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August 8, 2012

Clerk of the Court  
Ingham County Circuit Court  
313 W. Kalamazoo  
Lansing, MI 48933

RE: Ken Ross, Commissioner of OFIR v American Community Mutual Ins. Co.  
Ingham County Circuit Court File: 10-397-CR

Dear Clerk:

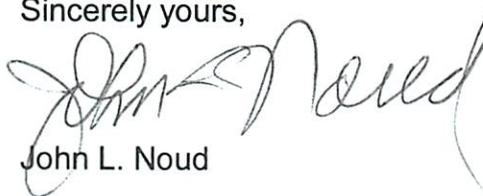
Enclosed for filing are:

1. Reply Brief Of Holdco Advisors, L.P. On Behalf Of Surplus Noteholder Financials Restructuring Partners, Ltd. Regarding Former Officers' Claims For Severance And Other Benefits Under Pre-Rehabilitation Executive Employment Agreements; and
2. Proof of Service of a copy of same upon interested persons.

By a copy of this letter service is being accomplished.

Thanks for your continuing cooperation.

Sincerely yours,



John L. Noud

lb

Enclosures

cc: Judge Collette  
Ms. Lori McAllister  
Mr. Philip L. Sternberg  
Mr. Christopher Kerr  
Ms. Carolyn Thagard  
Mr. Vik Ghei  
Mr. Mudassir Mohamed

DEPT. OF  
ATTORNEY GENERAL

AUG 09 2012

CORPORATE OVERSIGHT  
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STATE OF CALIFORNIA  
DEPARTMENT OF REVENUE  
SACRAMENTO, CALIFORNIA

DATE: 08/09/2012  
TIME: 10:00 AM

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CORPORATE OVERSIGHT

STATE OF MICHIGAN  
CIRCUIT COURT FOR THE 30TH JUDICIAL CIRCUIT  
INGHAM COUNTY

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

Petitioner,

No. 10-397-CR

v

HON. WILLIAM E. COLLETTE

AMERICAN COMMUNITY MUTUAL  
INSURANCE COMPANY,

Respondent.

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**REPLY BRIEF OF HOLDCO ADVISORS, L.P. ON BEHALF OF SURPLUS  
NOTEHOLDER FINANCIALS RESTRUCTINR PARTNERS, LTD. REGARDING  
FORMER OFFICERS' CLAIMS FOR SEVERANCE AND OTHER BENEFITS UNDER  
PRE-REHABILITATION EXECUTIVE EMPLOYMENT AGREEMENTS**

**INTRODUCTION**

The Former Officers have overreached both factually and legally in requesting payment of their golden parachute benefits. Factually, they attempt to distance themselves from the results of their management decisions, blaming the company's failure on their predecessors. The numbers tell a different story. In 2007, when each of the Former Officers held executive management positions, American Community's net worth was over \$106 million and the

company had an A.M. Best financial strength rating of B+ (Good) with a stable outlook. By the end of 2009, under the watch of the Former Officers, the company's net worth had plummeted to \$21 million and its A.M. Best rating was downgraded C+ (Marginal) with a negative outlook. Under these circumstances, the expected \$16 million remaining at the end of the rehabilitation (leading to this payment dispute) is more accurately attributable to the Rehabilitator's timely intervention and actions in this rehabilitation. This money is available *despite* the Former Officers' management decisions, not *because* of them.

Legally, the job performance of the Former Officers has no bearing on the payment of their golden parachute claims. By law, these claims are not "payment for services rendered prior to" the Rehabilitation Order and are not payable. Yet the Former Officers overreach again, advancing an interpretation of MCL 500.8137(4) that is conveniently broad enough to include their claims, but so broad that it renders the statute meaningless. The cases they rely upon for such nonsensical interpretation, however, tell a different story. Similarly, the Former Officers rely on bankruptcy law to justify payment of their golden parachute benefits, but bankruptcy law would flatly prohibit such claims, and indeed illustrates why such claims should be disallowed here.

**I. Severance Payments Are Not Payments for Services Rendered.**

The Former Officers attempt to muddy the waters on a clear issue: these golden parachute benefits are not payments for services rendered. The severance package offered by American Community was, as the Former Officers currently point out, offered as an inducement for the Former Officers to continue working for the company. But an inducement to stay is *not* the same as compensation for services rendered. The Former Officers' wages and other current

benefits were their compensation for services rendered. The golden parachute benefits were a bonus intended to prevent them from quitting.

None of the cases relied upon by the Former Officers refute this point. Indeed, none of the cases cited by the Former Officers equate severance payments with payments for services rendered. See, e.g., *Holland v. Earl G. Graves Publishing Co., Inc.* 46 F.Supp. 2d 861 (E.D. Mich. 1998) (describing offers of severance as unilateral contracts); *Cain v. Allen Electric & Equipment Co.*, 78 N.W. 296 (1956) (same). Rather, these cases merely stand for the proposition that an offer for severance, and the acceptance of that offer by a party choosing to stay with the company, creates a binding contract. This is not in dispute. But compensation for *not quitting* is distinct from compensation for *services rendered*.

Indeed, the Former Officers' own cases make this point clear. For example, the Former Officers lean on a sentence from *Erwin v. FIDC*, which is a quote from *Office & Professional Employees Int'l Union, Local 2 v. FDIC*, 27, F.3d 598, 603-04 (D.C. Cir. 1994) explaining that "severance payments are properly characterized as consideration *for entering into (or continuing under) the employment contract . . .*" (emphasis added). Entering into or continuing under an employment contract is distinct from actually "rendering services" to the company. If it is *not* distinct, then, as the Rehabilitator correctly points out in its reply brief filed substantially contemporaneously herewith, MCL 500.8137(4) is rendered meaningless.

Moreover, the each of the cases relied upon by the Former Officer discusses severance benefits for non-insider employees. In this case, the Former Officers have given themselves these golden parachute benefits. It is apples to oranges to compare compensation and benefits provided to employees at arm's length to compensation and benefits that insiders provide themselves.

## II. The Bankruptcy Code's Strict Limitations on Retention Bonuses Illustrates Why Payment of the Former Officers' Severance Claims Is Improper.

The Former Officers' reliance on section 503(c) of the Bankruptcy Code to justify the severance payments is woefully misplaced. The Bankruptcy Code prohibits retention bonus compensation to insiders in virtually all circumstances. Indeed, the thrust of bankruptcy law regarding such compensation is that transactions between a debtor and its insiders – especially those that enrich the insiders – require careful scrutiny. *See In re Regensteiner Printing Co.*, 122 B.R. 323, 326 (N.D. Ill. 1990) (courts "must scrutinize" transactions between insiders and debtor); *see also Pepper v. Litton*, 308 U.S. 295, 306 (1939) (dealings by insiders subject to "rigorous scrutiny" and requires a showing of their "inherent fairness"). Close scrutiny is particularly warranted with management bonus plans, and insiders "bear the burden of proof as to the fairness of such arrangements". *See In re Am. Plumbing & Mechanical, Inc.*, 323 B.R. 442, 463 (Bankr. W.E. Tex. 2005) ("appropriate to more closely scrutinize bonuses" to officer and directors; such insiders "bear the burden of proof as to fairness of any such arrangements"). As the court noted in *In re U.S. Airways, Inc.* 329, B.R. 793, 797 (Bankr. E.D.Va 2005), management bonus plans "have something of a shady reputation," and for good reason:

All too often they have been used to lavishly reward – at the expense of the creditor body – the very executives whose bad decisions or lack of foresight were responsible for the debtor's financial plight. But even where external circumstances rather than the executives are to blame, there is something inherently unseemly in the effort to insulate the executives from the financial risks all other stakeholders face in the bankruptcy process.

*Id.*

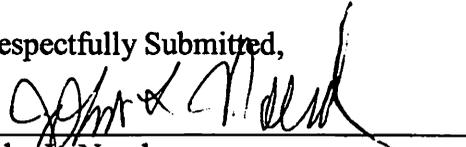
Congress enacted 503(c) precisely for the purpose of reigning in executive compensation schemes. *See In re Dana Corp. ("Dana I")*, 358 B.R. 96, 100-01 (Bankr. S.D.N.Y. 2006); *see also In re Dana Corp. ("Dana II")*, 358 B.R. 567, 575 (Bankr. S.D.N.Y. 2006) (noting Congress' concern over the "glaring abuses of the bankruptcy system by the executives of giant

companies... who lined their own pockets, but left thousands of employees and retirees out in the cold”) (quoting statement of Sen. Kennedy).

Because of the inherent unseemliness of insider bonuses and the potential for abuse, section 503(c) of the Bankruptcy Code establishes strict evidentiary standards for allowing retention bonuses or severance payments. Specifically, payment of retention bonuses requires that (a) the retained insider has a bona fide job offer at the same or greater compensation, (b) that the insider’s services are essential to the survival of the business, and (c) a similar type of compensation is provided to non-management employees. 11 U.S.C § 503(c)(1). Payment of severance is not permitted unless (i) the payment is part of a program that is generally applicable to all full-time employees and (ii) payment to insiders is not greater than 10 times the severance provided to non-management employees. 11 U.S.C. § 503(c)(2). The Former Officers’ golden parachute benefits do not meet these strict standards. They do not even come close. Yet the Former Officers insist that the creditors and employees of American Community – those with the least ability to control the fate of the company – be left out in the cold while these insiders are handsomely rewarded. This is precisely the abuse that section 503(c) was designed to curb. Indeed, as the court explained in *In re Forum Health*, 427 B.R. 650 (Bankr. N.D. Ohio 2010), “[t]he purpose of the limitation 11 U.S.C. § 503(c)(2)(A) . . . is to ensure that the insider severance is not specially created for . . . insiders.” The Former Officers should not be permitted to create for themselves a special benefit that is payable upon the collapse of the company they are supposed to run. Their claims should be denied.

August 8, 2012

Respectfully Submitted,



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*Counsel to Financials Restructure Partners, Ltd.  
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**STATE OF MICHIGAN  
IN THE 30th CIRCUIT COURT FOR THE COUNTY OF INGHAM**

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

**Petitioner,**

**File No. 10-397-CR**

**vs.**

**Judge William E. Collette**

**AMERICAN COMMUNITY MUTUAL  
INSURANCE COMPANY,**

**PROOF OF SERVICE**

**Respondent.**

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**STATE OF MICHIGAN )  
COUNTY OF INGHAM )**

Lisa M. Bodell, being first duly sworn, deposes and says that on the 8<sup>th</sup> day of August 2012, she served copies of "Reply Brief Of Holdco Advisors, L.P. On Behalf Of Surplus Noteholder Financials Restructuring Partners, Ltd. Regarding Former Officers' Claims For Severance And Other Benefits Under Pre-Rehabilitation Executive Employment Agreements" upon the following, by first class mail, with postage fully prepaid thereon:

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Assistant Attorney General  
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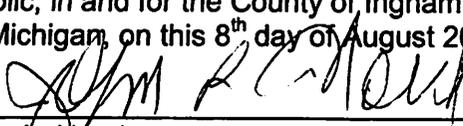
**Phillip L. Sternberg  
Couzens, Lansky, Fealk Ellis, Roeder &  
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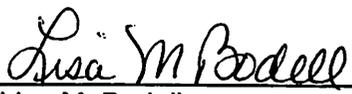
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Lori McAllister  
Dykema Gossett PLLC  
201 Townsend Street, Suite 900  
Lansing, MI 48933

Subscribed and sworn to before me, a Notary  
Public, in and for the County of Ingham, State  
of Michigan, on this 8<sup>th</sup> day of August 2012.

  
\_\_\_\_\_  
John L. Noud  
My commission expires: 9/24/2013  
Acting in the County of Ingham

  
\_\_\_\_\_  
Lisa M. Bodell