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February 28, 2013

VIA HAND DELIVERY

Clerk of the Court
Michigan Court of Appeals
Michigan Hall of Justice – 2nd Floor
925 W. Ottawa Street
P.O. Box 30022
Lansing, MI 48909

Re: **Ken Ross, Commissioner of the Office of Financial and Insurance
Regulation v. American Community Mutual Insurance Company
Court of Appeals N. 312470
(Ingham Circuit Court No. 10-387-CR)**

Dear Clerk:

Enclosed for filing in the above referenced case are the original and four (4) copies of the JOINDER AND BRIEF OF APPELLEE HOLDCO ADVISORS, L.P., AS MANAGER AND POWER OF ATTORNEY FOR SURPLUS NOTEHOLDER FINANCIALS RESTRUCTURING PARTNERS, LTD., IN SUPPORT OF DENIAL OF FORMER OFFICERS' CLAIMS FOR SEVERANCE AND OTHER POST-TERMINATION BENEFITS UNDER PRE-REHABILITATION EXECUTIVE EMPLOYMENT AGREEMENTS in regard to the above-referenced file number. I have also enclosed a Proof of Service. These documents are being submitted to the court via hand delivery.

Very truly yours,



Daniel R. Brown

Enclosures

c Phillip Sternberg
Lori McCallister
Christopher Kerr

DEPT. OF
ATTORNEY GENERAL

MAR 04 2013

CORPORATE OVERSIGHT
RECEIVED

STATE OF MICHIGAN
IN THE COURT OF APPEALS

KEN ROSS, COMMISSIONER OF THE OFFICE
OF FINANCIAL AND INSURANCE
REGULATION,

Petitioner,

Court of Appeals No. 312470

Ingham Circuit Court No. 10-397-CR

[IN REHABILITATION]

v

AMERICAN COMMUNITY MUTUAL
INSURANCE COMPANY,

Respondent.

In re: the Matter of:

AMERICAN COMMUNITY MUTUAL INSURANCE
COMPANY'S FORMER OFFICERS MICHAEL TOBIN,
ELLEN DOWNEY, FRANCIS DEMPSEY, MICHAEL
McCOLLOM, BETH McCROHAN, and LESLIE GOLA,

Claimants/Appellants,

v

OFIR COMMISSIONER, AS REHABILITATOR OF
AMERICAN COMMUNITY MUTUAL INSURANCE COMPANY,

and

SURPLUS NOTEHOLDERS TRAPEZA CDO IX, LTD. AND
CDO X, LTD., and HOLDCO ADVISORS, L.P., on behalf of SURPLUS NOTEHOLDER
FINANCIALS RESTRUCTURING PARTNERS, LTD.,

Respondents/Appellees.

**JOINDER AND BRIEF OF APPELLEE HOLDCO ADVISORS, L.P., AS MANAGER
AND POWER OF ATTORNEY FOR SURPLUS NOTEHOLDER FINANCIALS
RESTRUCTURING PARTNERS, LTD., IN SUPPORT OF DENIAL OF FORMER
OFFICERS' CLAIMS FOR SEVERANCE AND OTHER POST-TERMINATION
BENEFITS UNDER PRE-REHABILITATION EXECUTIVE EMPLOYMENT
AGREEMENTS**

ORAL ARGUMENT REQUESTED

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Dated: February 28, 2013

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STATEMENT OF JURISDICTION

Respondent-Appellee the HoldCo Advisors, L.P., as manager and power of attorney for Financials Restructuring Partners, Ltd., agrees with the Claimants-Appellants' statement of jurisdiction.

COUNTER-STATEMENT OF QUESTIONS PRESENTED

1. In the rehabilitation of a financially troubled insurance company under Chapter 81 of the Insurance Code, MCL 500.8137(4) limits claims made under pre-rehabilitation employment contracts by the officers and directors of the failed insurer to “payment for services [they] rendered prior to the issuance of” the rehabilitation order. This statutory limitation on “insider” claims requires that the purpose of a claimed payment must be in direct exchange “for services rendered prior to” entry of the rehabilitation order. Here, six former officers of American Community, who remained employed at the company when the rehabilitation order was entered, have made claims against the rehabilitation estate for severance and other non-wage, post-termination benefits arising under their pre-rehabilitation “golden parachute” agreements. Did the Rehabilitator and circuit court correctly decide that MCL 500.8137(4) bars payment of these claims?

Appellants’ answer: No.

Appellees’ answer: Yes.

Trial court’s answer: Yes.

2. American Community’s former management reviewed, approved, and stipulated to the rehabilitation order, which provides consistent with MCL 500.8137(4) that “the Rehabilitator shall not pay” any severance or other non-wage claims arising under an officer’s pre-rehabilitation employment contract. In addition to their claims being legally barred under MCL 500.8137(4), did the Rehabilitator and circuit court properly deny the former officers’ claims for severance and other non-wage, post-termination benefits under their pre-rehabilitation golden

parachute agreements because the rehabilitation order they agreed to expressly prohibits these claims?

Appellants' answer: No.

Appellees' answer: Yes.

Trial court's answer: Yes.

3. MCL 500.8137(4) evidences the Legislature's determination that when an insurance company fails, the officer and director insiders who managed the company to financial collapse should not be rewarded with severance and other non-wage, post-termination benefits that they granted themselves in pre-rehabilitation golden parachute agreements. The statute is supported by sound public policy, where a contrary rule requiring payment of these claims: (a) sets bad precedent for future insurance receiverships, both in Michigan and in other states with comparable receivership laws; (b) creates perverse incentives for those currently running insurance companies; and (c) unfairly subjects the claims of legitimate creditors to the risk of non-payment or greatly reduced payments, which in turn could diminish insurers' access to capital and result in more insurance company receiverships. Given these policies supporting the Legislature's enactment of MCL 500.8137(4), did the Rehabilitator and circuit court correctly enforce the statute as written to deny payment of the former officers' claims?

Appellants' answer: No.

Appellees' answer: Yes.

Trial court's answer: Yes.

CONSTITUTIONAL PROVISIONS, STATUTES, RULES INVOLVED

MCL 500.8137 Contingent claims; discounting claims at legal rate of interest; claims made under employment contracts.

Sec. 8137.

* * *

(4) Claims made under employment contracts by directors, principal officers, or persons in fact performing similar functions or having similar powers are limited to payment for services rendered prior to the issuance of an order of rehabilitation or liquidation under section 8113 or 8118.

INTRODUCTION

HoldCo Advisors, L.P. (“Holdco”) joins in the briefs of the Rehabilitator and fellow surplus noteholders Trapeza CDO IX, Ltd. and CDO X, Ltd. (“Trapeza”) in all respects. Holdco files this separate brief solely to highlight two points.

First, the Appellants’ have no legs to stand on when arguing that the retention inducements provided by American Community Mutual Insurance Company (“American Community”) were provided in exchange “for services rendered.” Their expansive, virtually limitless construction of “payment for services rendered” essentially provides that any consideration provided by an employer to an employee under a contract is a “service rendered.” Case law is clear, however, that non-“service” consideration, such as agreeing to stay on as an employee, is distinct from “rendering services.” Indeed, compensation for rendering services is limited to ordinary wage, salary, and benefits. This limitation makes complete sense, especially in light of MCL 500.8137. If senior executives could simply hang around as a company fails and get paid huge incentives on the back end, the statute is rendered meaningless, and prohibits almost no payments to insiders.

Second, these managers that now seek nearly \$3 million in “golden parachute” benefits are the same managers that oversaw the demise of a previously healthy insurance company. It is simply bad policy to allow them to hand themselves handsome rewards for this failure, especially at the expense of the company’s creditors.

For those reasons, as well as the numerous reasons outlined in the briefs of Trapeza and the Rehabilitator, the Appellant’s claims were properly denied, and the decision below should be affirmed.

COUNTER-STATEMENT OF FACTS

Holdco adopts in full Counter-Statement of Facts contained in the Rehabilitator's brief, and hereby incorporates such statement as if fully set forth herein.

PROCEEDINGS BELOW

Holdco adopts in full the Rehabilitator's statement regarding the proceedings below, and hereby incorporates such statement as if fully set forth herein.

ARGUMENT

I. Standard of Review

The central question here is one of statutory interpretation: does MCL 500.8137 prohibit the Appellants' claims? This Court reviews questions of statutory interpretation *de novo*.

Kuznar v Raksha Corp, 481 Mich 169, 176 (2008).

II. MCL 500.8137 Disallows the Appellants' Claims Because the Consideration Provided for the Severance and Change-In-Control Bonuses Was Staying on With the Company

The crux of Appellants' argument is that the "services rendered" to American Community were some combination of staying with the company during troubled times and not leaving for more secure employment. (*See* App. Br., p. 10.) This consideration provided by the Appellants, however, was not "services rendered" to American Community. Not all consideration provided under a contract – including employment contracts – is *de facto* considered "services rendered" to the employer. Instead, that term has an ordinary and plain meaning: "services rendered" are the day-to-day work performed for or on behalf of the company. The type of compensation that you get for "services rendered", quite obviously, is wages, salary, and benefits. Agreeing to remain in someone's employ, however, is not itself

“services rendered.” And, consistently, lump-sum severance and other inducements to stay at a particular a job are a not payments “for” services rendered.

The Appellants’ own authorities even make this principle clear. In *Mason v. Official Comm of Unsecured Creditors (In re FBI Distribution Corp.)*, the First Circuit explained that severance payments and other inducements to join or remain with an employer other than ordinary wages or salary – the exact same consideration that the Appellants claims is “services rendered – do not constitute claims for services rendered. 330 F.3d 36 (1st Cir. 2003). In that case, Mason was lured away from high-paying employment to help save a failing company. *Id.* at 39-40. As an inducement, the failing company offered her a cushy “golden parachute” package, including a severance and a “change of control” bonus. *Id.* The company still failed and filed bankruptcy, and Mason stayed on even after the failure. *Id.* Then, after being terminated during the bankruptcy case, Mason sought payment of severance and “change of control” benefits. *Id.* at 40-41. If such payments were for services that Mason had rendered to the debtor during her post-petition employment, then they would be entitled to administrative priority under the Bankruptcy Code, and Mason would be paid the full amount. *Id.* at 46-47. If they were not for services rendered, then they could not qualify for priority. *Id.*

As the Appellants highlight, the *Mason* court determined that Mason had a *claim* against the estate for the promised severance and bonus, but, as the Appellants have chosen to ignore, such claim was *not a claim for services rendered*. As the First Circuit explained:

. . . Mason stated that the severance provisions in her Employment Agreement and Retention Agreement were part of the inducement to leave her high-paying position at Home Goods. Unlike severance or vacation benefits geared to length of service--benefits that clearly constitute a part of an employee's wages for services rendered . . . *the severance benefits here do not constitute any part of her compensation for services rendered. Whether she worked two minutes or thirty-five and one-half months after executing the Employment Agreement, she was entitled to in excess of*

\$1.2 million if she were terminated without cause. In fact, by the literal terms of the agreement, it appears that she was entitled to over \$ 1.2 million regardless of whether she rendered any services whatsoever. Her compensation for services rendered simply did not include severance pay As should now be clear, however, we hold that Mason's severance pay was not a component of compensation for services she rendered and thus is not entitled to administrative priority.”

Id. at 46-47 (citations omitted).

The question answered by the First Circuit in *Mason* is the central question before the Court in this case, and the same conclusion is warranted. Here, as in *Mason*, the Appellants may have provided pre-rehabilitation ***consideration*** for the severance and change-in-control bonuses they now seek,¹ but such consideration was ***not*** “for services rendered.” As they themselves claim throughout their opening brief “American Community promised specific compensation to the Petitioners ***if they stayed and continued*** to render services” (App. Br., p. 10.) The “staying and continuing” was the consideration provided, not the actual rendering of services. As the *Mason* court makes quite clear, “staying and continuing” is indeed distinct from the actual “rendering of services.” The compensation for rendering services is not severance or change-in-control bonuses, but rather regular wages or salary, and benefits. *See Mason*, 330 F.3d at 48 (“Of course, Mason is entitled to receive the reasonable value of the beneficial services rendered during the reorganization. For these services, she was fully compensated by the debtor in possession: she received her full salary plus fringe benefits pursuant to the terms of her Employment Agreement for all the services she rendered”).

The *Mason* court’s conclusion is clear: not all consideration provided by an employee under an employment contract is consideration for “services rendered,” and the mere agreement

¹ Even this assertion is dubious at best, and Holdco rejects any argument that the Appellants provided any re-failure consideration that gives rise to a valid claim in the rehabilitation proceeding.

to stay employed in exchange for valuable inducements like severance and change-in-control bonuses does not qualify as “services rendered.” Here, the Appellants were offered large bonuses to stay with the company. They received *separate* compensation, however, to actually “render services” – namely their large executive salaries and related benefits. Their agreement to stay with the company, however, was not “services rendered,” and, as a result, MCL 500.8137 applies and disallows the claim.

The principle of *Mason* and MCL 500.8137 – limiting payment “for services rendered” to ordinary wages and salary – has been echoed in numerous bankruptcy cases examining the same issue. For example, in *Supplee v. Bethlehem Steel Corp. (In re Bethlehem Steel Corp.)*, the Second Circuit explained that severance payments are compensation for the termination of employment, not for the services leading up to it:

[S]everance payments are a form of compensation for the termination of the employment relation . . . primarily to alleviate the consequent need for economic readjustment but also to recompense [the terminated parties] for certain losses attributable to the dismissal. The severance payment at issue . . . did not accrue day to day over the course of employment, but rather was triggered by termination, and as such it represented a new benefit payable because of termination

479 F.3d 167, 173 (2d Cir. 2007).

The Fourth Circuit reached the same conclusion in *Matson v. Alarcon*, highlighting the uniqueness of severance payments as compensation for termination, in contrast with ordinary wages as compensation for services rendered:

The purpose of such severance compensation is to alleviate the consequent need for economic readjustment and to recompense [the employee] for certain losses attributable to the dismissal [E]mployees do not ‘earn’ ‘severance pay’ in exchange for services rendered as they do when they ‘earn’ wages, salaries, and commissions. Rather, employees receive ‘severance pay’ as compensation for the injury and losses resulting from the employer’s decision to terminate the employment relationship.

651 F.3d 404, 409 (4th Cir. 2011) (citations and quotes omitted); *see also In re Eutsler*, Case No. 11-31133, 2012 Bankr. LEXIS 90, at *6 (W.D.N.C. Jan. 5, 2012) (“[A] severance package [is] earned on the date the employee became entitled to receive such compensation.”) (citations and quotes omitted); *Straus-Duparquet, Inc. v. Local Union No. 3, Int'l B'hood of Elec. Workers*, 386 F.2d 649, 651 (2d Cir. 1967). (“Severance pay is not earned from day to day and does not ‘accrue’ so that a proportionate part is payable under any circumstances. After the period of eligibility is served, the full severance pay is due whenever termination of employment occurs . . . [S]everance pay is compensation for termination of employment.”).

Thus, the First Circuit in *Mason*, the Second Circuit in *Bethlehem Steel*, and the Fourth Circuit in *Alarcon* have already made quite clear that payment for “services rendered” does *not* include severance and change-in-control bonuses. The context here may be slightly different, but the principle is the same. The Appellant’s claims are not claims for services rendered. Thus, MCL 500.8137 disallows the claims. The court below did not err in reaching this conclusion.

The Appellants, confusingly, cite *Mason* as a case supporting their position. Their misplaced reliance on this case, however, exposes the fatal flaw with their argument. They fail to grasp that under bankruptcy law there is no automatic disallowance of severance and bonus claims like that required under MCL 500.8137. Indeed, the definition of “claim” under the Bankruptcy Code is intentionally expansive:

The term “claim” means—

- (A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured;
- (B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured.

11 U.S.C. § 101(5); *see also* 2-101 Collier on Bankruptcy P 101.5 (explaining that “claim” is broadly defined under the bankruptcy to be “coextensive with the term “debt”).

Thus, if this was a *bankruptcy* case, the Appellants could potentially assert a general, unsecured “claim” for the amounts owed under the severance and change-in-control provisions. Such claim, however, would not be on account of services rendered. And since this is not a bankruptcy case, and MCL 500.8137 governs, the Appellants’ claim was rightfully disallowed.

III. Payment of the Appellants’ Claims Is Against Public Policy Because Executives Should Not Be Able to Reward Themselves on the Eve of Their Company’s Failure

The *Mason* court also highlighted a concern raised by the Rehabilitator here: without limitations on the concept of “services rendered,” company managers could give themselves sweetheart deals before a failure, and then collect on the way out at the expense of creditors. Specifically, the *Mason* court explained that under the Appellants’ argument, “an executive would be entitled to administrative priority for lump-sum severance pay, no matter how astronomical, simply by working one day for the debtor in possession so long as she was in good standing at the time of the discharge.” 330 F.3d at 46. The First Circuit held that “we cannot accept this conclusion.” *Id.*; *see also In re AppliedTheory Corp.*, 312 B.R. 225, 241 (Bankr. S.D.N.Y. 2004) (Severance payments were “not a measure of the value of the services the Executives provided to the estate. While the Executives introduced proof that during the time they remained employed by the Debtors . . . they provided valuable services, they introduced no proof that their salaries were less than a fair exchange for the work they performed during that time, and, in particular introduced no proof that that there was any nexus between . . . the doubled or quadrupled compensation they would receive for *not* working.”).

Indeed, it is precisely this concern that underpins MCL 500.8137. Company executives wield far too much sway over compensation decisions to have their “golden parachute” benefits

paid out after the company fails. The holders of the \$30 million of surplus notes – obligations undertaken by American Community long before its failure – should not have their recoveries diminished by the payment of bonuses to the company’s failed management team. The mismanagement of the company by its officers, however, has cut recoveries on the Surplus Notes nearly in half of their face value. Yet these same officers now seek to further reduce these recoveries by nearly \$3 million – \$3 million essentially sought as a reward for failing to prevent the company’s collapse.

The management team’s overreaching is highlighted by their claims for the “enhanced” benefits that allegedly come along with a “change of control.” They assert that the rehabilitation itself constitutes a “change of control” entitling them to an even greater payout. Not only is this flatly and obviously wrong, it is insulting to the creditors that are scrambling to limit their losses in the wake of this management team’s incompetence. For one, the obvious intended meaning of “change in control” is a change of control resulting from the sale or merger of the company – hence the constant reference to a “transaction” – not from the company’s failure and the resulting rehabilitation proceeding. No fiduciaries could, within the boundaries of their duties, build in a bonus for themselves that triggers upon the company’s failure. Further, it would be both inequitable and absurd to *increase* the management team’s recoveries *because* the company failed.

At bottom, it is simply bad policy to pay these insider’s claims in the wake of the American Community’s failure. Public furor over extravagant bonuses paid to company officers, despite poor-to-abysmal job performance, has been a fixture in this country for the last several years. In 2009, the public was outraged when AIG paid \$165 million in bonuses on the heels of

its federal bailout using taxpayer money.² And this past summer, JPMorgan Chase's Chief Investment Officer resigned while the company suffered over \$2 billion in investment losses, yet she is due to receive a severance package estimated at nearly \$15 million.³ Actions like these have led to investigations, Congressional hearings, proposed legislation, and vigorous debate. Here, paying generous golden parachute benefits to the very officers responsible for causing American Community to fail is, put bluntly, outrageous.

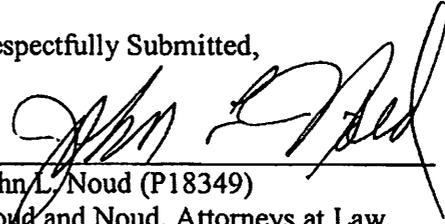
Despite their efforts to revise history, the Appellants are not struggling workers whose livelihoods are at the behest of their employers. They *were* the employers, the managers of American Community, and they now seek to be rewarded for their failure to properly manage the company. The court below saw through the Appellants' efforts to twist the facts and paint themselves as the hapless victims of a struggling economy. This Court should not overturn that sound decision.

² See Wall Street Journal Online, *Some Will Pay Back AIG Bonuses* (March 19, 2009), available at: <http://online.wsj.com/article/SB123743055512280701.html> (accessed June 14, 2012).

³ See CNN Money Online, *Ex-JPMorgan exec may face pay 'claw back'* (June 6, 2012), available at: <http://money.cnn.com/2012/06/05/news/companies/JP-morgan-senate/index.htm> (accessed June 14, 2012).

Dated: February 28, 2013

Respectfully Submitted,



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STATE OF MICHIGAN
IN THE COURT OF APPEALS

KEN ROSS, COMMISSIONER OF THE OFFICE
OF FINANCIAL AND INSURANCE
REGULATION,

Petitioner/Appellee

Court of Appeals No. 312470

Circuit Court No. 10-397-CR
Hon. William E. Collette

v

AMERICAN COMMUNITY MUTUAL
INSURANCE COMPANY,

Respondent/Appellant

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PROOF OF SERVICE

The undersigned certifies that a copy of the JOINDER AND BRIEF OF APPELLEE HOLDCO ADVISORS, L.P., AS MANAGER AND POWER OF ATTORNEY FOR SURPLUS NOTEHOLDER FINANCIALS RESTRUCTURING PARTNERS, LTD., IN SUPPORT OF DENIAL OF FORMER OFFICERS' CLAIMS FOR SEVERANCE AND OTHER POST-TERMINATION BENEFITS UNDER PRE-REHABILITATION EXECUTIVE EMPLOYMENT AGREEMENTS was served upon the parties listed below by sending the same via FedEx 2nd Day Air delivery service from a Fedex location in the city of Chicago, Illinois, enclosed in a FedEx envelop with fully prepaid delivery fee, plainly addressed as follows on the 28th day of February 2013.

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