

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

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ABN AMRO BANK N.V.; BARCLAYS BANK :
PLC; BNP PARIBAS; CALYON; CANADIAN :
IMPERIAL BANK OF COMMERCE; CITIBANK, :
N.A.; HSBC BANK USA, N.A.; JPMORGAN :
CHASE BANK, N.A.; KBC INVESTMENTS :
CAYMAN ISLANDS V LTD.; MERRILL LYNCH :
INTERNATIONAL; BANK OF AMERICA, N.A.; :
MORGAN STANLEY CAPITAL SERVICES INC.; :
NATIXIS; NATIXIS FINANCIAL PRODUCTS :
INC.; COÖPERATIVE CENTRALE RAIFFEISEN- :
BOERENLEENBANK B.A., NEW YORK :
BRANCH; ROYAL BANK OF CANADA; THE :
ROYAL BANK OF SCOTLAND PLC; SMBC :
CAPITAL MARKETS LIMITED; SOCIÉTÉ :
GÉNÉRALE; UBS AG, LONDON BRANCH; and :
WACHOVIA BANK, N.A., :
:

Petitioners, :

- against - :

ERIC DINALLO, in his capacity as Superintendent :
of the New York State Insurance Department, the :
NEW YORK STATE INSURANCE :
DEPARTMENT, MBIA INC., MBIA INSURANCE :
CORPORATION, and NATIONAL PUBLIC :
FINANCE GUARANTEE CORPORATION (f/k/a :
MBIA INSURANCE CORP. OF ILLINOIS), :
:

Respondents. X

Index No. 601846/09

Hon. Barbara R. Kapnick

**SUR-REPLY AFFIDAVIT OF
JOSEPH W. BROWN**

JOSEPH W. BROWN, being duly sworn, deposes and says:

1. I am the Chief Executive Officer of MBIA Inc. I submit this affidavit on behalf of respondents MBIA Inc. and its operating insurance company subsidiaries, MBIA Insurance Corporation (“MBIA Insurance”) and National Public Finance Guarantee Corporation (f/k/a MBIA Insurance Corporation of Illinois) (“MBIA Illinois”) (collectively, “MBIA”), in further opposition to petitioners’ (the “Banks”) Article 78 petition. This affidavit is based on my

personal knowledge and review of certain documents maintained by MBIA, as well as my discussions with other employees of MBIA.

2. I have spent much of the past twelve years as either a member of MBIA's most senior management or as a member of the Board of Directors of MBIA Inc. From January 1999 to May 2004, I was the Chief Executive Officer of MBIA Inc. I resigned from that position in 2004, but continued on as the Executive Chairman of MBIA Inc. until May 2007, a position I had held since May 1999. In May 2007, I resigned as Executive Chairman of MBIA Inc. At the request of the Board of Directors of MBIA Inc., I returned to the company in February 2008 as the Executive Chairman and Chief Executive Officer.

3. Following my return to MBIA, the company proposed to respondent Eric R. Dinallo, then-Superintendent of the New York State Insurance Department (the "Superintendent"), and the New York State Insurance Department (collectively with the Superintendent, the "NYID") a series of transactions (collectively, the "Transformation") that restructured MBIA's insurance businesses. Set forth below, I respond to certain of the Banks' principal incorrect assertions, including mischaracterizations of my public statements and communications, which were not addressed in my deposition testimony in this proceeding.

**A. MBIA Implemented The Transformation To Establish
A Separate Municipal Bond Insurer That Would Unfreeze The Market**

4. The Banks and their experts repeatedly suggest that MBIA implemented the Transformation so that I and other senior executives, as well as MBIA Inc.'s shareholders, could benefit financially at the expense of the structured-finance policyholders of MBIA Insurance. (See Banks' Reply 3, 4, 87, 133-34; Muhl Aff. ¶ 13; Stewart Aff. ¶ 8; Serio Aff. ¶ 14-16; Stulz Aff. ¶ 4.) This is not correct.

5. The Transformation was implemented in order to establish a viable, separate public finance bond insurance company able to write new business and, consequently, unfreeze the public finance bond market (*i.e.*, insurance for towns, cities, states and other municipalities). As a result of the crisis in the global financial markets that began in 2007, the rating agencies threatened to downgrade MBIA below its triple-A rating and thus MBIA was required to raise additional capital in late 2007 and early 2008 at rates that were prohibitively high. Based on these factors, even before I returned to MBIA in February 2008, I believed that MBIA's business model needed to be restructured so that MBIA was operating its insurance businesses from two independent companies. Specifically, it was my view that MBIA Insurance's mixed portfolio of, among other things, public finance bonds and structured finance products created uncertainty for the rating agencies, investors and potential customers as to the financial outlook for the company, all of which made it difficult, if not impossible, to maintain MBIA Insurance's triple-A rating. Conversely, I believed that operating the two insurance businesses from distinct platforms would allow MBIA to segregate its risks and increase policyholder and investor confidence and certainty, decreasing the cost of capital, and, thereby, lowering the cost for preserving each company's credit rating.

6. It thus was clear to me that MBIA, and the financial guarantor industry as a whole, could not continue operating on a single platform business model, but instead needed to separate its structured finance and public finance businesses in order to attain the proper ratings from the rating agencies. That most companies in the financial guarantee industry, including MBIA Insurance, were downgraded by the principal rating agencies by the middle of 2008 reinforced my belief that a restructuring of MBIA's business was necessary. The ratings downgrades made it practically impossible for MBIA Insurance to write any new insurance,

leaving it unable to serve the U.S. public finance markets because, at the time, most municipalities required insurance with a triple-A rating. This withdrawal of insurance capacity had the effect of freezing out many municipal and state issuers from the public finance bond market.

7. Accordingly, the objectives of the Transformation were therefore simple: (1) establish MBIA Illinois as a separate insurance company that only insures domestic public finance obligations, thereby unfreezing the public finance bond market; (2) preserve MBIA Insurance as a well-capitalized, solvent insurer capable of paying the claims of the structured finance policyholders; and (3) strengthen the entire MBIA franchise for all shareholders, policyholders and investors. Nonetheless, the Banks quote a February 17, 2009 e-mail in which I stated: “I need somebody to push the wheelbarrow across the bank vault” to support their assertion that the “Transformation was structured to enrich MBIA Inc. and its executives and shareholders, at the expense of Petitioners’ and other MBIA Insurance structured-finance policyholders.” (Banks’ Reply 3; RX 84 (WP0019230-31); *see also* Banks’ Reply 86.)

8. The Banks’ characterization of this e-mail is flatly wrong. My statement referred not to any personal financial gain resulting from the Transformation, but was simply a colorful reference to the transfer of funds from MBIA Insurance to MBIA Illinois that occurred as part of the Transformation.

9. Further, the Banks and their experts contend that I and other senior executives received “*massive* bonuses” in 2009 for our efforts in obtaining approval of the Transformation. (Banks’ Reply 86-87, 133; Stewart Aff. ¶ 45; Serio Aff. ¶ 71; Stulz Aff. ¶ 52.) As an initial matter, in 2009, I did not receive any bonus. Moreover, the bonuses given to other members of MBIA’s senior management were based upon a number of factors, including, among other

things, proper capitalization of the MBIA entities, maintaining a stable liquidity position, and retaining and attracting talent, each of which was assigned a relative weight. (RX 82 (MBIA_Plenary_11419553-589); RX 75 (MBIA, Inc. Definitive Proxy, March 20, 2009) 13.) While the “de-stacking” of MBIA Insurance and MBIA Illinois was a factor in the calculation of those bonuses, it was assigned a relative weight of only four percent. (RX 82 at 565.)

10. Likewise, the Banks’ and their experts’ assertions that the stock grants I received on February 18, 2009 were a result of the Transformation are not true. (Banks’ Reply 3, 86, 133; Stewart Aff. ¶ 45; Serio Aff. ¶ 71, Stulz Aff. ¶ 52.) As an initial matter, that I received those stock grants on February 18, 2009, the day after the Transformation was approved, is pure coincidence. Those stock grants were approved, in connection with my return to the company, by MBIA Inc.’s independent board of directors in February 2008, more than nine months before the Transformation application was even submitted to the NYID, and were approved by MBIA’s shareholders in May 2008, more than six months before the Transformation application was submitted to the NYID. The terms of those stock grants provided that I would receive a portion of the grant upon my return to MBIA -- on February 16, 2008 -- and the remainder one year thereafter on February 18, 2009. (RX 74 (MBIA Inc. Definitive Proxy Statement, March 28, 2008) 16.) The stock grants referenced by the Banks were not connected in any way to the NYID’s approval of the Transformation. (RX 76 (MBIA Inc. Form 8-K, February 19, 2008) 2.) This is confirmed by the very authority cited by the Banks and their experts. (Banks’ Reply at 134 (citing RX 75 (MBIA Inc. Definitive Proxy Statement, March 20, 2009) 15-16); Serio Aff. ¶ 71 (same); Stulz Aff. ¶ 52 (citing MBIA Inc. Definitive Proxy Statement, March 28, 2008, p. 16; MBIA Inc. Definitive Proxy Statement, March 20, 2009, p. 16).)

B. The Banks Assert Incorrectly That MBIA Implemented The Transformation To Pressure Bank Counterparties To Commute

11. Throughout their papers, the Banks and their experts quote out of context various statements I made to suggest that MBIA pursued the Transformation in order to pressure bank counterparties to enter into commutations. (Banks' Reply 3, 86; Stewart Aff. ¶ 44; Stulz Aff. ¶ 119; Corcoran Aff. ¶ 57.) This insinuation is incorrect. As set forth above, MBIA implemented the Transformation, primarily, in order to allow MBIA to write new public finance bond insurance business in the wake of the global financial crisis and the resulting freeze in the municipal bond market.

12. Moreover, the Banks and their experts have misleadingly cited those statements. For example, the Banks and their experts quote, out of context, a single sentence from a multi-page February 18, 2009 *Dow Jones* article, in which I stated: "I would expect some would be far more interested in commuting. . . . They will say, 'Oh my God, there is only \$10 billion instead of \$14 billion or \$15 billion, maybe I better cut a settlement today.'" (RX 83; Banks' Reply 3, 86; Stewart Aff. ¶ 44; Stulz Aff. ¶ 119.) That statement, however, was a response to a direct question by the interviewer as to whether I believed the Banks would be more willing to commute because of the Transformation, and not, as the Banks and their experts suggest, an explanation of why MBIA pursued and implemented the Transformation. I answered this question as such because I believed certain bank counterparties might be more willing to commute following approval of the Transformation because they might incorrectly believe MBIA Insurance, as a smaller company, would have insufficient assets to pay claims as they come due. In fact, after the Transformation, the company remained sufficiently capitalized to pay all of its claims as they come due and has done so to this date.

13. Former Superintendent Corcoran cites a December 5, 2008 e-mail that I sent to Superintendent Dinallo regarding the status of commutation discussions with various bank counterparties, claiming that it shows the Transformation was implemented to “pressure” MBIA Insurance’s structured-finance policyholders to commute. (Corcoran Aff. ¶ 57; RX 78 (MBIA_Plenary_01194872).) That is not correct. As an initial matter, the discussion in the e-mail was completely unrelated to the Transformation. At the time of this e-mail, MBIA and Merrill Lynch were discussing a possible commutation and, as MBIA understood it, Merrill Lynch’s CEO at the time, John Thain, was speaking with Superintendent Dinallo regarding those discussions and commutations with other monoline insurers. (RX 80 (MBIA_Plenary_01195373).) As MBIA’s lead regulator, and given the NYID’s ongoing efforts to address the volatility of the monoline industry’s exposures, keeping Superintendent Dinallo aware of such negotiations was entirely appropriate and indeed necessary. We understood that the NYID was in favor of commutations because they would provide certainty to all parties concerning such volatile exposures. Thus, it was our understanding that the NYID was supportive of such discussions, and wanted to know whether MBIA Insurance and the other monolines would be able to commute any of their structured finance policies. As I testified at my deposition, however, I am unaware as to whether Superintendent Dinallo ever raised these issues with any of MBIA’s structured finance policyholders, including the Banks.

14. Former Superintendent Corcoran also quotes a November 18, 2008 e-mail exchange between Mike Callen, Chief Executive Officer of Ambac Assurance Corp. (“Ambac”), and myself as alleged support for the proposition that MBIA sought to use the Transformation to pressure structured finance policyholders to commute. (Corcoran Aff. ¶ 55; RX 79 (MBIA_Plenary_01195286-87).) While the Banks asked me a question about the contents of

this e-mail at deposition, they did not show it to me. Having now read the e-mail, it is clear that Mr. Corcoran's assertion is wrong. First, the focus of my e-mails to Mr. Callen were the "flaws with trying to solve the [problems facing the] existing and future muni[cipal insurance market] indirectly," not the structured finance business. In fact, as noted in the e-mail, I believed that the Banks were "no longer under any survival threat from the monolines under any outcome."

15. I also believed a government intervention to support the monoline industry, as a whole, -- through a government-backed reinsurance facility, as was discussed at that time -- was unnecessary and harmful to MBIA and its non-Bank structured and public finance policyholders. Specifically, I believed that MBIA was in far better financial shape than the rest of the monoline industry and did not need such government support. Thus, if MBIA was forced to participate in a government-backed reinsurance facility, it would be required to provide funds to support the other monolines and their creditors -- an outcome that would not benefit MBIA or its policyholders. And, if a monoline government-backed reinsurance facility was anything like the government's intervention in AIG, it would unnecessarily benefit the Bank counterparties at the expense of MBIA and its other structured and public finance policyholders. Specifically, I was concerned that, as with the AIG scenario, in any government-backed reinsurance facility for the monolines, the Bank counterparties would be paid one hundred cents on the dollar immediately to "rip-up" their contracts with the monolines, even though, as was the case with MBIA, those Banks were not entitled to such payments, would be paid in full over time by MBIA, and may not even have claims to be paid over time, an outcome that would significantly harm MBIA and its policyholders.

16. Second, I believe that Mr. Callen was referring to his own company, Ambac, when he stated that the "best outcome" would be for his company to be viewed as "near death,"

so that the investment banks would commute at a more reasonable price, were entirely inapplicable to MBIA. I did not, and do not, believe that assessment, even if true for Ambac, is or was true for MBIA. MBIA's financial outlook never resembled that of Ambac. Ambac faced a far worse financial outlook than MBIA, and indeed, it was placed into rehabilitation by its regulator (the Wisconsin Insurance Commissioner) in 2010.

C. MBIA Did Not Believe Superintendent Dinallo Approved The Transformation For Political Reasons

17. The Banks quote select portions of an interview I gave the *Financial Times* in February 2008 and a March 11, 2008 e-mail I sent to claim that MBIA believed Superintendent Dinallo approved the Transformation to further his own political aspirations at the expense of structured finance policyholders. (Banks' Reply 89; RX 85, RX 81 (MBIA_Plenary_01195416-17).) That is false. As the e-mail itself makes clear, my statement simply contrasted Superintendent Dinallo's effort to do something positive -- "save" the monoline insurance industry for all policyholders, which, of course, included protecting the interests of structured finance policyholders -- with the perception of former Governor Spitzer's previous efforts to do something negative -- "destroy" the banking industry. My statement did not reflect, nor did I have, any knowledge that Superintendent Dinallo actually held political aspirations. Rather, it reflected an assumption on my part that, as with the experiences of his predecessors, opportunities for political office would present themselves to him simply as a result of holding a high profile position. At no time did I indicate or suggest that Superintendent Dinallo was acting at the expense of bank policyholders, and nothing in the documents cited by the Banks is to the contrary. Indeed, as I testified at my deposition, I never had any discussions with Mr. Dinallo concerning the impact his approval of the Transformation would have on his political career. (RX 86 (Brown Dep.) 187:22-188:5.)

18. The Banks also quote an e-mail I sent to a colleague shortly after MBIA Insurance was downgraded in which I, offering my impressions of a recent public statement made by Superintendent Dinallo in a *New York Times* article, stated that Superintendent Dinallo “has now publicly opened the door to us to reinsure our existing book into a new company, something he would not consider when I spoke with him February,” as alleged evidence that the NYID initially viewed the Transformation as “unprecedented and controversial.” (Banks’ Reply 30, RX 77 (MBIA_Plenary_01194687-690).) That interpretation could not be further from the truth. It is true that, when I first shared my conceptual understanding of the Transformation with the NYID in February 2008, the NYID preferred to assist MBIA (and the other monoline insurers) in maintaining its triple-A rating and raising further capital, if necessary, rather than establish two separate insurance companies. However, it was apparent from the statement by Superintendent Dinallo that his views changed as the events of 2008 unfolded. Once MBIA lost its triple-A rating, and it became clear that neither MBIA Insurance, nor any other MBIA entity, would be able to write new business, the NYID became more receptive to a variety of restructuring plans, including the Transformation, and less focused on further capital raising by the monolines to try to regain their triple-A ratings.

D. MBIA Did Not Rush The NYID To Complete Its Transformation Review

19. The Banks assert that MBIA rushed the NYID to complete its review of the Transformation application. (Banks’ Reply 75-76.) While I pushed my subordinates to have the Transformation application reviewed as expeditiously as possible, I did so because I believed that it was in the best interests of MBIA to have the Transformation approved as soon as possible. Indeed, absent implementation of the Transformation, MBIA would be unable to write new business, and, in my view, based on the market conditions at the time, the municipal

financial bond market would remain frozen. In addition, based on my experience at MBIA and elsewhere, I also believed that once a company undertakes a major project, particularly a restructuring of its business, it is critical that the project be completed as quickly as possible so that the company's resources can return to operating the business. However, at no time did I or (to my knowledge) any other MBIA employee suggest that the NYID rush its review. Rather, MBIA ensured that the NYID received all the information it needed or requested for its review by providing the NYID with unfettered access to MBIA's records and personnel.

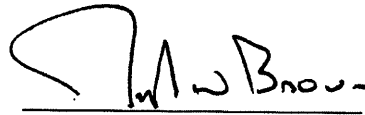
E. MBIA Did Not Engage In A "Rhetorical Campaign" Against The Banks

20. Quoting e-mails dated February 9 and 10, 2009 (RX 69- (MBIA_Plenary_01194986); RX 70 (MBIA_NYS0006109); RX 71 (MBIA_NYS0005897)), the Banks claim that I engaged in a "rhetorical campaign" against the Banks. (Banks' Reply 89-90; *see also* Corcoran Aff. ¶ 51.) This is incorrect. In those e-mails, I shared with Superintendent Dinallo my views concerning the importance of taking steps to provide assistance to the thousands of municipalities and millions of public finance policyholders (a constituency I described as "Main Street") by allowing MBIA's re-entry into the public finance bond market. In sharing this view with Superintendent Dinallo, I contrasted the public finance policyholders (Main Street) with the investment banks and large financial institutions (a constituency I described as "Wall Street"), which already had received hundreds of billions of dollars in bailouts from the federal government. My concern was reinvigorating the municipal bond market, not the unfounded concerns of the entities that had received hundreds of billions of dollars in government assistance. I also attempted to explain to Superintendent Dinallo that it was clear that the federal regulators were working to assist their constituents -- "Wall Street" -- and that no one was assisting "Main Street." I was therefore encouraging Superintendent Dinallo

to take action that, while protecting all of MBIA's structured finance policyholders, also benefitted public finance policyholders and bond holders.

F. MBIA Inc. Has Strong Incentives To Keep MBIA Insurance Solvent

21. Notwithstanding the Banks' suggestions (*see, e.g.*, Banks' Reply 35, 89-90, 133), MBIA Inc. has strong incentives to keep MBIA Insurance solvent rather than simply looting it for cash or allowing it to become insolvent, since the latter strategy would harm the MBIA franchise and MBIA's ability to write more insurance policies through MBIA Illinois. Indeed, MBIA's primary goals through the Transformation were to revive its public finance business through a highly-rated, segregated entity and maintain MBIA Insurance as a solvent, well-capitalized insurance company with sufficient claims paying resources. Nevertheless, MBIA always understood that, even with the separation of the public finance and structured finance businesses, a default by MBIA Insurance on a structured finance obligation would damage the entire MBIA franchise, resulting in, among other things, difficulty for MBIA Illinois to position itself well in the public finance bond insurance industry.


Joseph W. Brown

Sworn to before me
this 16th day of November, 2011


Notary Public

Stella M. Lieberman
Notary Public State of New York
No. 4998416
Qualified in Westchester County
Commission Expires June 29, 2014