGIC Contract or any Transaction Document executed in connection with the issuance of or entry into such FGIC Contract or related to such FGIC Contract or any obligations insured or covered thereby (all rights and remedies described in this clause (i), the "FGIC Rights"); (ii) except as expressly provided by Section 3.7 hereof, failing to take, or taking any action inconsistent with, any action (or inaction) directed (whether actively or passively) to be taken pursuant to the exercise by the FGIC Parties of any FGIC Rights or (iii) failing to provide, or causing to be provided, to the FGIC Parties any notice, request or other communication or document that the FGIC Parties may have the right to receive (or that the FGIC Parties would or may have the right to receive but for the Rehabilitation or the occurrence or existence of any of the Rehabilitation Circumstances). For the avoidance of doubt, this subsection 7.8(e) shall not enjoin or restrain any trustee from exercising any remedial power in the absence of any conflicting direction from FGIC (to the extent that FGIC is entitled to give such direction) or any servicer (including any master servicer, sub-servicer or special servicer) from servicing underlying collateral, in each case to the extent permitted under and in accordance with the terms and conditions of the applicable Transaction Documents (and in each case without regard to the Rehabilitation and the occurrence or existence of any of the Rehabilitation Circumstances)[.]

8 Many indentures provide that the available funds (such as collections from the borrowers' mortgage payments in a residential mortgage backed (RMBS) transaction) are distributed on each payment date pursuant to a priority of payments colloquially referred to as a waterfall among the investors in what may be several series of bonds with different payment priorities and other parties, including the bond insurer. Where there are shortfalls in payment from the underlying source of payment such as borrowers unable to make their mortgage payments, a party's position in the waterfall will have important consequences on whether it is receives full payment, partial payment, or any payment at all.

9 Indenture dated as of November 29, 2006 among BFC Ajax CDO Ltd., as Issuer, BFC Ajax CDO LLC, as Co-Issuer, Financial Guaranty Insurance Company, as Credit Enhancer and The Bank of New York Trust Company, National Association (now named The Bank of New York Mellon Trust Company, National Association), as Trustee attached as Exhibit B to the Facendola November Aff.

10 The term used in this indenture for the Bond Insurer.

11 Defined to include failure to make payments when due under the Credit Enhancement (the Financial Guaranty Insurance Policy) and the entry of an order for relief in a rehabilitation proceeding or the appointment or a receiver, here the Rehabilitator.

12 Facendola November Aff. Ex. B at 169.

to the funds after the Insurer Default. The Proposed Plan proposes to reallocate the bargained for distributions now and in the future by declaring that FGIC is excused from the consequences of the "Rehabilitation Circumstances" which is defined to include FGIC's failure to pay Claims. Furthermore, to the extent the Transaction Documents provide that upon a Credit Enhancer Default (or similar event) that the Priority of Payments *among* bondholders changes, then those changes should not be disturbed in any way by the Proposed Plan.[13] The bondholders relied on those provisions when evaluating the RMBS issuances and it was material to their investment decision.

The Transaction Documents also generally provide that FGIC has certain rights, subject to conditions, to control or direct the Trustee. See Trust Indenture, dated February 1, 1997, between Jefferson County, Alabama and AmSouth Bank of Alabama (the predecessor in interest to The Bank of New York Mellon).[14] These rights, however, are expressly conditioned on its fulfillment of FGIC's contractual obligations under the Policies. Id., § 17.3. Thus, the Transaction Documents grant FGIC the right to direct the Trustee to enforce remedies under the indenture only where FGIC is able perform or able to continue to perform. Id. at §§ 17.3(c); 13.5. Where FGIC is unable to meet payment obligations, however, the economic risk has

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13 The last paragraph of §3.5 provides:

> Notwithstanding anything to the contrary in this Section 3.5, during any period of time in which a Claim has been submitted in accordance with the Plan with respect to a Policy and such Claim has not been satisfied in full in Cash and/or Deemed Cash Payments, this Section 3.5 shall not apply with respect to the determination of priority of distributions between and among Instruments insured by such Policy.

This provision is unclear in its application to Claims that arose prior to the commencement of this proceeding and with respect to future Claims. If a Claim was submitted and has been unpaid, for the reasons set forth in the discussion of Point II below, Section 3.5 should not be given effect to determine the priority of distributions under any Transaction Documents. This apparent savings clause is limited by its terms to the determination of the priority of distributions between and among Instruments insured under any one Policy when the principle should be applied to the priority of distributions under any relevant Transaction Documents.

14 Facendola November Aff., Ex. C, §§ 17.3(c); 13.5.

shifted back to the insured Bondholders. FGIC loses the right to direct and control the Trustee which right reverts to the holders of the Insured Bonds. Id., § 17.3(c). Because FGIC has not complied with its payment obligations and will be unable to comply in the future, under the terms of the parties' agreements, FGIC has no right to control or direct the Trustee.[15]

Sections 3.5 and 7.8 of the Proposed Plan operate in tandem to strip the holders of their bargained-for Control Rights. This would fundamentally alter the relationship of the parties to the Transaction Documents and allow FGIC to direct the Trustee even though the holders of the Insured Bonds bear the risk of loss. The party exercising Control Rights would have the ability to make important decisions affecting the subject of the financing funded by the Insured Bonds, discretion in determining how rights and remedies under the Transaction Documents are exercised, and directing the Trustee to take significant actions including prosecuting litigation that may involve incurring significant fees and expenses and may risk substantial liability.[16]

This unilateral attempt to strip Claimholders of their rights is beyond the power of the court and an abuse of the Rehabilitator's discretion. The NYIL only allows the Rehabilitator to "remov[e] the causes and conditions which have made the [rehabilitation proceeding]

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[15] Notably, the 1310 Order required FGIC to suspend paying all claims and prohibited FGIC from writing any new policies. In a press release issued the same day as the 1310 Order, FGIC affirmatively and unequivocally acknowledged that it would "immediately suspend all claims payments" and that it was prohibited from "writing any new policies." FGIC Press Release, November 24, 2009, available at http://www.fgic.com/aboutfgic/news/fgic20091124.pdf. As a consequence of this unequivocal inability to perform, FGIC has been and continues to be in anticipatory breach of its contractual obligations under the FGIC Bond Insurance policies. See, e.g., Alabama v. North Carolina, 130 S. Ct. 2295, 2312 (2010) ("A repudiation occurs when an obligor either informs an obligee that the obligor will commit a breach that would of itself give the obligee a claim for damages for total breach, or performs a voluntary affirmative act which renders the obligor unable or apparently unable to perform without such a breach") (internal quotations omitted); Tenavision, Inc. v. Neuman, 45 N.Y.2d 145, 150 (1978) (holding that an anticipatory breach occurs when the "intention not to perform [is] positive and unequivocal"); Viacom Outdoor Inc. v. Wixon Jewelers, Inc., 82 A.D.3d 604 (1st Dep't 2011) (an unequivocal statement conveying the intent not to perform constitutes an anticipatory breach). Therefore, to the extent that FGIC has not yet technically failed to pay under certain Policies supporting any particular Transaction Document, there has been an anticipatory breach of all such Transaction Documents as a consequence of FGIC's unequivocal confirmation that it is prohibited from paying claims payments since the 1310 Order and proposes to make significantly less than full payment in the future.

[16] As discussed in Point III below, the indemnification provisions in the Proposed Plan are inadequate to protect the trustee in connection with any exercise of control rights by FGIC.

necessary." NYIL § 7403(a). There has been no showing, nor could there be, that the exercise of Control Rights by the holders of the Insured Bonds in any way "caused" FGIC to require rehabilitation. Indeed, the Disclosure Statement states that "[s]ince the fourth quarter of 2007, FGIC's business, results of operations and financial condition have been adversely affected by, among other things, significant losses on certain policies issued by FGIC relating to RMBS and ABS CDO backed primarily by subprime RMBS. Because of a dramatic, sustained increase in payment defaults on the U.S. residential mortgage loans collateralizing these securities, there have been, and are expected to be, substantial shortfalls in funds available to make required payments on such securities . . . . ." Disclosure Statement at 10. Nor does the Rehabilitator cite to any other provision of the NYIL, or any case, because no such law or case exists, that grants this Court or the Rehabilitator the authority to wholesale re-write contracts, which are not contracts of insurance subject to state regulation to which, in many cases, it is not even a party.[17]

Finally, in this proceeding, the Court may only exercise *in rem* jurisdiction over the assets of FGIC and its affiliates. Matter of Rehab. of Nat'l Heritage Life Ins. Co., 656 A.2d 252, 260 (Del. Ch. 1994) (rehabilitation proceedings are *in rem* proceedings); Ballesteros v. New Jersey Prop. Liab. Ins. Guar. Assoc., 530 F. Supp. 1367 (D.N.J. 1982) (same). The Control Rights FGIC seeks to obtain are rights of the holders of the Insured Bonds and thus are not an asset of FGIC. Cf. Agstar Fin. Servs. FLCA v. Rock Creek Dairy Leasing, LLC, No. 09-cv-272, 2010

[17] The plans of rehabilitation from other states and case cited by the Rehabilitator are not precedent for the powers of this Court. Rehabilitator's Memo at 25-26 citing Ambac, Plan of Rehabilitation, Case No. 10-CV-1576, §8.01 (Wis. Cir. Ct. Jan. 24, 2011); Grode v. Mut. Fire, Marine & Inland Ins. Co., Plan of Rehabilitation, Case No. 3483 1986, § XIII(E)(Pa. Commw. Ct. 1989); Muir v. Transp. Mut. Ins. Co., 523 A.2d 1190, 1193-94 (Pa. Commw. Ct. 1987). Plans are not statutes or case authority; the terms that the Rehabilitator points to may have been included upon consent and are not authority on what a court would have decided had the validity of the terms been contested by the parties to that proceeding. Muir merely affirmed an order which stated that no person, firm governmental and business entity or corporation could institute any suit or proceeding at law or in equity or otherwise against the company in rehabilitation (Muir, 523 A.2d at 1193-94) and is no authority for the proposition that a rehabilitator could unilaterally modify contracts to which the company in rehabilitation was not a party.

WL 1257465, at *1 (N.D. Ind. 2010) (court overseeing receivership could not approve sale of property falling outside of receivership estate).

To the extent that the Proposed Plan would modify the distribution of funds that will be made in the future and grant FGIC the right to receive funds through offset or otherwise that are to be paid to others due to FGIC's defaults, this would gravely affect the rights of parties that are not parties to the FGIC Policies and further exceed the powers of the Rehabilitator or this Court.[18] Accordingly, Sections 3.5 and 7.8 of the Proposed Plan are unfair and inequitable and an abuse of the Rehabilitator's discretion. See Callon, 53 A.D.3d at 845 (holding that rehabilitator of Frontier Insurance Company acted arbitrarily and capriciously by ignoring obligation to pay $2.7 million default judgment against Frontier to Callon Petroleum despite judicial decisions by two appellate courts confirming award).[19]

In an attempt to justify its assertion of these additional rights, including Control Rights, the Rehabilitator (i) relies on bankruptcy and banking law including arguing that the termination of its consent rights are unenforceable *ipso facto* clauses and (ii) argues that in the absence of these provisions of the Proposed Plan, certain holders of Insured Bonds may exercise rights like Control Rights to the detriment of other holders. Each of these arguments is meritless.

The bankruptcy and bank cases and statutes discussed in the Rehabilitator's Memo (Memo at 28-29) are no authority for relief sought in this proceeding since this proceeding for the rehabilitation of an insurance company is not subject to the rules applicable in bankruptcy or bank insolvency proceedings. Nor are the cases persuasive as analogies. While the statutory scheme of the Bankruptcy Code does preserve a contract with an *ipso facto* clause so the debtor

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[18] The modifications to the Proposed Plan have eliminated "claw back" of funds already disbursed pursuant to the relevant Transaction Documents.

[19] Similarly, the Proposed Plan cannot enlarge FGIC's subrogation rights as suggested by the language of Section 4.13.

can enforce the agreement, it does not allow the underlying bargain to be altered by the debtor. The debtor must assume the entire contract and accept the burdens as well as the benefits. In re N.Y. Skyline, Inc., 432 B.R. 66, 84 (Bankr. S.D.N.Y. 2010) ("When the debtor assumes the lease or the contract under § 365, it must assume both the benefits and the burdens of the contract. Neither the debtor nor the bankruptcy court may excise material obligations owing to the non-debtor contracting party.") (quoting City of Covington v. Covington Landing Ltd. Pship., 71 F.3d 1221, 1226 (6th Cir. 1995)); In re S.E. Nichols Inc., 120 B.R. 745, 747 (Bankr. S.D.N.Y. 1990) ("It is well-settled that a debtor cannot assume part of an unexpired lease while rejecting another part; the debtor must assume the lease *in toto* with both the benefits and burdens intact.") Thus, under the Bankruptcy Code, if the debtor (like FGIC in this case) is unable to perform or provide assurance of future performance and satisfactory indemnity, it cannot enforce the contract against the non-debtor party.

Furthermore, an *ipso facto* clause conditions a remedy upon a party's insolvency. In re W.R. Grace & Co., 475 B.R. 34, 152 (D. Del. 2012) ("*Ipso facto* clauses are contractual provisions which expressly state that upon a borrower's filing of a bankruptcy petition, the creditor may accelerate the payment of the entire unpaid balance due under the terms of the contract."); see also Nemko, Inc. v. Motorola, Inc. (In re Nemko, Inc.), 163 B.R. 927, 938 n. 5 (Bankr. E.D.N.Y. 1994). Thus, clauses that trigger a remedy upon a payment default, are not *ipso facto* clauses and are thus enforceable. I.T.T. Small Bus. Fin. Corp. v. Frederique, 82 B.R. 4, 6 (E.D.N.Y. 1987); In re Delaware River Stevedores, Inc., 129 B.R. 38, 41 (Bankr. E.D. Pa. 1991). Even in the bankruptcy contexts, courts have recognized that the filing of a petition for relief does not relieve the debtor of consequences of a payment default. In re Margulis, 323 B.R. 130, 136 (Bankr. S.D.N.Y. 2005) (failure of debtor to pay reduced amount due by agreed upon deadline, which resulted in obligation to payment in full, did not constitute unenforceable *ipso facto* clause even though bankruptcy filing made it more difficult to satisfy the condition); In re C.A.F. Bindery, 199 B.R. 828, 833 (Bankr. S.D.N.Y. 1996).[20] Thus, FGIC's attempt to justify its unilateral rewriting of the Transaction Documents cannot be sustained on this ground.

The Rehabilitator's reference to certain powers provided the Federal Deposit Insurance Corporation ("FDIC") under section 1821(e)(13)(A) of the Financial Institutions Reform Recovery and Enforcement Act, 12 U.S.C. §1821(e)(13)(A), are similarly inapposite. Congress provided that the FDIC "may enforce any contract . . . notwithstanding any provision of the contract providing for the termination, default, acceleration, or exercise of rights upon, or solely by reason of, insolvency or the appointment of or the exercise of rights or powers by a conservator or receiver . . . ." Id. As recognized in the legislative history of this provision, "[t]his amendment enables the FDIC to continue to enforce contracts that would otherwise terminate by their terms upon the appointment of the receiver or conservator for a financial institution." See Technical Amendments to s. 413, Federal Deposit Insurance Corporation Act, 101st Cong. (1989) as quoted in Bank of New York v. FDIC, 453 F. Supp. 2d 82, 96 (D.D.C. 2006). While this provision keeps a party from terminating a contract based solely on the appointment of the FDIC as a receiver, it does not provide the FDIC the right to modify the contract or to require performance when FDIC is unable to perform.

In a fact pattern analogous to this case, the court in Peoples Heritage Sav. Bank v. New Heritage Holdings, Inc., CIV. A. 93-10169-Z, 1994 WL 175029 (D. Mass. Apr. 29, 1994), held that the FDIC could not use its powers to become the lead bank in a participation agreement when those powers had already been lost pre-receivership due to the implementation of a cease

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[20] Nor does the Bankruptcy Code enable a party to assume a contract that is no longer executory or is a contract for a financial accommodation. Bankruptcy Code §365.

and desist order, an event that pursuant to the terms of the participation agreement prohibited the bank from exercising such control powers. Just as the FDIC cannot use a receivership to change the terms of its agreements and require one-sided performance, the Rehabilitator should not be allowed to use this proceeding to try to force the Trustee to accept its direction and control without the corresponding protections afforded the Claimholders and the Trustee by the Transaction Documents.

The Proposed Plan does not seek to preserve the Transaction Documents to allow for FGIC's performance in the future. It seeks to change the underlying bargain. Just as the Bankruptcy Code and the laws applicable to the FDIC do not permit substantial alteration of rights and performance obligations under a contract, the Proposed Plan should not broaden FGIC's rights to the detriment of the Claimholders and the Trustee.

Finally, FGIC's argument that controlling holders may at some time in the unforeseen future act in manner detrimental to other holders is completely speculative. Rehabilitator's Memo at 29-30. Indeed, every holder will have the incentive to maximize their recovery. See Facendola November Aff. at ¶ 5. Thus, there is no basis to conclude that FGIC would be a better advocate for all of the holders when it is the holders' assets – and not FGIC's – that are at risk.

POINT II.

SECTION 7.8(C) OF THE PROPOSED PLAN UNLAWFULLY STRIPS THE TRUSTS OF LEGALLY PROTECTED RECOUPMENT AND SETOFF RIGHTS

Section 7.8(c) also seeks to strip the Claimholders of their rights to recoupment and setoff and subordination of FGIC's claims (even when FGIC was already subordinated pursuant to the Transaction Documents irrespective of the occurrence of the Rehabilitation Circumstances). Proposed Plan § 7.8(c).[21] The unfairness and inappropriateness of this provision of the

[21] In relevant part, Section 7.8(c) enjoins holders from:

Proposed Plan is demonstrated by the contrast with Section 4.9. While the Trustee seeks only to have its otherwise applicable rights of recoupment or setoff recognized, the Proposed Plan creates an express right of setoff for FGIC and seeks to override generally applicable compulsory counterclaim rules that might otherwise deprive it of its right of setoff. Furthermore, this provision would violate the "best-interests of the creditors" test by taking away from Claimholders recoveries they would have retained had FGIC been liquidated. This provision is inequitable and an abuse of discretion because it eviscerates rights as provided by the common law, the NYIL, and the Transaction Documents.

A. Section 7.8(c) violates the Claimholders' common law, statutory and contractual rights to setoff

Section 7.8(c) violates the Claimholders' common law, statutory and contractual rights to setoff and recoupment. The Trustee and Claimholders have common law rights to recoupment and setoff independent of the provisions of the Transaction Documents. Nat'l Cash Register Co. v. Joseph, 299 N.Y. 200, 203 (1949) ("Recoupment means a deduction from a money claim through a process whereby cross demands arising out of the same transaction are allowed to compensate one another and the balance only to be recovered. Of course, such a process does not allow one transaction to be offset against another, but only permits a transaction which is made the subject of suit by a plaintiff to be examined in all its aspects, and judgment to be rendered that does justice in view of the one transaction as a whole."); Matter of Midland Ins. Co., 79 N.Y.2d 253, 264 (1992) ("Contracting principals, who are debtors and creditors of each

withholding or continuing to withhold, subordinating, failing to pay, setting-off or taking similar action with respect to FGIC Payments owed (or that would have been or would be owed but for the Rehabilitation or the occurrence or existence of any of the Rehabilitation Circumstances), to the FGIC Parties under any FGIC Contract, or any Transaction Document executed in connection with the issuance of or entry into such FGIC Contract or related to such FGIC Contract or any obligations insured or covered thereby, regardless of the existence of any provisions in such FGIC Contract or Transaction Document that would or may otherwise permit such withholding, subordination, failure to pay, setting-off or similar action . . . .

other by virtue of entry into a contract or contracts, have the same legal capacity and may set off debts against each other."); Siegel v. State, 262 A.D. 388, 390 (3d Dep't 1941) (confirming the right of setoff).

Rights to recoupment and setoff are also recognized by the New York Insurance Law statute. NYIL § 7427 ("In all cases of mutual debts or mutual credits between the insurer and another person in connection with any action or proceeding under this article, such credits and debts shall be setoff and the balance only shall be allowed or paid."); see also, Matter of Midland Ins. Co., 79 N.Y.2d at 259-61 (1992) (holding that NYIL §7427 applies to rights of recoupment and setoff).[22] Courts have repeatedly affirmed this right of set-off in insolvency proceedings, including in the insurance context. See Van Schaick v. Astor, 154 Misc. 543, 545-46 (1st Dep't 1935). Thus, in Astor, for example, the First Department held that under §420 (now §7427) of the NYIL, the policy holder was entitled to set off premiums owed Union against Union's delinquent claims payments. Id. at 545; see also Matter of Midland Ins. Co., 79 N.Y.2d at 260, n. 2 (the general rule that mutual debts and credits may be set off applies in cases "involving insolvent insurance companies"). The provision of the NYIL recognizing setoff rights is applicable to rehabilitation as well as liquidation proceedings for insurance companies. New York Title & Mortgage Co. v. Irving Trust Co., 241 A.D. 246, 248 (1934) aff'd sub nom. New

[22] "Under the bankruptcy laws [even] offsets arising out of different transactions have consistently been permitted; they are distinguished from recoupment which involves claims arising from the same transaction (see, 4 Collier, Bankruptcy ¶ 553.03 [15th ed.], and authorities cited therein; Schwab, Anderson, Reed and Mendelsohn, Onset of an Offset Revolution: The Application of Set–Offs In Insurance Insolvencies, 8 J. of Ins. Reg. 464, 470–473, also reported in 95 Dick L. Rev. 449; see generally, 5 Carmody–Wait 2d, N.Y. Prac. § 31.2)." see also, City of Grand Rapids, Mich., v. McCurdy, 136 F.2d 615, 619 (6th Cir. 1943)("Recoupment differs from set-off mainly in that the claim must grow out of the same transaction which furnishes the plaintiff's cause of action, and is in the nature of a claim of right to reduce the amount demanded. Recoupment goes to the justice of the plaintiff's claim, while set-off is not necessarily confined to the justice of such particular claim. The defense of recoupment exists as long as the plaintiff's cause of action exists and may be asserted, though the claim as an independent cause of action is barred by limitations.")

York Title & Mortgage Co., by Van Schaick, v. Irving Trust Co., 268 N.Y. 547, 198 N.E. 397 (1935).

Finally, the Transaction Documents may provide recognition of the right to set off any amounts due and owing to FGIC against any amounts due and owing from FGIC to the Policyholder. The Transaction Documents and applicable law may also subordinate the claims of FGIC to the claims of Policyholders. The Rehabilitator's attempt to ignore the Claimholders' common law, statutory and contractual, rights of recoupment, and setoff and possible rights to the subordination of FGIC are contrary to law, and if otherwise lawful, arbitrary and capricious and an abuse of discretion.

B. Section 7.8(c) violates New York Insurance Law and the "Best Interests of Creditors" Test

As acknowledged by the Rehabilitator in presenting the analysis appearing at page 20 of the Rehabilitator's Memo, insurance insolvency law, like bankruptcy law, mandates that a creditor must receive as much, or more, under a rehabilitation plan as they would have received on liquidation. Carpenter, 10 Cal. 2d at 336. There is no doubt that holders would have had a right to setoff and recoupment had FGIC been liquidated. N.Y. Ins. § 7427. Since those rights would increase their net recoveries, the inclusion of Section 7.8(c) in the Proposed Plan is inconsistent with the parties' rights under the Insurance Law causing the Proposed Plan to fail the best interests of creditors test and common precepts of insurance rehabilitation law.

C. FGIC proposes to improperly impair the parties' rights in the identified transactions

FGIC has posted on the Rehabilitation Proceeding website [23] a document entitled: "Exhibit 1: Preliminary Analysis of FGIC Payments Not Paid to FGIC" (the "Preliminary Analysis") illustrating the application of the provisions of the Proposed Plan to the transactions

[23] http://www.fgicrehabilitation.com/docs.php

identified in the document. See Facendola November Aff. Ex. E. Based on the arguments presented above, the Trustee specifically objects to the proposed reductions in cash payments to be made to the Trustee as Policyholder on the transactions for which it is Trustee presented in the Preliminary Analysis that deprive the Trustee of its common law recoupment and setoff rights and vary the terms of the Transaction Documents as applied in those transactions.[24]

POINT III.

THE PROPOSED PLAN FAILS TO ADEQUATELY PROTECT THE TRUSTEE AGAINST LIABILITY FOR ACTS TAKEN AT FGIC'S DIRECTION

The revised Section 7.5(b) governs FGIC's indemnification obligations under the Proposed Plan.[25] The Proposed Plan provides that an Indemnified Trustee must accept the unsecured indemnity of FGIC so long as FGIC has $100 million in Admitted Assets, overriding any contractual requirement that the indemnity be satisfactory to an Indemnified Trustee. Even as revised, this provision is unfair and inequitable. To the extent the Indemnified Trustees must rely on FGIC's indemnification, before acting they must be allowed to make a determination as

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[24] The Trustee reserves the right to object to the Preliminary Analysis on all available grounds, including but not limited to its rights of recoupment and offset outlined in this Objection.

[25] In relevant part, Section 7.5(b) provides:

> FGIC shall indemnify each Indemnified Trustee for any Losses incurred by such Indemnified Trustee arising from its compliance with the express terms and conditions of the Plan or any direction given to it by FGIC pursuant to the relevant FGIC Contract or Transaction Document (in each case, excluding Losses resulting from gross negligence or willful misconduct of such Indemnified Trustee); provided, however, that (i) no amounts shall be payable by FGIC pursuant to this Section 7.5(b) to any Indemnified Trustee to the extent that the same is reimbursed to the Indemnified Trustee under or pursuant to any of the Transaction Documents . . . As long as FGIC has at least $100 million of Admitted Assets, the indemnity provided in this Section 7.5(b) shall be deemed to satisfy for all purposes any requirement under any provisions of a FGIC Contract or Transaction Document that the Indemnified Trustee be provided with an indemnity to or for its benefit (including any requirement that such indemnity be "adequate," "sufficient," "reasonable," "acceptable" or similar terms) prior to performing any action required under the Plan, including complying with any direction given to it by FGIC pursuant to the relevant FGIC Contract or Transaction Document, and including provisions that allow the Indemnified Trustee to refrain from performing any action in the absence of such an indemnity.

to whether FGIC can satisfy any potential liability that may arise from that direction. $100 million in Admitted Assets provides little comfort to the Trustee which could face liability much greater than such an amount in certain circumstances. Even if the threshold were reasonable for a given direction, the provision fails to address the impact on the strength of the indemnity when FGIC may give multiple directions to several trustees. The Trustee will not know what other indemnified directions have been given and the cumulative impact of such directions on the Admitted Assets. To compel the Trustee to act without any assurance that FGIC could satisfy its indemnification in such circumstances is unfair and inequitable.

POINT IV.

THE PROPOSED PLAN IMPROPERLY SHIFTS PAYMENT OF ATTORNEYS' FEES IN CLAIMS DISPUTES IN THE ABSENCE OF CONTRACT IN VIOLATION OF THE "AMERICAN RULE"

Section 4.6 of the Proposed Plan improperly imposes the payment of attorneys' fees to the non-prevailing party in the absence of contract in contravention of established law. See Hooper Assocs., Ltd. v. AGS Computers, Inc., 74 N.Y.2d 487, 492 (1989) ("attorney's fees are incidents of litigation and a prevailing party may not collect them from the loser unless an award is authorized by agreement between the parties, statute or court rule"); Gotham Partners, L.P. v. High River Ltd. P'ship, 76 A.D.3d 203, 204 (1st Dep't 2010) ("the longstanding 'American rule' precludes the prevailing party from recouping legal fees from the losing party 'except where authorized by statute, agreement or court rule'"); 546-552 W. 146th St. LLC v. Arfa, 99 A.D.3d 117, 122 (1st Dep't 2012) (parties are responsible for their own attorney's fees). This shifting of attorneys' fees is not provided for in the Transaction Documents, and if it were, it would not need to be repeated in the Proposed Plan. This section appears intended to dissuade any Claimholder from ever challenging any determination made by FGIC. Section 4.6 should be modified to make clear that each party is responsible for its own attorney fees.

POINT V.

THE FORCED PAYOVER/SETOFF PROVISIONS VIOLATE NEW YORK'S "MADE WHOLE" DOCTRINE[26]

As described in Point II of the Jefferson County Warrantholders' Objection at pp. 19 et seq., the Proposed Plan first creates two concepts it styles "FGIC Payments" and "FGIC Payment Payors." "FGIC Payments" is characterized as the Forced Payover/Setoff Provisions. "FGIC Payments" include "the then-current CPP multiplied by the amount of all recoveries, reimbursements, settlements and other amounts . . . which would be payable to [FGIC], or which [FGIC] would otherwise have a right to receive or recover . . . under the terms of or in connection with such Policy or any related Transaction Document, as if . . . FGIC had at all times paid Policy Claims in full in Cash." (Plan Ex. A (Definitions) at A-6.). The Plan then provides that:

> Each FGIC Payment Payor shall pay in Cash to the FGIC Parties all FGIC Payments payable by such FGIC Payment Payor, or that would have been payable had the Plan . . . been in effect at all times from and after the issuance of the 1310 Order, when due under the applicable Policy or any related Transaction Document, or if such FGIC Payment would have been due prior to the Effective Date . . .
>
> If FGIC determines in good faith that, notwithstanding the requirements of the foregoing paragraph, all or a portion of any FGIC Payment has not been paid to the FGIC Parties in accordance with the such paragraph, then, in addition to any other rights or remedies that FGIC may have, Cash payments that would otherwise be payable by FGIC in respect of the applicable Policy shall be reduced by the amount of such unpaid FGIC Payment.

(Plan Ex. B (Restructured Policy Terms) § 1.4(A).)

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26 This is not a new objection. The Trustee's Objection filed on November 19, 2012 (at p. 16) , asserted that "applicable law may also subordinate the claims of FGIC to the claims of Policyholders" and that "[t]he Rehabilitator's attempt to ignore the Claimholders' . . . possible rights to the subordination of FGIC are contrary to law." The Jefferson County Warrantholders' Objection, filed the same day elaborated on the Trustee's arguments by raising the "made whole" doctrine, a doctrine that is premised on the principles of equitable subrogation, which are not dependent on the terms of the Jefferson County transaction documents.

The Proposed Plan's Forced Payover/Setoff Provisions violate the well-settled New York law principle — known as the "made whole" doctrine — that an insurer claiming subrogation rights may not recover until the insured is fully compensated for its insured loss. In New York, "[u]nder the common law of subrogation, an insurer has the right to 'stand in the shoes' of the insured and seek recompense from the third-party tortfeasor for the amount paid to the insured, *provided that the insured has been made whole.*" USF&G v. Maggiore, 299 A.D.2d 341, 344 (2d Dep't 2001) (citation omitted; emphasis in original). This rule is premised on bedrock insurance principles. Where an insurer has provided coverage, "the burden of loss should rest on the party paid to assume the risk, and not on an inadequately compensated insured, who is the least able to shoulder the loss." Id. Indeed, placing the burden of loss on the insured would be "contrary to the principal purpose of an insurance contract: to protect an insured from loss, thereby placing the risk of loss on the insurer, and the insurer has accepted payments from the insured to assume this risk of loss." Id. (quoting 16 Couch, Insurance 3d § 223:136).

Contrary to the "made whole" doctrine, the Forced Payover/Setoff Provisions would grant FGIC a right of subrogation that would be enforceable even though its insured will not be paid in full on its insured loss. Those provisions would require Claimholders to turn over a portion of available recoveries from the obligor on the insured obligations or the property that is the subject of the transaction — regardless of whether the Claimholders have first been made whole on their insured loss. Allowing FGIC to receive FGIC Payments before the Claimholders are paid in full would turn the law of subrogation and "made whole" doctrine on their heads.

FGIC's payment of CPP (initially at the rate of 17.25% obligation) and the possibility that it will receive additional payments on account of DPO does not satisfy the "made whole" doctrine. Northwestern Mutual Life Insurance Co. v. Delta Air Lines, Inc. (In re Delta Air Lines, Inc.), 608 F.3d 139 (2d Cir. 2010).[27]

The policy justifications for the "made whole" doctrine are discussed in Restatement (Third) of Surety and Guaranty, § 27(1) Comment b:

> The purpose of subrogation is to reallocate the cost of performance from the secondary obligor to the principal obligor. The mechanism by which this reallocation is accomplished should not cause any disadvantage to the obligee. The obligee would be disadvantaged, however, if the secondary obligor were subrogated to rights of the obligee before complete satisfaction of the underlying obligation. In such a case, the rights obtained pursuant to the underlying obligation, with the result that the remaining rights of the obligee on account of the underlying obligation could be diminished. Moreover, because both the secondary obligor and the obligee would be asserting rights arising from the same undivided claim, conflicting enforcements could easily result. Thus, the secondary obligor is not entitled to subrogation to the right of the obligee until the underlying obligation is completely discharged.

In re Applause LLC, 2006 Bankr. LEXIS 2341, *14-15 (Bankr. Cen. D. Cal. 2006) (citing Restatement (Third) of Surety and Guaranty, § 27(1), Comment b).

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27 As argued in the Jefferson County Warrantholders' Objection, see pp. 23-24, requiring Claimholders to turn over the property that secures only the payment of their insured obligations so that the collateral may be shared by other claimholders in unrelated transactions would be subject to challenge as a taking of the Claimholders' property in violation of the Fifth and Fourteenth Amendments to the United States Constitution as well as Article 1, Sections 6 and 7 of the New York Constitution.

CONCLUSION

For the foregoing reasons, the Trustee respectfully requests that the Court deny approval of the Proposed Plan absent modifications to address the Trustee's objections and grant such other and further relief as the Court deems just and proper. The Trustee reserves the right to join in the Amended Objections served by other parties.

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