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 Seq. No. 004

THE AMENDED OBJECTIONS OF CQS ABS MASTER FUND LTD., CQS SELECT ABS MASTER FUND LTD., AND CQS ABS ALPHA MASTER FUND LTD. TO PLAN OF REHABILITATION FOR FINANCIAL GUARANTY INSURANCE COMPANY

Pursuant to the Orders of this Court dated September 28, 2012 and December19, 2012, CQS ABS Master Fund Ltd., CQS Select ABS Master Fund Ltd., and CQS ABS Alpha Master Fund Ltd. (together, "CQS") hereby objects as follows to the motion of Benjamin M. Lawsky, Superintendent of Financial Services of the State of New York as the Court-appointed receiver of FGIC, for entry of an Order approving a proposed Plan of Rehabilitation for FGIC.

1. CQS objects to Sections 3.5, 4.6, 4.9 and 7.8 of the Plan

2. CQS objects to Exhibit B, Section 1.4(A).

The grounds for the objections are set forth in the accompanying memorandum of law.

Dated: January 22, 2013
New York, New York

Respectfully submitted,

By: ______________________
Thomas M. Mullaney

The Law Offices of Thomas M. Mullaney
275 Madison Avenue, 37th Floor
New York, NY 10016
212-223-0800

Attorney for CQS ABS Master Fund Ltd.,
CQS Select ABS Master Fund Ltd. and CQS
ABS Alpha Master Fund Ltd.

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In the Matter of the Rehabilitation of FINANCIAL GUARANTY INSURANCE COMPANY	))))))	Index No. 401265/2012 Doris Ling – Cohan, J. Motion Seq. No. 004

MEMORANDUM OF LAW IN SUPPORT OF THE AMENDED OBJECTIONS OF CQS ABS MASTER FUND LTD., CQS SELECT ABS MASTER FUND LTD. AND CQS ABS ALPHA MASTER FUND LTD. TO PLAN OF REHABILITATION FOR FINANCIAL GUARANTY INSURANCE COMPANY

CQS ABS Master Fund Ltd., CQS Select ABS Master Fund Ltd. and CQS ABS Alpha Master Fund Ltd. (collectively "CQS"), holders of insurance policies issued by Financial Guaranty Insurance Company ("FGIC"), hereby file this Memorandum of Law in Support of the Amended Objections to the Plan of Rehabilitation for FGIC (the "Plan") proposed by Benjamin M. Lawsky, Superintendent of Financial Services of the State of New York (the "Superintendent"), as the court-appointed rehabilitator (the "Rehabilitator") of FGIC in the above-captioned rehabilitation proceeding, and respectfully submit as follows:

PRELIMINARY STATEMENT

CQS objects to two material provisions of the Plan that render it unfair and inequitable to FGIC's policyholders. As the Rehabilitator has recognized, these two objections are "overlapping" with the "same short list of objections" raised by all of the remaining Objectors. See Omnibus Reply Memorandum of Law in Further Support of Approval of First Amended Plan of Rehabilitation for Financial Guaranty Insurance Company, dated December 12, 2012 ("FGIC Reply"). at 2-3. First, the Plan allows FGIC to regain the right to excess cash flows produced from the underlying securities it has insured – a right only meant for an insurer that is current on payments under its policies – despite the fact that, under the Plan, FGIC proposes to pay its bondholders an amount as low as 15% of their policy claims and then declare itself "current." See id., at 5, 20. This provision would be inequitable because the excess cash flows from the underlying securities, on a net present value basis, exceed the value of FGIC's proposed payments under the Plan for many of the bonds insured by FGIC. Thus, with respect to these bonds, the Plan provides less value to bondholders than either the status quo or a liquidation of FGIC and operates to essentially redistribute cash from those bondholders whose underlying securities are producing excess cash to those bondholders whose underlying securities are not.

Second, the Plan proposes to terminate FGIC's unilateral right under a reinsurance agreement with National Public, an affiliate of MBIA, to (a) "reassume" $138 billion of U.S. municipal bond policies that FGIC ceded to National Public in 2008, and to (b) obtain approximately $500 million in cash from National Public (in the form of related net unearned premiums and any ceded loss reserves on the policies). See id., at 6, 35. These municipal bond policies are good assets, and the right to reassume them should not be given away for nothing. The Plan is giving away a right that could provide FGIC's stakeholders with more than $400 million in excess cash, according to National Public's own most recent claim reserve disclosure (stating that National Public is likely reserving less than $100 million for future claims on these policies). In exchange, FGIC appears to be receiving nothing. Based just on the facts currently in the public record, the Plan's termination of FGIC's "reassumption" right will not maximize value for the benefit of FGIC's policyholders and should not be approved.

I. THE PLAN IS NEITHER FAIR NOR EQUITABLE AND BENEFITS CERTAIN POLICYHOLDERS AT THE EXPENSE OF OTHERS

Under the Plan, FGIC's policyholders are scheduled to receive an upfront cash payment that the Rehabilitator estimates will equate to 15% of each policyholder's claims (defined in the

Plan as the "CPP") while the remaining payment obligation with respect to the policy will be treated as a deferred payment obligation ("DPO"). That 85% payment obligation will be payable only if, when and to the extent FGIC determines, in consultation with a third-party firm and with NYSDFS approval, that is has sufficient assets to make such cash payment. See Plan, Exhibit D (Disclosure Statement) at 21.

By making the CPP payment, and offering a quasi-promise to make a DPO payment, FGIC will declare itself current on its policies, and receive all of the benefits of a contractually-current monoline insurer while abdicating 85% of its obligations. Cf. Affidavit of John S. Dubel, dated December 12, 2012, ("Dubel Aff."), ¶19-23. Some other benefits that FGIC will obtain include voting rights with respect to its insured securities and, most importantly, the right to loss reimbursement, including any excess cash flow from its insured policies. See id. Currently, as a result of FGIC's ongoing default and non-payment on its policies, FGIC's policyholders receive such excess cash flow and enjoy the right to vote such securities. See id., ¶23. Unless and until FGIC actually becomes current on its obligations concerning those policies, those policyholders should continue to receive those benefits, just as they had bargained-for.

That is so because it is unfair and inequitable to pay as little as 15% of overdue policy claims (leaving policyholders to absorb those large losses), declare yourself current, and then take the cash stream currently going to such policyholders (the "excess spread") who bargained to receive those very funds in the event of a default. This would permit FGIC essentially to take funds currently going to certain bondholders in compensation for FGIC's default, and redistribute it to other bondholders who are otherwise not entitled to that money. Cf. id. Also, the 15% CPP has less value (on a present value basis) to bondholders in certain issues than the value of the excess spread such bondholders currently receive from those insured bonds. Cf. id.

The question of how many other bondholders are damaged, and in what amount, is an unknowable question of fact because FGIC refuses to disclose the CPP for each insured security and the impact of the Plan on the cash flow from each such security. What is known about the Plan, however, is that the compensation in the event of a default gets unilaterally cut, and the default is never cured. Moreover, because the DPO is completely at the discretion of the Superintendent and may never be paid, the Plan will redistribute the excess spread to FGIC while bondholders in exchange receive only an entirely voluntary DPO payment based entirely on the potential exercise of discretion of the Superintendent. While the facts necessary to perform an exact quantification are exclusively in the hands of FGIC, the secrecy surrounding them strongly suggests that many bondholders are worse off under the Plan than under either the status quo or a liquidation of FGIC.

This strong inference is further bolstered by the fact that the basic tenets of the current Plan were previously proposed to FGIC policyholders and, not surprisingly, were rejected by a majority of such policyholders. Specifically, in March 2010, FGIC attempted a plan called Sharpes whereby FGIC attempted to pay an upfront (and much larger) "Cash Consent Fee" and a "Surplus Note" in exchange for eliminating FGIC's insurance obligations and FGIC retaining its rights, including its voting right and reimbursement right to excess spread recapture. See Affirmation of Thomas M. Mullaney, dated January 22, 2013 ("Mullaney Aff."), ¶3, attaching the Offer to Exchange of Sharps SP I LLC, dated March 25, 2010 as Appendix A. The Sharps Plan in turn was rejected by a majority of the bondholders on September 30, 2010. See id., ¶4, attaching an October 1, 2013 FGIC press release showing that only 43.2% of bondholders approved the Sharps Plan, as Appendix B. CQS understands that this plan was rejected by bondholders in large part because, many of the bonds were better off, on a present value basis, with the excess spread rather than the cash payment.

Now, two years after the failure of the Sharps Plan, FGIC has put some old wine in a new bottle, and changed the description of the plan terms from "Cash Consideration" and "Surplus Note" to "CPP" and "DPO." Otherwise, the terms remain the same, as FGIC wants to reinstate its voting rights and reimbursement rights for a small-percentage cash payment and the future possibility of another unquantified payment at an unknown later date. As in October 2010, this is not the deal that policyholders want.

To be clear, the concept of an upfront cash payment (i.e., the CPP) and a deferred payment obligation (i.e. the DPO) are acceptable. However, there is nothing fair or equitable with allowing FGIC to regain reimbursement rights – rights meant only for insurers who have paid all outstanding claims on such policies – while its policyholders are left to absorb unpaid and overdue claims but without the compensatory benefit of receiving cash flows on the insured securities.

Rather, a fair and equitable outcome – and one consistent with the parties bargain -- would allow FGIC's bondholders to obtain the CPP and the DPO while continuing to receive the excess spread on the insured securities they own until FGIC has made all past claim payments on such policies (and thus is current). When current on its obligations, FGIC should then begin to receive reimbursement via the excess spread.

II. THE PLAN ELIMINATES A VALUABLE ASSET OF FGIC FOR NO CONSIDERATION TO THE DETRIMENT OF ALL FGIC'S STAKEHOLDERS

The Plan calls for FGIC to terminate its right to "resassume" certain reinsured policies covering certain municipal bonds from National Public. If FGIC to retained and exercised this right, it could obtain approximately $500 million in cash for policies that will require less than

$100 million in cash reserves to pay future losses, based on National Public's own latest municipal bond reserve projections, as approved by the Superintendent. See Section V, paragraph (C)(1) of the Disclosure Statement (entitled "Significant Post-Filing Actions: the Novation of National Public Reinsured Policies"). Even the right to "reassume" such policies standing alone is a valuable asset of FGIC that would materially benefit all policyholders, an asset that may or not have been subject to a "market check" to seek interested bidders – information currently unavailable in the public record. Accordingly, further action should be taken, and analysis provided, before this significant asset is simply discarded for no apparent consideration to FGIC's stakeholders.

It is known that in September 2008, FGIC entered into an agreement (the "Reinsurance Agreement") with MBIA, pursuant to which FGIC ceded to MBIA exposure under policies covering U.S. public finance credits with total net par in force of approximately $188 billion, of which $138 billion remained outstanding as of December 31, 2011 (collectively, the "National Public Reinsured Policies"). Shortly thereafter, National Public, an affiliate of MBIA, replaced MBIA as the party to such transaction and assumed MBIA's obligations thereunder (the "National Public Reinsurance Transaction"). Section 15(v) of the Reinsurance Agreement (see Mullaney Aff., ¶5, Appendix C, attaching September 30, 2008 Reinsurance Agreement) provides that FGIC retains the right, in its sole discretion, to terminate the National Public Reinsurance Transaction and "reassume" the rights and obligations under the National Public Reinsured Policies back from National Public, and to receive the related net unearned premiums and any ceded loss reserves as of such date (the "FGIC Reassumption Right"), upon the occurrence of certain events, including if National Public's credit rating is downgraded below (i) BBB- (as measured by Standard & Poor's Financial Services LLC ("S&P")) or (ii) Baa3 (as measured by Moody's Investors Services, Inc. ("Moody's")).

National Public is currently rated just slightly higher than those minimal levels delineated in the Reinsurance Agreement – earning a BBB rating from S&P and a Baa2 rating (outlook negative) by Moody's. The slightest future downgrade would trigger FGIC's ability to exercise the FGIC Reassumption Right.

MBIA and National Public face a host of legal and financial problems, any one of which could precipitate a ratings downgrade. One, myriad litigations that challenge MBIA's own restructuring in 2009 (that created and funded National Public) remain pending around the nation. Two, MBIA Corp., an affiliate of National Public, is experiencing an on-going diminishing cash position which could easily trouble the ratings agencies further. MBIA recently made a problematic and controversial consent solicitation to its bondholders to amend a provision of the indentures governing its bonds, which provides that if MBIA Corp. were to go into receivership, MBIA Inc. would be in default under such bonds.

Bank of America, however, has since announced a tender offer to purchase many of these bonds, at a premium, in an attempt to defeat this consent solicitation. See Mullaney Aff., ¶6, attaching the Offer to Purchase by Bank of America Corporation dated November 13, 2012 as Appendix D. MBIA has warned that if the consent solicitation fails, MBIA Inc. may be forced to file a chapter 11 bankruptcy case in the event MBIA Corp. goes into receivership. Id., ¶7, attaching the MBIA Inc. Consent Solicitation Statement dated November 7, 2012 as Appendix E, at 10 ("The Company believes the Proposed Amendments will be beneficial to the Company and its creditors, including Holders of the Notes, because they will remove the possibility of a

Subsidiary Insolvency Default in the event that MBIA Corp. is placed into rehabilitation or liquidation proceedings, the result of which could be a Company [MBIA Inc.] Bankruptcy.")

Additionally, National Public has a $1.6 billion loan outstanding to MBIA Corp. and MBIA has warned that repayment of such loan could be jeopardized if MBIA Corp. were to go into receivership. See id., ¶8, Appendix E, at 11 ("Additionally, a significant part of the value of National is made up of intercompany receivables, including a $1.6 billion secured loan to MBIA Corp. that may be impaired in the event that MBIA Corp. is in a rehabilitation or liquidation proceeding...") Accordingly, with all the litigation and potential pitfalls surrounding MBIA and National Public, National Public could very well be downgraded below the investment grade level in the near future, which would provide an opportunity for FGIC to exercise its Reassumption Right.

The municipal assets that FGIC would acquire upon exercise of the Reassumption Right are of high quality. In fact, according to its National Public's Q3 2012 Operating Supplement, National Public has established loss reserves of approximately $165 million on $356 billion of outstanding bonds. See Mullaney Aff., ¶9, attaching National Public's Q3 2012 Operating Supplement as Appendix F. Assuming such loss reserves are spread evenly among the insured bonds, National Public would have established loss reserves of approximately $64 million on the remaining $138 billion of FGIC municipal bonds it has reinsured. Subtracting this $64 million loss reserve from the approximately $500 million in capital would provide approximately $435 million of value for FGIC's policyholders. Id., ¶10, attaching the MBIA press release of October 1, 2008 as Appendix G ($500 million is an estimate based on the amortization of the bonds, as MBIA received $639 million for reinsuring FGIC's municipal business in 2008). The Rehabilitator has the underlying data necessary to verify these estimates in its exclusive possession, and should disclose it and its own analyses. This would include a detailed analysis[1] of the value of the municipal bonds under the Reassumption Right that illustrates the current balance outstanding and the loss reserves associated with the policies.

Further, if the Superintendent has proposed terminating the Reassumption Right because he is concerned about the municipal policyholders under the reassumed policies being exposed to FGIC's structured-finance obligations, such municipal bondholders can be put in a subsidiary of FGIC like the "drop-down" or "stacked" company that was created for municipal bondholders in Syncora. Or, FGIC could see if someone would buy the "Reassumption Right" from it.

In sum, the Reassumption Right is a call option with enormous value. To give this option away for free is clearly not in the best interest of any FGIC policyholder. Accordingly, CQS submits that the Rehabilitator should provide policyholders with data establishing this value, and confirmation that it has attempted to realize this value. If the Rehabilitator fails to do so or such analysis confirms that FGIC is indeed forgoing substantial value in terminating the Reassumption Right, the Plan should be denied.[2]

RESERVATION OF RIGHTS AND JOINDER

CQS expressly reserves all of its rights to object to supplement this Objection, to object to the Plan at the Plan Approval Hearing on any further grounds, take discovery regarding the Plan, and cross-examine any witnesses at the Plan Approval Hearing. CQS joins the amended objections of The Bank of New York Mellon and The Bank of New York Mellon Trust

[1] On October 9, 2012 the Steering Committee conducted a conference call for the benefit of all structured finance policyholders. On that call the objection to Novation of the National Public Reinsured Policies was raised and is was decided that FGIC's financial advisors would provide a cost benefit analysis of the reinsured municipal business. As of the date of this Objection, that information has not been provided.

[2] Further, CQS again requests that the Superintendent reveal the bids from the 2008 sale of FGIC's municipal business to allow policyholders to gauge potential current interest in such business. CQS understands that National Public may not have submitted the highest bid for this business.

Company, N.A. (together, "BYNM"), Jefferson County, Alabama Warrant Holders ("JeffCo"), Childrens Health Partnership Holding Pty Ltd ("CHP"), and Aurelius Capital Management, LP ("Aurelius") which also speak to the issues raised above. The Rehabilitator has recognized that these arguments coincide with CQS', (See FGIC Reply, at 20-22, 35-38), and so repetition of them here would serve no purpose and inflict no prejudice.

CONCLUSION

WHEREFORE, for the foregoing reasons, CQS requests that the Court (1) deny approval of the Plan absent the modification requested herein, and (2) grant such other relief which it deems just and proper.

Dated: January 22, 2013
New York, New York

Respectfully submitted,

B y: ______________________________
Thomas M. Mullaney

The Law Offices of Thomas M. Mullaney
275 Madison Avenue, 37th Floor
New York, NY 10016
212-223-0800

Attorney for CQS ABS Master Fund Ltd., CQS Select ABS Master Fund Ltd. and CQS ABS Alpha Master Fund Ltd.

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AFFIRMATION OF THOMAS M. MULLANEY

1. THOMAS M. MULLANEY, an attorney admitted to practice law in the courts of the State of New York, affirms the following under the penalties of perjury.

2. I counsel for objectants CQS ABS Master Fund Ltd., CQS Select ABS Master Fund Ltd., and CQS ABS Alpha Master Fund Ltd ("CQS"). I am fully familiar with the facts and circumstances set forth herein. This Affirmation is based upon my personal knowledge, and review of the relevant documents in this case.

3. A true and correct copy of the "Sharps Plan" is attached as Appendix A.

4. A true and correct copy of an October 1, 2013 FGIC press release showing that only 43.2% of bondholders approved the Sharps Plan is attached as Appendix B.

5. A true and correct copy of the National Public Reinsurance Agreement is attached as Appendix C.

6. A true and correct copy of the Offer to Purchase by Bank of America Corporation dated November 13, 2012 is attached as Appendix D.

7. A true and correct copy of the MBIA Inc. Consent Solicitation Statement dated November 7, 2012 is attached as Appendix E, at 10 ("The Company believes the Proposed Amendments will be beneficial to the Company and its creditors, including Holders of the

Notes, because they will remove the possibility of a Subsidiary Insolvency Default in the event that MBIA Corp. is placed into rehabilitation or liquidation proceedings, the result of which could be a Company [MBIA Inc.] Bankruptcy.").

8. Additionally, National Public has a $1.6 billion loan outstanding to MBIA Corp. and MBIA has warned that repayment of such loan could be jeopardized if MBIA Corp. were to go into receivership. Appendix E, at 11 ("Additionally, a significant part of the value of National is made up of intercompany receivables, including a $1.6 billion secured loan to MBIA Corp. that may be impaired in the event that MBIA Corp. is in a rehabilitation or liquidation proceeding...").

9. A true and correct copy of National Public's Q3 2012 Operating Supplement is attached as Appendix F.

10. A true and correct copy of the MBIA press release of October 1, 2008 is attached as Appendix G ($500 million is an estimate based on the amortization of the bonds, as MBIA received $639 million for reinsuring FGIC's municipal business in 2008).

Dated: New York, New York
January 22, 2013

THOMAS M. MULLANEY