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UNITED STATES BANKRUPTCY COURT  
DISTRICT OF DELAWARE

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In the Matter of:

WASHINGTON MUTUAL, INC., et al.,  
Debtors.

Case No. 08-12229 (MFW)  
(Jointly Administered)

- - - - - x

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NANTAHALA CAPITAL PARTNERS, LP,  
BLACKWELL CAPITAL PARTNERS, LLC,  
AXICON PARTNERS, LLC,  
BRENNUS FUND LIMITED,  
COSTA BRAVA PARTNERSHIP III, LLP,  
SONTERRA CAPITAL MASTER FUND, LTD.

Plaintiffs,

Adv. Proc. 10-50911 (MFW)

v.

WASHINGTON MUTUAL, INC.,  
MICHAEL MURPHY,  
WILLIAM REED, JR.  
THOMAS LEPPERT,  
STEPHEN CHAZEN,  
STEPHEN FRANK,  
REGINA MONTOYA,  
PHILLIP MATTEWS,  
ORIN SMITH,  
MARGARET OSMER MCQUADE,  
JAMES STEVER,  
FRANCIS BAIER,  
DAVID BONDERMAN,  
CHARLES LILLIS

Defendants.

- - - - - x

1       - - - - -x  
MICHAEL WILLINGHAM and ESOPUS  
2       CREEK VALUE LP,  
3                    Plaintiffs,  
4       v.                                    Adv. Proc. 10-51297 (MFW)  
5       WASHINGTON MUTUAL, INC.,  
6                                    Defendant.  
7       - - - - -x  
8       - - - - -x  
9       WASHINGTON MUTUAL, INC. and  
10       WMI INVESTMENT CORP.  
11                                    Plaintiff,  
12       v.                                    Adv. Proc. 10-53420 (MFW)  
13       PETER J. AND CANDANCE R. ZAK  
14       LIVING TRUST OF 2001 U/D/O  
15       AUGUST 31, 2001, ET AL.  
16                                    Defendant.  
17       - - - - -x  
18       - - - - -x  
19       OFFICIAL COMMITTEE OF UNSECURED  
20       CREDITORS OF WASHINGTON MUTUAL,  
21       INC., ET AL., ON BEHALF OF CHAPTER  
22       11 ESTATES OF WASHINGTON MUTUAL,  
23       INC., ET AL.  
24                                    Plaintiff,  
25       v.                                    Adv. Proc. 10-53149 (MFW)  
26       ALEXANDER SASHA KIPKALOV,  
27       - - - - -x  
28       AMY DRIVER ANDERSON,                    Adv. Proc. 10-53135 (MFW)  
29       - - - - -x  
30       ANTHONY BOZZUTI,                        Adv. Proc. 10-53131 (MFW)  
31       - - - - -x  
32       CHANDAN SHARMA,                        Adv. Proc. 10-53147 (MFW)  
33       - - - - -x  
34       DAVID M. SCHWARTZ,                    Adv. Proc. 10-53144 (MFW)  
35       - - - - -x  
36       EDWARD F. BACH,                        Adv. Proc. 10-53132 (MFW)  
37       - - - - -x  
38       GREGORY H. WOOD,                        Adv. Proc. 10-53137 (MFW)  
39       - - - - -x

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2	2	- - - - -x	
		HENRY J. BERENS,	Adv. Proc. 10-53134 (MFW)
3	3	- - - - -x	
		HOWARD MATTHEWS,	Adv. Proc. 10-53134 (MFW)
4	4	- - - - -x	
		JAMES CORCORAN,	Adv. Proc. 10-53134 (MFW)
5	5	- - - - -x	
		JIANGUO ZHONG,	Adv. Proc. 10-53148 (MFW)
6	6	- - - - -x	
		JOHN M. BROWNING,	Adv. Proc. 10-53156 (MFW)
7	7	- - - - -x	
		JONI WYCKOFF,	Adv. Proc. 10-53151 (MFW)
8	8	- - - - -x	
		KEITH O. FUKUI,	Adv. Proc. 10-53139 (MFW)
9	9	- - - - -x	
		MARC MALONE,	Adv. Proc. 10-53152 (MFW)
10	10	- - - - -x	
		MATTHEW WAJNER,	Adv. Proc. 10-53136 (MFW)
11	11	- - - - -x	
		MICHAEL R. ZARRO,	Adv. Proc. 10-53143 (MFW)
12	12	- - - - -x	
		NIRMAL BAID,	Adv. Proc. 10-53145 (MFW)
13	13	- - - - -x	
		PETER GERRALD,	Adv. Proc. 10-53138 (MFW)
14	14	- - - - -x	
		PETER HELLER,	Adv. Proc. 10-53146 (MFW)
15	15	- - - - -x	
		RACHEL M. MILEUR a/k/a	Adv. Proc. 10-53133 (MFW)
16	16	RACHELLE M. MILEUR,	
		- - - - -x	
17	17	RICHARD BLUNCK,	Adv. Proc. 10-53157 (MFW)
		- - - - -x	
18	18	ROBERT C. HILL,	Adv. Proc. 10-53153 (MFW)
		- - - - -x	
19	19	STEPHEN E. WHITTAKER,	Adv. Proc. 10-53150 (MFW)
		- - - - -x	
20	20	STEVEN HERUTY,	Adv. Proc. 10-53141 (MFW)
		- - - - -x	
21	21	THOMAS E. MORGAN,	Adv. Proc. 10-53154 (MFW)
		- - - - -x	
22	22	WILLIAM K. GLASBY,	Adv. Proc. 10-53142 (MFW)
23	23	Defendants.	
24	24	- - - - -x	
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United States Bankruptcy Court

824 North Market Street

Wilmington, Delaware

July 13, 2011

9:30 AM

B E F O R E:

HON. MARY F. WALRATH

U.S. BANKRUPTCY JUDGE

ECR OPERATOR: BRANDON MCCARTHY

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HEARING re Debtors' Fifth Omnibus (Substantive) Objection to  
Claims [Docket No. 1233; filed 6/26/09]

HEARING re Debtors' Sixth Omnibus (Substantive) Objection to  
Claims [Docket No. 1234; filed 6/26/09]

HEARING re Debtors' Motion Pursuant to Sections 105 and 363 of  
the Bankruptcy Code for Order Approving Procedures for the Sale  
of Certain Intellectual Property [Docket No. 1701; filed  
10/7/09]

HEARING re Debtors' Twenty-Third Omnibus (Substantive)  
Objection to Claims (Claim Nos. 2463, 2470, 2500, and 2505)  
[Docket No. 2443; filed 3/1/10]

HEARING re Debtors' Objection to Proof of Claim filed by the  
Oregon Department of Revenue (Claim No. 3693) [Docket No. 3196;  
filed 4/14/10]

HEARING re Debtors' Objection to Proof of Claim Filed by AT&T  
Corp. (Claim No. 3725) [Docket No. 3691; filed 5/10/10]

HEARING re Debtors' Forty-Third Omnibus (Substantive) Objection  
to Claims [Docket No. 4749; filed 6/16/10]

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HEARING re Debtors' Forty-Fourth Omnibus (Substantive)  
Objection to Claims [Docket No. 4750; filed 6/16/10]

HEARING re Debtors' Forty-Sixth Omnibus (Non-Substantive)  
Objection to Claims [Docket No. 5117; filed 7/21/10]

HEARING re Debtors' Fifty-Fifth Omnibus (Substantive) Objection  
to Claims [Docket No. 5616; filed 10/17/10]

HEARING re Debtors' Fifty-Sixth Omnibus (Substantive) Objection  
to Claims [Docket No. 5618; filed 10/18/10]

HEARING re Michael Willingham Esopus Creek Value, LP v.  
Washington Mutual, Inc. et al. (Adv. Pro. No. 10-51297)

HEARING re Nantahala Capital Partners, LP, Blackwell Capital  
Partners, LLC, Axicon Partners, LLC, Brennus Fund Limited,  
Costa Brava Partnership III, LLP, and Sonterra Capital Master  
Fund, Ltd. v. Washington Mutual, Inc., Michael Murphy,  
William Reed, Jr., Thomas Leppert, Stephen Chazen, Stephen  
Frank, Regina Montoya, Phillip Mattews, Orin Smith, Margaret  
Osmer McQuade, James Stever, Francis Baier, David Bonderman and  
Charles Lillis (Adversary Proceeding No. 10-50911)

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HEARING of Official Committee of Unsecured Creditors of Washington Mutual, Inc., et al., on behalf of Chapter 11 estates of Washington Mutual, Inc., et al. v. Alexander Sasha Kipkalov re: Adversary Proceeding No. 10-53149.

HEARING of Official Committee of Unsecured Creditors of Washington Mutual, Inc., et al., on behalf of Chapter 11 estates of Washington Mutual, Inc., et al. v. Amy Driver Anderson re: Adversary Proceeding No. 10-53135.

HEARING of Official Committee of Unsecured Creditors of Washington Mutual, Inc., et al., on behalf of Chapter 11 estates of Washington Mutual, Inc., et al. v. Anthony Bozzuti Re: Adversary Proceeding No. 10-53131.

HEARING of Official Committee of Unsecured Creditors of Washington Mutual, Inc., et al., on behalf of Chapter 11 estates of Washington Mutual, Inc., et al. v. David M. Schwartz re: Adversary Proceeding No. 10-53144.

HEARING of Official Committee of Unsecured Creditors of Washington Mutual, Inc., et al., on behalf of Chapter 11 estates of Washington Mutual, Inc., et al. v. Gregory H. Wood re: Adversary Proceeding No. 10-53137.

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HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. James Corcoran  
re: Adversary Proceeding No. 10-53158.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Jianguo Zhong re:  
Adversary Proceeding No. 10-53148.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. John M.  
Browning re: Adversary Proceeding No. 10-53156.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Joni Wyckoff re:  
Adversary Proceeding No. 10-53151.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Keith O. Fukui  
re: Adversary Proceeding No. 10-53139.



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HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Marc Malone  
Re: Adversary Proceeding No. 10-53152.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Matthew Wajner  
Re: Adversary Proceeding No. 10-53136.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Nirmal Baid  
Re: Adversary Proceeding No. 10-53145.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Peter Gerrald re:  
Adversary Proceeding No. 10-53138.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Peter Heller  
Re: Adversary Proceeding No. 10-53146.

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HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Rachel M.  
Mileur a/k/a Rachelle M. Mileur re: Adversary Proceeding No.  
10-53133.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Richard Blunck  
re: Adversary Proceeding No. 10-53157.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Robert C. Hill  
re: Adversary Proceeding No. 10-53153.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Stephen E.  
Whittaker re: Adversary Proceeding No. 10-53150.

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HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Steven Heruty  
re: (Adversary Proceeding No. 10-53141.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Thomas E.  
Morgan re: Adversary Proceeding No. 10-53154.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. William K.  
Glasby re: Adversary Proceeding No. 10-53142.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Chandan Sharma  
Re: Adversary Proceeding No. 10-53147.

HEARING of Official Committee of Unsecured Creditors of  
Washington Mutual, Inc., et al., on behalf of Chapter 11  
estates of Washington Mutual, Inc., et al. v. Edward F. Bach  
re: Adversary Proceeding No. 10-53132.

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2 HEARING of Official Committee of Unsecured Creditors of  
3 Washington Mutual, Inc., et al., on behalf of Chapter 11  
4 estates of Washington Mutual, Inc., et al. v. Henry J. Berens  
5 re: Adversary Proceeding No. 10-53134.

6

7 HEARING of Official Committee of Unsecured Creditors of  
8 Washington Mutual, Inc., et al., on behalf of Chapter 11  
9 estates of Washington Mutual, Inc., et al. v. Howard  
10 Matthews re: Adversary Proceeding No. 10-53155.

11

12 HEARING of Official Committee of Unsecured Creditors of  
13 Washington Mutual, Inc., et al., on behalf of Chapter 11  
14 estates of Washington Mutual, Inc., et al. v. Michael R. Zarro  
15 re: Adversary Proceeding No. 10-53143.

16

17 HEARING re Modified Sixth Amended Joint Plan of Affiliated  
18 Debtors Pursuant to Chapter 11 of the United States Bankruptcy  
19 Code [Docket No. 6696; filed 2/8/11]

20

21 HEARING re Application for an Order Pursuant to 11 U.S.C. §§  
22 328, 330 and 1103 and Fed. R. Bankr. P. 2014 Authorizing the  
23 Retention and Employment of Schwabe, Williamson & Wyatt as  
24 Securities Counsel to the Official Committee of Equity

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Security Holders of Washington Mutual, Inc., et al., Nun Pro  
Tunc to June 1, 2011 [Docket No. 7981; filed 6/23/11]

HEARING re Motion to Compel Aurelius Capital Management LP and  
Centerbridge Partners, LP to Produce Documents [Docket No.  
8117; filed 7/8/11]

HEARING re Debtors' Motion In Limine to Exclude Portions of the  
Expert Reports and the Testimony of the Equity Committee's  
Expert Witnesses Anders J. Maxwell and Kevin D. Anderson  
[Docket No. 8159; filed 7/11/11]

Transcribed by: Clara Rubin

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MARISSA B. WILEY, ESQ. (TELEPHONICALLY)

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MARIA E. DOUVAS, ESQ.

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1 P R O C E E D I N G S

2 THE COURT: Good morning.

3 MR. ROSEN: Good morning, Your Honor. Brian Rosen,  
4 Weil, Gotshal & Manges on behalf of the debtors, and I'm here  
5 with several of my partners and associates who will be taking  
6 part in the confirmation hearing, and they'll introduce  
7 themselves as we go along, Your Honor.

8 Your Honor, there are a few items that are on the  
9 agenda besides the confirmation hearing itself, pursuant to  
10 your Court's order shortening the time to consider them, and  
11 what we'd like to do first is take up the motion in limine that  
12 the debtors filed.

13 THE COURT: All right. Any objection to that?

14 All right. You may proceed.

15 MR. MASTANDO: Good morning, Your Honor. John  
16 Mastando from Weil Gotshal on behalf of the debtors.

17 Your Honor, we have filed a motion in limine seeking  
18 to exclude portions of two experts proffered by the equity  
19 committee, Mr. Maxwell on valuation issues and Mr. Anderson on  
20 tax issues.

21 If I could start with Mr. Maxwell. His report is full  
22 of rank speculation and baseless assumptions that make it  
23 unreliable and inadmissible under Daubert. There's one aspect  
24 of his report where, and he testified at his deposition, that  
25 the value of the stock of reorganized WMI is 130 to 135 million

1 dollars. That's not materially different from Blackstone's  
2 valuation for the debtors, and it's the only part of his report  
3 that is reliable. In fact, his valuation is potentially  
4 millions of dollars lower than Blackstone's valuation. And he  
5 testified at his deposition that he doesn't believe Blackstone  
6 undervalued reorganized WMI. So --

7 THE COURT: Can't you bring this out in cross-  
8 examination of him, though?

9 MR. MASTANDO: Certainly I can, Your Honor. I think  
10 with the assumptions he makes and the speculation in his  
11 report, though, they're so baseless and assumptions are layered  
12 upon assumptions, that there's really no basis for the  
13 admission of the testimony.

14 What he assumes is, he assumes that reorganized WMI  
15 becomes a going concern, and he doesn't account for any risks  
16 or costs associated with that. He assumes that hundreds of  
17 millions and billions of dollars can be raised. He assumes  
18 that reorganized WMI is something wholly different than what it  
19 will be at the time of emergence, and so therefore the report  
20 is speculative, which he also admits and should be inadmissible  
21 under Daubert.

22 THE COURT: Well, I am going to deny the motion,  
23 because I think all of these issues can be brought out in  
24 cross-examination. I know that expert witnesses make factual  
25 assumptions all the time, and it is the role of cross-

1 examination to show that they are baseless. I don't think that  
2 it's sufficient, though, to throw out the report.

3 MR. MASTANDO: Okay. Would you like to hear my  
4 arguments as to Mr. Anderson?

5 THE COURT: Yes.

6 MR. MASTANDO: Okay. As to Mr. Anderson, Your Honor,  
7 he submitted three reports in the case. The first one largely  
8 addressed Section 382 of the Internal Revenue Code, which  
9 appears to be largely in agreement between the parties as to  
10 the general application of Section 382.

11 His first report covered briefly Section 269 of the  
12 Code, which involves a situation where if there's an  
13 acquisition of control and the principal purpose of that  
14 acquisition is deemed to be tax avoidance, you can lose the  
15 benefit of NOLs. He barely addressed it in his first report,  
16 did not address it in his second report, and slightly addressed  
17 it in his third report, but kind of missed the point.

18 But putting all that aside, his expertise under  
19 Section 269 is clearly insufficient. I do not believe he can  
20 be qualified as an expert under Section 269. He admitted that  
21 the issues have never been front and center in the matters he's  
22 dealt with over 30 years, he's never done any report, or  
23 analysis, or study of Section 269, and whatever advice he's  
24 given clients, he can't share with us because it's  
25 confidential. So we don't really know what any of his

1 positions are on Section 269.

2 So that's in term of qualification. And then, Your  
3 Honor, what he basically opines is, "I think Section 269 is  
4 unlikely to apply based on my experience." And the problem  
5 with that, Your Honor, is he's not applying the test under  
6 Section 269, the principal purpose test that's employed to  
7 determine whether there's a Section 269 issue.

8 All he's saying, you know, I've been doing this a long  
9 time, and based on the cases I've happened to work on, I  
10 haven't really seen it applied that much. It would be akin to  
11 a lawyer coming before Your Honor and saying, I haven't seen  
12 summary judgment motions granted that frequently, so I assume  
13 you won't grant one in this case, Your Honor, even though I'm  
14 not really opining on the case, or talking about the case in  
15 particular. And I just think that's inappropriate under  
16 Daubert as well.

17 THE COURT: Well, is he really making -- giving any  
18 opinion then on Section 269?

19 MR. MASTANDO: He's opining that he thinks it's  
20 unlikely to apply based on his experience, and he doesn't apply  
21 the principal purpose test, that is the test under Section 269  
22 to the acquisition of control by the creditors here.

23 THE COURT: Because he doesn't think it applies. So  
24 again, isn't this something you can raise in cross-examination  
25 of --



1 MR. MASTANDO: I certainly will, Your Honor.

2 THE COURT: Okay.

3 MR. MASTANDO: Okay. Thank you, Your Honor.

4 MR. ROSEN: Your Honor, the next item, Item 43  
5 actually on the agenda, is the motion to compel Aurelius and  
6 Centerbridge Partners to produce documents, and that is by the  
7 TPS Plaintiffs.

8 MR. KAPLAN: Good morning, Your Honor. Howard Kaplan  
9 from Arkin, Kaplan & Rice representing certain of the trust  
10 preferred holders.

11 If I may just provide context for our motion, Your  
12 Honor. Unquestionably, discovery has shown that Aurelius and  
13 Centerbridge had nonpublic information, and unquestionably they  
14 traded at times when they had nonpublic information. And the  
15 justification that's been offered is that the information is  
16 not material. I think that's going to be the principal issue.

17 And they say this in part, because they say they  
18 received advice from counsel attempting to show good faith, and  
19 they say this as well because during the critical period  
20 between December 2009 when settlement negotiations advanced  
21 dramatically and March 12th, 2010, when it was announced in  
22 court that there was a deal, they claimed they did not get any  
23 updates of any settlement discussions from their counsel.

24 Now, we don't have any documents or any e-mails on  
25 those subjects, and our motion relates to a very narrow set of

1 documents, in fact, e-mails mentioned specifically in the  
2 testimony of the representatives of Centerbridge and Aurelius.

3 Just to give the Court a couple of examples, we put  
4 this in our brief, Aurelius' representative, Mr. Groper,  
5 testified that he -- after receiving confidential information  
6 in December of 2009, and there was a sixty-day confidentiality  
7 period, Your Honor, so there was an agreement in place until  
8 December 30, after receiving confidential information, he said  
9 he consulted with two law firms, and determined that he was not  
10 in possession of material nonpublic information.

11 Needless to say that the term sheets in those  
12 negotiations were never publicly disclosed, so clearly it was  
13 nonpublic information, so it's a materiality question.

14 And Centerbridge's representative, Mr. Melwani, he  
15 gave similar testimony, but even more specific. He said that  
16 he recalled reviewing e-mails in which his outside counsel  
17 supposedly confirmed with the debtors that certain information  
18 Centerbridge had was not material. He couldn't remember a  
19 date, so that's not as specific as to date.

20 Now, Your Honor, this clearly is an issue, because I  
21 just note the creditors' committee put in a brief that we  
22 received yesterday, I think it was filed under seal, and on  
23 page 15, they claimed to have done their own investigation, the  
24 creditors' committee, and on page 15 of their brief, they say,  
25 "The settlement noteholders also sought and appeared to have

1 received written confirmation from debtor's counsel that all  
2 such information had been disclosed prior to removing WMI trade  
3 restrictions or ethical walls."

4 That's what we're here asking for. I mean, everyone  
5 is talking about e-mails and documents that have not yet been  
6 produced by Centerbridge and Aurelius.

7 Quite plainly, Your Honor, this testimony is going to  
8 be offered and has been offered to show good faith, and we  
9 believe that based on that, to the extent these communications  
10 are privileged, and it's not clear that they are, because if  
11 Fried Frank, who is the lawyer for Centerbridge and Aurelius at  
12 the time is simply passing information from the debtors saying,  
13 you're free to trade or whatever. We don't know what the  
14 communication said, I don't see how that's privileged.

15 On the other hand, we think clearly based on the  
16 testimony, and based on what's going to be offered in this  
17 court that this has been waived. And there's an argument  
18 that's been made in the papers, Your Honor, that the two firms  
19 merely consulting with lawyers, that it's not clear that they  
20 got legal advice and so forth.

21 But under, you know, the one case I'll point out to  
22 the Court is the ML-Lee case. It doesn't matter what you call  
23 it. If you're using a privileged communication to show your  
24 good faith then you waive your attorney/client privilege.

25 In that case, the defendant was accused of recklessly

1 violating the Investment Company Act, and in the answer, the  
2 defendant said that they relied in part on counsel who reviewed  
3 the transactions. That was it. District of Delaware case.

4 And the Court found that the defendant is putting that  
5 in to show good faith and the privilege is waived. And we  
6 think that's a very similar situation to what we have here.

7 On our second category, Your Honor, the communications  
8 concerning settlement discussions, communications with counsel  
9 concerning settlement discussions, again, don't see how that's  
10 privileged. I mean, obviously there might be privileged  
11 material in such a communication, but just passing on updates  
12 on settlement communications, we think would not be.

13 But more importantly, Your Honor, there are some e-  
14 mails that have been produced, that show or suggest, I should  
15 say, that there were such communications. And you know, I have  
16 two of them here, Your Honor. I can hand them up, but let me  
17 just put them into the record and describe them.

18 One, which has been marked as EC-204 is an e-mail from  
19 Mr. Roose dated February -- he's from Fried Frank -- dated  
20 February 15th, 2010, so this is in the period of December '09  
21 through March 12th, 2010. And he's writing to a  
22 representative -- to Mr. Rosen, actually, and he says, "We  
23 should plan to meet in person first thing next week, so that  
24 you can provide insight and color to clients as above, and so  
25 that we can walk through the term sheet and discuss."

1           There's another e-mail that Centerbridge -- the  
2 representative of Centerbridge in January, January 11th, 2010  
3 writes to a representative of the debtor, and says, "If you  
4 have a sec, please give me a buzz."

5           So, Your Honor, look, the testimony is we didn't get  
6 updates. These two firms were trading throughout this period,  
7 and they were saying that, obviously to say we were, you know,  
8 if even not formally restricted, we were restricting ourselves.  
9 That's basically the suggestion here.

10           We think there's evidence that there were these  
11 communications, Your Honor, and you know, obviously since  
12 that's going to be an issue, and that's what they're saying,  
13 we're entitled, we feel, to test that. It's only fair if  
14 that's going to be a defense in this case, or an offer of good  
15 faith to the Court that we should know whether there were such  
16 e-mail communications with counsel.

17           THE COURT: All right. Let me hear a response.

18           MR. KAPLAN: Thank you, Your Honor.

19           MR. TRACHTMAN: Good morning, Your Honor, Jeffrey  
20 Trachtman from Kramer Levin for Aurelius.

21           I guess it's not good form to tell a federal judge I  
22 told you so, but we kind of are where we were afraid we were  
23 going to be. We were here a couple of weeks ago, and the trust  
24 preferreds have been on the sidelines for months letting their  
25 fiduciary, the equity committee pursue this. They suddenly

1 surfaced. You gave them their basic rights as parties in  
2 interest to get the existing discovery, but you cautioned them  
3 that they would probably not be able to get more discovery.

4 And what's happened now predictably, is they're piling  
5 on more, they're trying to create more burden, more expense,  
6 and it's just too late. It's just unconscionable.

7 THE COURT: Well, let me ask you a question. Were  
8 you -- did the equity committee request this information from  
9 you?

10 MR. TRACHTMAN: The equity --

11 THE COURT: Did you produce it?

12 MR. TRACHTMAN: The equity committee requested very  
13 broad discovery of all communications.

14 THE COURT: Right.

15 MR. TRACHTMAN: Your Honor limited it to information  
16 provided during the settlements. Two weeks ago, they came in  
17 and relitigated the exact same question. They wanted all  
18 communications with the lawyers, and you said, that's not what  
19 I ordered, and you turned it down. In part, they are  
20 relitigating that point again.

21 They are also asking for things that weren't  
22 specifically asked for before.

23 THE COURT: Well, except that in denying their  
24 request, it was based on the settlement noteholder's  
25 representation that they had produced all nonprivileged

1 communications with their attorneys, specifically all  
2 communications from Fried Frank forwarding information from the  
3 debtor. Now, I'm hearing that apparently it was not all  
4 produced.

5 MR. TRACHTMAN: No, no. To the extent it's seeking  
6 that category, that has been produced. What they're now  
7 seeking is discussions about that, and simply counsel's  
8 communication what's happening in the case. That's not  
9 communicating information from the debtors. The information  
10 from the debtors has been produced.

11 This is really exactly what was litigated two weeks  
12 ago. Now, let me address the privilege issue, because it's  
13 just an incorrect statement of the standard.

14 To waive the privilege, you need to plead an  
15 affirmation defense of a reliance on advice of counsel. And  
16 the very cases they cite, the Glen Meade case, which cites  
17 their Rhone Poulence case, which is the standard case in the  
18 Third Circuit, makes that very clear. You can't come into a  
19 deposition and say did you talk to a lawyer, when the person  
20 says yes, you say ah-ha, you've waive the privilege.

21 When the state of mind of a client is at issue, that  
22 doesn't necessarily make reliance on advice of counsel the  
23 defense. What Mr. Groper testified to, what he will testify to  
24 at the confirmation hearing, is that Aurelius made its own  
25 judgment about whether it was in possession of material

1 nonpublic information and was free to trade.

2 It had a series of inputs. One of those inputs was  
3 that the contract required the debtor to publish the  
4 information that it had given. Another was the debtor's own  
5 judgment talking to the debtor's expert securities lawyers, and  
6 the e-mail that was referred to from the debtors, of course,  
7 has been produced, that's been marked at depositions, and the  
8 debtors specifically in writing, and orally, informed  
9 noteholders that they had disclosed all of the material  
10 nonpublic information, and they had a right to rely on that.

11 Independently of that, Aurelius made its own  
12 determination based on its own knowledge about the state of the  
13 settlement negotiations, that nothing that it had was material  
14 nonpublic information. And as a further input, in addition to  
15 that, they consulted their own securities lawyers. And they  
16 have not put the content of those communications at issue, it  
17 is another input that they had. If that constitutes a waiver,  
18 then it's the easiest thing in the world to force someone to  
19 waive the privilege.

20 Now, leaving aside that, the -- what's happening now  
21 is an attempt to introduce an entirely new argument. The trust  
22 preferreds do not have their own objection here. They've  
23 piggybacked on the equity committee.

24 The equity committee has a very clear allegation. The  
25 allegation is, you were given these confidential settlement



1 term sheets in November, not in December, and that remained  
2 material nonpublic information. No one has ever alleged that  
3 there was a breach, that there was material nonpublic  
4 information shared between January and March.

5 Mr. Groper testified he was not involved in settlement  
6 negotiations, he did not enter another confidentiality  
7 agreement. He found out the terms of the settlement when it  
8 was stated on the record on March 12th.

9 So what they're doing here is a complete fishing  
10 expedition, to try to come up with another claim on the day  
11 that we're starting the hearing that has not been alleged.

12 THE COURT: Well, let me say this. I'm going to  
13 reserve ruling on this with respect to the waiver issue until I  
14 hear the testimony. I'm not going to grant the motion with  
15 respect to communications forwarding information from the  
16 debtors because -- based on the representation it was produced.

17 If, in fact, there's evidence it was not, then I will  
18 revisit that. But I'll reserve on the motion at this point, on  
19 the waiver issue.

20 MR. TRACHTMAN: Thank you, Your Honor.

21 MR. ROSEN: With that, Your Honor, we'd like to  
22 commence with the hearing on the confirmation of the plan  
23 itself. As the Court is aware, there have been a few  
24 objections interposed, I know some people consider them, their  
25 objections, to be nonevidentiary, and they have asked me to ask

1 the Court that they be released at this time to appear at the  
2 closing arguments so that they could make or raise their  
3 objections at that time.

4 We would at this time, like to proceed directly into  
5 the testimony by way of either the declarations or the direct  
6 testimony that we suggested.

7 Additionally, Your Honor, while we have not been able  
8 to agree on many things in connection with the presentation of  
9 the evidence today, we were able to agree, however, with  
10 respect to how the witnesses were going to be tendered to the  
11 Court. And we did alert the Court to that last week.

12 But if I could, Your Honor, I'd just like to go  
13 through that again so that everyone understands what we are  
14 going.

15 Your Honor, it was decided that we would attempt to  
16 put the evidence on in, I'll call it three tranches or three  
17 mods. Specifically, the first tranche would be the 1129 case  
18 itself. Which are the debtor's five witnesses in support of  
19 confirmation. And in that regard, we will start with Mr.  
20 Robert Klamser and Mr. David Sharp, who are both from KCC, and  
21 they will be testifying by way of a declaration and then  
22 available for cross-examination, with respect to the voting  
23 results.

24 Third, Your Honor, would be Mr. James Carreon. He  
25 testified at the prior confirmation hearing about certain tax

1 issues, and he will do that again at this time.

2 Fourth, Your Honor, would be Mr. Steven Zelin from  
3 Blackstone and he will be testifying as to the valuation of the  
4 reorganized debtor.

5 The equity committee has asked us to take out of order  
6 one of their witnesses, Mr. Kevin Anderson, who Mr. Mastando  
7 referred to earlier. Mr. Anderson is going to talk about tax  
8 issues, similar to what Mr. Carreon did, and because of his  
9 unavailability on Thursday and Friday, they've asked to the  
10 extent that we have time available to permit him to testify  
11 today, and the debtors are agreeable with that.

12 Likewise, in response to our request with respect to  
13 one witness, Mr. Richard Reinhold, who is a rebuttal witness,  
14 Your Honor, on tax related issues. Because of scheduling  
15 issues there, and because his testimony is very similar to  
16 Mr. Anderson's, we thought that we would take him out of order  
17 out of the rebuttal stage, and put him right behind  
18 Mr. Anderson.

19 We would then move to Mr. Jonathan Goulding, who will  
20 testify as to 1129 issues. Mr. Goulding has already submitted  
21 a declaration to the Court and for everyone here to review, and  
22 he will be testifying as to other issues, as we alluded to in  
23 that declaration, which were not included in the declaration,  
24 several aspects of 1129.

25 And then the last witness, Your Honor, in what I'll

1 refer to as tranche two, which would be Mr. Anders Maxwell.  
2 Again, Mr. Mastando referred to him earlier. That would be the  
3 witness of the equity committee who will be contesting the  
4 valuation that is being raised by Mr. Zelin and Blackstone.

5 We would then, Your Honor, to tranche three, which is  
6 the issues associated with the allegations of inequitable  
7 conduct. And for the first two tranches that we talked about,  
8 Your Honor, there would not be any testimony with respect to  
9 that.

10 It is our understanding that the witnesses, although  
11 they are being requested to be put on by the equity committee,  
12 they will be put on, however, by direct testimony, initially by  
13 their respective counsel, subject to cross-examination by the  
14 equity committee. And they will appear at this point, as far  
15 as we know, in the following order: Mr. Daniel Groper from  
16 Aurelius, Mr. Daniel Krueger from Owl Creek, Mr. James Bowling  
17 (ph) from Appaloosa, and then Mr. Vivek Melwani from  
18 Centerbridge.

19 And lastly, Your Honor, the debtors would then call  
20 Mr. William Kostoros, who was also requested to be in the  
21 courtroom by the equity committee, and the debtors will put  
22 Mr. Kostoros on by direct testimony, subject to cross-  
23 examination by the equity committee, and any others actually,  
24 Your Honor.

25 So with that, Your Honor, we would like to call

1 Mr. Klamser, and I --

2 THE COURT: Well, wait --

3 MR. ROSEN: -- would turn the podium over to  
4 Ms. DiBlasi.

5 MR. SARGENT: A couple of procedural points I could  
6 raise with the Court before we start.

7 THE COURT: Yes.

8 MR. SARGENT: Edgar Sargent on behalf of the equity  
9 committee, Your Honor, thank you.

10 First of all, what I heard Mr. Rosen to say is that  
11 Mr. Anderson will be presented today to the extent that there's  
12 time. It wasn't our understanding that that was the agreement.  
13 Unfortunately, he has a commitment tomorrow morning in  
14 California that just cannot be changed, and so he needs to go  
15 on today, regardless.

16 We offered a compromise that we would put him on with  
17 a declaration and use the deposition testimony as cross, if  
18 they felt that it was inappropriate to go out of order today,  
19 and they said that no, that they would prefer to put him on  
20 today. So just to make that clear.

21 We filed yesterday, I believe, under seal, a motion  
22 to, seeking standing to file a complaint and adversary action  
23 against two of the funds, Centerbridge and Aurelius, for  
24 equitable disallowance of their claims. And I just wanted to  
25 make it clear to the Court, there's been a lot of papers filed

1 in case you haven't had a chance to review that --

2 THE COURT: Okay.

3 MR. SARGENT: -- we're asking that that motion for  
4 standing be ruled on after this hearing, and that the Court  
5 take into account the evidence that we adduced at this hearing  
6 on the inequitable conduct allegations, take that into account  
7 when deciding the colorable claim prong of the standing motion.

8 Third, Your Honor, we'd like to invoke the Rule. We  
9 think that fact witnesses, to the degree that there are any,  
10 should be excluded from the courtroom before they testify.

11 And finally, at this hearing, this is different from  
12 last time. We've asked that exhibits be moved for admission  
13 prior to any testimony being given on those exhibits, as the  
14 Rules of Evidence require. I think the last time we waited  
15 until the end of the entire hearing to determine what was going  
16 to be admitted. It created a pretty messy record, and it  
17 wasn't clear what was admissible, what wasn't, and we think  
18 it's much better to just proceed as the rules require.

19 MR. ROSEN: Your Honor, with respect to Mr. Anderson,  
20 we believe that that's going to be a non-issue, based upon the  
21 projected time that we see for direct testimony, and what we  
22 have been told by Mr. Sargent to be cross-examination of our  
23 witnesses. However, Your Honor, we have not spoken to the  
24 great masses who are lining up to talk, or who may just want to  
25 come out of the woodwork and ask questions. And as the Court

1 knows last time, there were many people who sought to cross-  
2 examine witnesses, and we --

3 THE COURT: How long do you think you're going to be  
4 on Carreon?

5 MR. ROSEN: His direct? His direct is approximately  
6 thirty minutes, Your Honor. And Mr. Zelin would be  
7 approximately one hour.

8 THE COURT: Well, why don't we do Anderson after  
9 Carreon, same issues?

10 MR. ROSEN: That's fine with us, Your Honor.

11 THE COURT: It should fit him in, be able to do it  
12 today.

13 MR. ROSEN: Okay. Again, Your Honor, we don't know  
14 who else will want to cross-examine Mr. Carreon, though.

15 THE COURT: All right.

16 MR. ROSEN: With respect to the motion that was filed  
17 yesterday, Your Honor, we did get a copy, both a sealed and an  
18 unsealed version, or we did get the copy that was filed under  
19 seal, and we note that it is on for July 28th, Your Honor.

20 We're not going -- or they're asking that it be on for  
21 July 28th. We're not taking a position with respect to that  
22 today or tomorrow at this confirmation hearing. What the Court  
23 decides to do with respect to that record, I assume the Court  
24 will make the decision on July 28th. And it's --

25 THE COURT: Well, I think you're on notice that --

1 MR. ROSEN: We do, Your Honor, but we will reserve our  
2 rights to object to that if we deem it appropriate, Your Honor.

3 THE COURT: All right. Well, I have scheduled it for  
4 the 28th, so we'll hear it on the 28th, and --

5 MR. ROSEN: And with respect to the exhibits, Your  
6 Honor, we note that the equity committee has chosen not to be  
7 agreeable with respect to any of the exhibits that were  
8 suggested to be tendered, so Your Honor, we will just go  
9 forward and deal with that as and when they are introduced on  
10 both sides.

11 THE COURT: Okay.

12 MR. ECKSTEIN: Your Honor, good morning, Kenneth  
13 Eckstein of Kramer Levin on behalf of Aurelius. Just two brief  
14 points in response to Mr. Sargent.

15 With respect to the complaint that was filed last  
16 night that accompanied the motion for authority to bring an  
17 action on behalf of the --

18 THE COURT: Well, it was attached to the motion, it  
19 wasn't filed.

20 MR. ECKSTEIN: That's correct, Your Honor, it was  
21 attached. I'm assuming obviously Your Honor will hear lengthy  
22 evidence over the next several days, but with respect to what  
23 the Court considers, I'm assuming we can defer that until the  
24 Court hears the motion. I understand what Mr. Sargent is  
25 suggesting, and I understand Your Honor's indication that



1 you're going to be hearing the evidence. And I think we'll  
2 just deal with that, if that's appropriate at the hearing.

3 THE COURT: Well, I feel confident that you are going  
4 to put on evidence that suggests that the claim is not a  
5 colorable claim.

6 MR. ECKSTEIN: Your Honor, we absolutely --

7 THE COURT: At this time, so --

8 MR. ECKSTEIN: Your Honor, we absolutely intend to do  
9 that.

10 THE COURT: All right. I think again you're on notice  
11 of what they're asking, but --

12 MR. ECKSTEIN: We are.

13 THE COURT: -- I'm inclined to not erase my memory --

14 MR. ECKSTEIN: I'm assuming.

15 THE COURT: -- of what I hear the next few days.

16 MR. ECKSTEIN: I'm assuming you're not going to erase  
17 your memory, Your Honor. I just wanted to note that we'll deal  
18 with that as a technical matter, I assume, later.

19 The other issue that Mr. Sargent raised, and I just  
20 want to clarify it so that there's no misunderstanding. With  
21 respect to parties who may be testifying at different stages of  
22 this hearing listening to earlier stages of the hearing. What  
23 we had understood was that phases one and two of the trial were  
24 as Mr. Rosen described. We had -- there are several clients  
25 who are obviously interested in what is taking place at the

1 confirmation hearing. We had assumed that there would not be a  
2 problem with parties who may testify here in phases one and  
3 two, but that with respect to phase three, that any witness who  
4 was going to testify would not be in the courtroom or listening  
5 to phase three before they testified.

6 I just wanted to make sure that that was acceptable to  
7 Your Honor.

8 THE COURT: Yeah. Were you suggesting that I bar them  
9 from the entire confirmation hearing?

10 MR. SARGENT: Yes, we were. There will be some issues  
11 that may arise with some of the witnesses in phase one and two  
12 that are least tangentially related, if not essentially  
13 related, frankly, to the insider trader allegations.

14 So we believe it would be appropriate to just follow  
15 the Rule as it's traditionally followed.

16 MR. ROSEN: Your Honor, Mr. Sargent has just flip-  
17 flopped. Because previously, he wrote e-mails, he represented  
18 to many people in this courtroom that phases one and two would  
19 not have anything to do with alleged inequitable conduct, and  
20 now he is saying directly the opposite.

21 THE COURT: Well, let me do this. I'm going to allow  
22 them in on the general confirmation issues. To the extent that  
23 the debtor or anybody else starts to get into the insider  
24 trading issues, then please object and I will exclude the  
25 witnesses relevant to that. But I think that since their

1 testimony is not relevant to the first two issues, they can sit  
2 in.

3 MR. SARGENT: Thank you, Your Honor.

4 MR. ROSEN: Your Honor, also just for the record, the  
5 debtors have asked our five witnesses that I referred to  
6 earlier to leave the courtroom. Mr. Kostoros is here, he is  
7 the corporate representative, and we are asking him to stay in  
8 the courtroom as well.

9 THE COURT: As a party?

10 MR. ROSEN: Yes. Your Honor, additionally, it is  
11 possible based upon some of the testimony that might be  
12 elicited that the debtors may add additional rebuttal  
13 witnesses, as we included in our notice that we filed with the  
14 Court last week.

15 THE COURT: Okay.

16 MR. STARK: Good morning, Your Honor, Robert Stark  
17 from Brown Rudnick. I rise for two quick issues.

18 The first is that I want Your Honor to understand that  
19 there are two separate trust preferred groups here, separately  
20 represented. I have a trust preferred consortium, Mr. Kaplan  
21 represents certain holders of TPS securities, and there's not  
22 an overlap. So I want to make sure that as the proceeding goes  
23 forward, if Mr. Kaplan speaks or I speak, it's not overlap, we  
24 have sort of independent clients, independent rights to be  
25 heard. So I hope we'll be recognized in that regard.

1           The second issue is a little bit more substantive.  
2           We've raised some, what I think, very significant  
3           jurisdictional issues in our papers, and we're going to need to  
4           talk about that. I'm happy to reserve it for the end, I'm  
5           happy to do it now. I just didn't want it to come and haunt me  
6           that if that's going to be included at the closing, that by not  
7           rising now before we got started, I've somehow precluded my  
8           ability to talk about that and say that all of this is not a  
9           worthwhile endeavor. So it's up to Your Honor how you'd like  
10          to proceed.

11           THE COURT: Well, let me ask you: If I agree with  
12          your position that I don't have jurisdiction to decide these  
13          issues, is not the procedure that I hear the evidence and  
14          present proposed findings and conclusions to the District  
15          Court?

16           MR. STARK: It would be, Your Honor, and so that's one  
17          way that we can handle it. There's a variety of other ways,  
18          but that's a perfectly legitimate way to proceed --

19           THE COURT: Okay.

20           MR. STARK: -- as I read Stern versus Marshall, so if  
21          that's -- with that in mind --

22           THE COURT: I daresay the District Court would not  
23          want me to send the entire thing over to them.

24           MR. STARK: No.

25           THE COURT: But --

1 MR. STARK: It still would be a de novo hearing before  
2 them.

3 THE COURT: Of course. It's not --

4 MR. STARK: So I don't know if he would --

5 THE COURT: Sub de novo review.

6 MR. STARK: I don't know if Judge Sleet's going to  
7 avoid it anyway, is all I'm saying.

8 THE COURT: I understand, but I think that we can  
9 proceed with the testimony and make a ruling on what issues, if  
10 any, I have jurisdiction to decide on a final basis or what  
11 issues, if any, I can only do a proposed ruling on.

12 MR. STARK: Understood. Thank you, Your Honor.

13 MR. SACKS: Your Honor, Robert Sacks from Sullivan and  
14 Cromwell. Just on the last point, so we don't get double and  
15 triple teamed again. I don't believe it's correct that  
16 Mr. Kaplan represents an independent group of trust preferred  
17 holders. Or excuse me, they're not trust preferred holders,  
18 they're preferred equity holders under Your Honor's ruling.

19 They are a subset of Mr. Stark's clients, and I  
20 understand that Mr. Kaplan's here for conflict purposes, but  
21 based upon the statements that have been filed, they are a  
22 subset, and I don't think we should be hearing the same thing  
23 from two separate counsel to extend this hearing unnecessarily.

24 I mean, if Mr. Kaplan is going to be examining the  
25 witnesses, Mr. Stark doesn't have to do it, and if Mr. Stark is

1 going to do it, Mr. Kaplan doesn't have to do it. They  
2 represent the same interests.

3 MR. STARK: May I respond, Your Honor?

4 Your Honor, I try a lot of cases, Mr. Kaplan tries a  
5 lot of cases, we know how to do it. If I'm going to be  
6 repeating what he's going to say, I don't think Your Honor will  
7 let me do that. I think the same for him. We do not have the  
8 same client base, we have ethical walls between us, I have not  
9 addressed the issues that he's addressing before this Court, I  
10 don't expect that I'm going to say anything on all that -- on  
11 all those matters. I might, but Mr. Sacks is completely  
12 inaccurate. I'm here representing an independent group.

13 MR. SACKS: Your Honor, again, Robert Sacks. I'm  
14 looking at the 2019 statements that they filed. It's a subset  
15 of the same client base, and they should not -- it's no more  
16 different than if Mr. Landis gets up and examines the same  
17 witness after I examine the witness, representing JPMorgan  
18 Chase. I mean, we shouldn't have to hear multiple lawyers for  
19 the same parties examining a witness time and time again.

20 THE COURT: I'm going to reserve on this. Mr. Stark,  
21 you represent the larger group?

22 MR. STARK: Yes, Your Honor.

23 THE COURT: I'm going to suggest --

24 MR. STARK: He is accurate. The 2019 statements,  
25 there is a subset of my larger group, but I filed papers on one

1 particular aspect of this case, largely the bankruptcy issues;  
2 Mr. Kaplan is representing a subset of the group on different  
3 matters. They've had different conference calls, and they talk  
4 about different things.

5 Again, Your Honor, I don't anticipate that I'm going  
6 to be repetitive. Your Honor has seen me in court a lot, it's  
7 not really what I do.

8 THE COURT: I'm going to suggest this. Since you're  
9 the larger group, you will go first, and I will assure that  
10 there's no repetition from the subset.

11 MR. STARK: I understand. But again, my task is  
12 different, so he may speak when I don't.

13 THE COURT: All right. I will allow it then.

14 MR. SPENCE: Good morning, Your Honor, Stephen Spence  
15 on behalf of the various former officers, Todd Baker, Tom  
16 Casey, Brooks, Horvath, McMurray, Schneider.

17 Mr. Rosen offered up and didn't ask for the Court's  
18 reaction on the possibility of certain parties not having to be  
19 present throughout the proceedings, and reserving the right to  
20 make argument at the close, we're one of those groups.

21 Mr. Wisler has a client I think fits into that  
22 category. The only observation I -- we'd like that  
23 opportunity, if we could save some costs for our clients. And  
24 two, the only factual matter that we would refer to is the  
25 existence of the amended and restated bylaws of Washington

1 Mutual as being part of the record, if you will, for purposes  
2 of the closing argument.

3 THE COURT: Okay.

4 MR. SPENCE: So unless there's an objection as to  
5 references to that particular document for it being directly in  
6 evidence, then we'd like to be at the tail end making argument  
7 only about the relevant Section 36.6 provision that we objected  
8 to.

9 THE COURT: Uh-huh.

10 MR. SPENCE: If I may -- if we may.

11 THE COURT: Any objection by any party? The Court  
12 certainly has no objection.

13 MR. SPENCE: And I think Mr. Wisler would come up here  
14 and say the same thing.

15 THE COURT: Same issues.

16 MR. SPENCE: Thank you, Your Honor.

17 THE COURT: Same with respect to him.

18 MR. SPENCE: And we'll probably part company with  
19 everybody, and good luck.

20 MR. HALPERIN: Good morning, Your Honor, Alan  
21 Halperin, Halperin, Battaglia, Raicht, on behalf of Normandy  
22 Hill.

23 Different issue, same point. We think we can be  
24 deferred to the end, and I prefer to save my client a few bucks  
25 if I can, and defer to the end, and avoid some of this.



1 THE COURT: You may.

2 MR. HALPERIN: Thank you, Your Honor.

3 MR. ROSEN: With that taken care of, Your Honor, I  
4 would turn the podium over to Ms. Kelly DiBlasi. She'll be  
5 handling the first two witnesses, Messrs. Klamser and Sharp.

6 THE COURT: All right.

7 MS. DIBLASI: Good morning, Your Honor. Kelly DiBlasi  
8 from Weil Gotshal and Manges on behalf of the debtors.

9 Your Honor, the first -- the debtor's first witness in  
10 support of confirmation is Mr. Robert Klamser. He is the  
11 director and senior managing consultant at KCC, who is the  
12 debtor's solicitation and tabulation agent in these cases.

13 We would like to offer Mr. Klamser's direct testimony  
14 via his declaration, which was filed on the docket.  
15 Mr. Klamser is in the courtroom.

16 THE COURT: Well, why don't you give us the docket  
17 number, just for the record.

18 MS. DIBLASI: Oh, sure.

19 THE COURT: If anybody knows that.

20 MS. DIBLASI: We're checking on that right now, Your  
21 Honor. I have a copy of it with me if you'd like, I can hand  
22 it up.

23 THE COURT: You can.

24 MS. DIBLASI: Your Honor, that's Docket No. 8113. And  
25 that was filed last Friday, July 8th.

1 THE COURT: Thank you.

2 MS. DIBLASI: Mr. Klamser is in the courtroom today.  
3 I have no additional questions on direct for him, but he's  
4 available for cross-examination if anyone would like.

5 THE COURT: All right. Does anybody wish to cross-  
6 examine Mr. Klamser? Mr. Steinberg.

7 MS. DIBLASI: I would ask that Mr. Klamser please be  
8 released from the remainder of the proceedings.

9 THE COURT: I think he might be being crossed.

10 MS. DIBLASI: Oh, I'm sorry. Oh, I'm sorry, I didn't  
11 see you.

12 MR. STEINBERG: Yeah, I do want to cross him.

13 THE COURT: All right. He should take the stand.  
14 Please step up, remain standing, so you can be sworn.

15 THE CLERK: Raise your right hand.

16 ROBERT KLAMSER, WITNESS, SWORN

17 THE CLERK: Be seated. State your first and last name  
18 and spell your last name.

19 THE WITNESS: Robert Quincy Klamser, it's K-l-a-m-s-e-  
20 r.

21 DIRECT EXAMINATION

22 BY MR. STEINBERG:

23 Q. Good morning, Mr. Klamser. My name is Arthur Steinberg  
24 from King and Spalding. I represent the litigation tracking  
25 warrant holders, which is Class 21 and perhaps Class 12 under

1 the sixth modified plan.

2 A. Uh-huh.

3 Q. I have a couple of questions with regard to how you  
4 solicited Class 21. And before I ask, is it my understanding  
5 that your testimony is being proffered for certain of the  
6 classes, but not all of the classes, as to how they were  
7 solicited?

8 A. That's correct.

9 Q. And that you were soliciting the Class 12 unsecured  
10 claims?

11 A. Yes.

12 Q. And you also -- also reporting on the Class 21 Dime  
13 warrant holders, right?

14 A. Only the registered holders from Class 21.

15 Q. The nonregistered holders are being --

16 A. By my colleague, David Sharp.

17 Q. Okay. And could you tell us how you solicited the  
18 registered holders?

19 A. How --

20 Q. How you got the names, how --

21 A. The registered names were available from the transfer  
22 agent, and -- were available from the transfer agent. Those  
23 were provided to David Sharp, and we put those names into our  
24 claims database, similar to the other classes, and generated  
25 ballots for those claims that were all unique to the holders,

1 and then they were distributed per the solicitation procedures.  
2 We followed the same procedures that we did for all the other  
3 classes.

4 Q. And you said you got it from the warrant agent? Is that  
5 Mellon?

6 A. I believe so. You would have to -- David Sharp is the one  
7 who acquired those records.

8 Q. Okay. And on your report, you have -- in your exhibits,  
9 the results of the stock election, and the results of the  
10 release with respect to the registered names; is that correct?

11 A. That's correct.

12 Q. And have you -- do you have your declaration?

13 A. No, I don't.

14 MR. STEINBERG: Can someone hand him his declaration?

15 THE WITNESS: Thank you.

16 Q. If you can turn to Exhibit C, which is the section on  
17 releases.

18 A. Right.

19 Q. I call your attention to the column called voting amount.

20 THE COURT: Are you in Class 21 of Exhibit C?

21 MR. STEINBERG: Yes.

22 THE COURT: Okay.

23 Q. Voting amount. And there are dollar signs next to the  
24 voting amount. How did you determine what the dollar amount of  
25 these Class 21 claims were?

1 A. There are dollar signs. It's actually the position, the  
2 number of shares held, so it's -- it shouldn't be formatted as  
3 currency. It should just be a number. So if it says one  
4 dollar, it's actually one share.

5 Q. One litigation tracking warrant?

6 A. Or one warrant, that's correct.

7 Q. Okay. So these aren't dollars, these are litigation  
8 tracking warrants.

9 A. Yeah.

10 Q. So if I looked at page 90 of 90, and looked at the first  
11 entry which says eight dollars, and that person having agreed  
12 to give a release, that is not eight dollars, but eight  
13 litigation tracking warrants, right?

14 A. Yeah, that's correct.

15 Q. Okay. Now, your declaration also said that you solicited  
16 claims pursuant to the claims bar date; is that correct?

17 A. Yes, that's correct.

18 Q. And isn't it true that you did not give the claims bar  
19 notice to the people who got the election notice in this case,  
20 the election for stock and the election for release?

21 A. I'm not sure I understand the question. That we didn't  
22 give a notice of bar date to --

23 Q. To the same people that you gave the stock election notice  
24 to.

25 MS. DIBLASI: Objection, Your Honor, I think this is

1 beyond the scope of Mr. Klamser's testimony.

2 THE COURT: Overrule, I'll allow it.

3 THE WITNESS: Can you repeat the question one more  
4 time, please?

5 BY MR. STEINBERG:

6 Q. Did you give the claims bar notice to the same people that  
7 you gave the stock election notice to Class 21?

8 A. No. The bar date notice was not distributed to holders of  
9 Class 21.

10 Q. How come?

11 A. Because the notice of bar date, it wasn't delivered -- it  
12 wasn't mailed out to common stockholders in Class 22 or the  
13 Dime warrant holders in Class 21. It was made publicly  
14 available on our website, and I know that it was published in  
15 various newspapers, but it wasn't distributed. It's not normal  
16 procedure in a bankruptcy case to send a notice of bar date to  
17 stockholders or any other kind of security holder.

18 Q. But it wasn't difficult to get those names, because you  
19 got these names from the warrant agent who maintains the  
20 register; isn't that correct?

21 A. Right.

22 Q. Okay. So let's talk about your Exhibit C, which are the  
23 parties who gave the release. Did you do a total of how many  
24 of the litigation tracking warrant holders actually gave the  
25 release?

1 A. I didn't in my exhibit, but I have that data, and I can  
2 get --

3 Q. What is the data?

4 A. Pardon?

5 Q. What is the data?

6 A. I don't have it in my declaration. I don't know off  
7 the --

8 Q. You mean total?

9 A. No, not in here, but I can.

10 Q. Right. Your colleague Mr. Sharp actually totaled it for  
11 the nonregistered names; isn't that correct?

12 A. I believe so.

13 Q. For the release holds, but you didn't total it?

14 A. Right.

15 Q. Okay. Well, did you -- do you have the data as to the  
16 aggregate of the Class 21 holders who made the stock election?

17 A. The --

18 Q. Which is your Exhibit B, right?

19 A. Exhibit B, yes.

20 Q. Right. Do you know how many of the Class 21 holders made  
21 the stock election?

22 A. I don't have a summary in my declaration, but I have the  
23 underlying data in a file that would be very easy to total, if  
24 I needed it.

25 Q. Okay. And your colleague in his declaration actually

1 didn't total the stock election, he only totaled the release  
2 election. Do you know why that was the case?

3 A. I do not know why.

4 Q. Okay. You have a sense, though, as to what level of the  
5 litigation tracking warrant holders actually opted for the  
6 stock; a large amount, a small amount?

7 A. I believe it's a small amount, but I mean, small is  
8 relative.

9 Q. Right. And how many litigation tracking warrants are  
10 there for Class 21?

11 A. I don't know that number off the top of my head.

12 Q. Okay. If I told you it was around 110 to 113 million  
13 dollars would that -- 113 million warrants, would that sound  
14 right?

15 A. I --

16 Q. You just don't know?

17 A. No.

18 Q. Okay. And do you know what percentage of the class of the  
19 Class 21 actually opted to give the release at this time?

20 A. I don't know the summary, no. That wasn't reported in my  
21 declaration, and like I said, I have the underlying data and  
22 it's very easy to subtotal, but it wasn't something that was  
23 subtotaled for the purposes of the declaration.

24 Q. Do you know whether it's a large amount or a small amount  
25 that opted to give the release at this time?



1 A. It appears to be a small -- I mean, it appears to be a  
2 larger amount that -- no. No, I don't. I wouldn't feel  
3 comfortable saying.

4 Q. Okay. Now, you also did the calculation for late filed  
5 claims.

6 A. Yes.

7 Q. And what's the definition of late filed claims under the  
8 plan?

9 A. Claims that were received after the bar date.

10 Q. So if people didn't get notice of the bar date and filed  
11 it, let's say two weeks after the bar date, that would be  
12 listed as a late filed claim for purposes of the plan, right?

13 A. That's correct.

14 Q. All right. And the debtor has estimated at the end, that  
15 it expects that there will be no allowed late filed claims in  
16 this case, right?

17 A. That's my understanding, yes.

18 Q. Okay. Now, you did a calculation for Class 12, which is  
19 the unsecured class, right?

20 A. Yes.

21 Q. And do you know whether there are claims in Class 12 that  
22 trade during the course of this case?

23 A. Yes. There are -- claims in Class 12 can be traded during  
24 the course of this case.

25 Q. Right. Were there -- did Class 12 creditors, were they

1 entitled to make a stock election?

2 A. Yes.

3 Q. And were they allowed -- did they have to indicate also  
4 whether they were going to give a release or not?

5 A. Yes.

6 Q. And even though the Class 12 creditors may have made a  
7 stock election, was there any restriction on them from  
8 subsequently trading their claims?

9 A. No, not that I'm aware of.

10 Q. Wasn't that administratively difficult for you to manage  
11 the Class 12 register by not stopping the trading in Class 12  
12 claims like it was done for the other security holders?

13 A. No, it was not.

14 Q. It's not difficult?

15 A. Not on the claim -- not in the Class 12, it's not.

16 Q. It's not difficult for that?

17 A. It's not difficult in Class 12 to monitor the trades that  
18 happen after release is made, no, it's not.

19 Q. Is it difficult to monitor the trades in Class 21 for the  
20 registered holders?

21 A. I -- that would be a question better suited for David  
22 Sharp. I don't manage the trading or the logistics of tracking  
23 ballot responses for the -- any of the securities.

24 Q. Do you have any sense whether you think you could do it?

25 A. I don't think we can. I mean, no, I don't.

1 Q. You don't know one way or the other?

2 A. I don't have a sense of the legality of it, and of the  
3 mechanics of it.

4 Q. Okay.

5 A. I think it's more of a legal issue than a mechanical  
6 issue, but I don't --

7 Q. Oh, you don't think it's an administrative convenience  
8 issue, you think it's a legal issue?

9 A. I believe it is. I don't know for sure. I mean, I know  
10 on our side, legally claims in Class 12, claims were allowed to  
11 be traded or claims were allowed to be purchased, and  
12 mechanically, we could follow that procedure.

13 Q. So Class 12 unsecured creditors who make a stock election  
14 could still continue to trade their claims today if they wanted  
15 to?

16 A. I believe yes, they're still --

17 Q. While Class 21 holders, registered or nonregistered, who  
18 made a stock election under the plan, were prohibited from  
19 trading their warrants after the date they made their election;  
20 isn't that correct?

21 A. That's my understanding, yes.

22 Q. And you think the issue may be a legality issue as  
23 compared to a convenience issue, or you don't know?

24 A. I believe so. It's my -- it's not my area of expertise.  
25 I know it's not my area of expertise.

1 Q. So you don't know?

2 A. Yeah, correct, I don't know.

3 MR. STEINBERG: I have no other questions for this  
4 witness.

5 THE COURT: Thank you. Anybody else wish to cross the  
6 witness?

7 No? Redirect?

8 MS. DIBLASI: Just a few questions, Your Honor.

9 REDIRECT EXAMINATION

10 BY MS. DIBLASI:

11 Q. Mr. Klamser, was the notice of the bar date served on the  
12 agent for the Dime warrant holders?

13 A. I believe it was, yes.

14 Q. And does KCC have any control over what the agent does or  
15 does not do with that bar date notice?

16 A. No, we don't.

17 Q. Are the registered holders of the Class 21 securities the  
18 same people today as they were as of the date that the bar date  
19 notice was served?

20 A. I would assume no, not as of the date that the bar date  
21 notice was served, because they're still tradable.

22 Q. The Class 21 security holders were given the option to  
23 reserve their decision on whether to grant the releases for up  
24 to a period of one year from the effective date, correct?

25 A. Yes, that is correct.

1 Q. And you previously testified in response to  
2 Mr. Steinberg's questions that the claims in Class 12 were  
3 permitted to trade even after claimants in that class may have  
4 granted releases, correct?

5 A. Yes, that's correct.

6 Q. Do the claims in Class 12 trade with frequency?

7 A. No, they do not.

8 Q. How does KCC become aware of the fact that a claim in that  
9 class has traded?

10 A. There will be a notice of transfer that's filed on the  
11 docket. And so KCC reviews the docket, reviews that transfer,  
12 and compares it to the claims register, and then we would  
13 effectuate a transfer if one is actually filed.

14 Q. And can you explain what you mean by effectuate a  
15 transfer?

16 A. Absolutely. We update the creditor's name and address  
17 information on the claims register, so if creditor A  
18 transferred their claim to purchaser B, the name on the claims  
19 register, the name and address once it's effective or once it's  
20 effectuated, the claims register would reflect that purchaser B  
21 now owns the claim. And any notices would go to purchaser B.

22 Q. So using your same example, if creditor A had granted the  
23 release and subsequently traded to creditor B, how is it that  
24 KCC would track that release and that claim?

25 A. The release is actually -- the release transfers with the

1 claim in our records, I mean, our records would indicate that  
2 if claim 100 was transferred, and creditor A granted the  
3 release for claim 100, we would then track that, the release  
4 was still granted for class -- for claim 100, even if it's been  
5 transferred to creditor B. So it follows the creditor  
6 essentially.

7 MS. DIBLASI: Okay. I have no further questions.

8 THE COURT: Recross?

9 MR. STEINBERG: Yes.

10 RECCROSS-EXAMINATION

11 BY MR. STEINBERG:

12 Q. Mr. Klamser, you indicated that the bar date notice was  
13 served on the warrant agent, right?

14 A. That's correct.

15 Q. Okay. Do you know under the warrant agreement, who the  
16 warrant agent takes instructions for -- from?

17 A. I do not.

18 Q. Would it surprise you to know that they take instructions  
19 from Washington Mutual, Inc.?

20 A. Like I said I don't know, so I --

21 Q. Maybe if you wanted to read at Section 5.1 of the warrant  
22 agreement. Do you know whether anybody from the company  
23 instructed the warrant agent not to file a claim on behalf of  
24 the litigation tracking warrant holders?

25 A. No, I'm not aware of that.

1 Q. Do you know whether the warrant agent actually filed a  
2 claim for the litigation tracking warrant holders?

3 A. Not off the top of my head I don't.

4 Q. Okay. Do you know any reason why he would not have?

5 A. No.

6 Q. Okay. Now, you were asked the question about people don't  
7 have to give the releases until one year after the effective  
8 date of the plan, right?

9 A. That's correct, yes.

10 Q. Okay. And what happens if the issues regarding to the  
11 litigation tracking warrants weren't decided by the appellate  
12 process within that one-year time period, do you know what  
13 happens then?

14 A. I do not know.

15 Q. Would it surprise you if I told you that they would have  
16 to make a decision to give a release or not, and waive  
17 distributions without knowing how the appeal process went,  
18 under this plan?

19 A. It wouldn't surprise me, because that's the procedures.

20 Q. Does it strike you as being fair?

21 A. It's the procedures.

22 Q. Okay. Now, you were asked that as of the bar date that  
23 there was a turnover of the people who were trading in the  
24 warrants. Trade -- there is an active market, right, for the  
25 warrants?

1 A. An active market?

2 Q. Trading market for the warrants.

3 A. To be honest, I'm not -- the logistics of how the warrants  
4 are traded, it's not in my expertise.

5 Q. Okay. That's Mr. Sharp, right?

6 A. That's correct.

7 Q. Okay. So if there was a trade of a registered holder, do  
8 you know whether they would have to give Mellon notice that  
9 they had just traded out, and Mellon would then adjust the  
10 record in the same way that you do for the claims?

11 A. Again, it's a question better suited for Mr. Sharp.

12 Q. And I think you said that as of the bar date, there was a  
13 trading market for the warrants, and that there was a turnover.  
14 But you -- of who were the warrant holders. But are -- you're  
15 not saying that nobody was a warrant holder as of the bar date,  
16 is still not a warrant holder now. There was a trading factor,  
17 but it wasn't a hundred percent turnover, was it?

18 A. I don't know for sure the trading factor. I mean, I don't  
19 know how much turnover there was. I just know that between --  
20 I can assume that from the time the notice of bar date was sent  
21 out until solicitation, at least one of the warrants would've  
22 traded, but it's just my assumption.

23 Q. Okay. But you don't know the level of trading?

24 A. I do not.

25 MR. STEINBERG: Okay. Thanks.



1 MS. DIBLASI: I have nothing further, Your Honor.

2 THE COURT: All right. You may step down,  
3 Mr. Klamser.

4 THE WITNESS: Thank you.

5 MR. ROSEN: Your Honor, while we go get Mr. Sharp to  
6 come in to testify, I would like to note that my comment  
7 earlier I think is proving true, we don't know who's going to  
8 come up and ask questions. And while Mr. Steinberg has a  
9 thirst for the theatric, Your Honor, I would like to note that  
10 pursuant to the Court's order, a 337 million dollar claim has  
11 been reserved. Mr. Steinberg has --

12 THE COURT: All right. Save it --

13 MR. ROSEN: He has nothing to say here in this case.

14 THE COURT: No, no. You can save it for argument to  
15 the end. He's a party in interest and can be heard.

16 MR. STEINBERG: Your Honor, as long as we're killing  
17 time, can I say something? Not in response to what --

18 THE COURT: No, no.

19 MR. STEINBERG: I just think that --

20 THE COURT: No, no. I don't need testimony or  
21 argument from attorneys.

22 (Pause)

23 MS. DIBLASI: Your Honor, the debtor's next witness in  
24 support of confirmation is Mr. David Sharp. He is also with  
25 KCC. Mr. Rosen just handed you a copy of Mr. Sharp's

1 declaration, which was filed on the docket as Docket No. 8108.

2 I also would like to submit Mr. Sharp's declaration as  
3 his direct testimony. He is in the courtroom today, and is  
4 available for cross-examination. I have no additional  
5 questions for him on direct, but reserve the right to ask  
6 questions if anybody would like to cross him.

7 THE COURT: All right. Anybody wish to cross-examine  
8 Mr. Sharp? Yes. Mr. Sharp, you should take the stand. And be  
9 sworn.

10 THE CLERK: Please raise your right hand.

11 DAVID SHARP, WITNESS, SWORN

12 THE CLERK: State for the record your first and last  
13 name, spelling your last.

14 THE WITNESS: David Sharp, S-h-a-r-p.

15 THE COURT: Before cross, I think I should have done  
16 this with Mr. Klamser, but just for the record, is your  
17 declaration, which is docket entry 8108, what you would testify  
18 on direct if asked?

19 THE WITNESS: It is, Your Honor.

20 THE COURT: All right. You may cross.

21 CROSS-EXAMINATION

22 BY MR. SARGENT:

23 Q. Do you have -- good morning, Mr. Sharp. I'm Edgar Sargent  
24 from Sussman Godfrey and we represent the equity committee in  
25 this action.

1 Do you have a copy of your declaration?

2 A. Yes, I do.

3 Q. I believe it's Defendant's Exhibit 377.

4 MR. SARGENT: The Court has a copy also?

5 THE COURT: I have it.

6 Q. I just have a couple of quick questions about it. One of  
7 the things that KCC tabulated in this case are the elections by  
8 certain creditors to take common stock in the reorganized  
9 debtor as opposed to cash; isn't that correct?

10 A. That is correct.

11 Q. And that's one of the items that you addressed in your  
12 declaration.

13 A. Correct.

14 Q. And could you turn to Exhibit B, which is attached to your  
15 declaration? It's about halfway through. It says Class 2 at  
16 the top --

17 A. Yes.

18 Q. -- page 104. And I'd just ask you to explain how to read  
19 this chart, the -- particularly the last three columns.

20 A. The election that was on the ballots that the holders  
21 received asked them what percentage of various distributions  
22 they were getting under the plan that they would prefer instead  
23 to receive as common stock in the reorganized company.

24 So the first column was an indication from the balance as  
25 to what percentage of the cash that they would be receiving if

1 the plan is approved, that they would prefer instead to receive  
2 as common stock.

3 So if you look at the first -- make sure I'm on the first  
4 example. The first example where they chose a hundred percent,  
5 that would mean that that particular beneficial owner was  
6 indicating that of the cash that they would receive under the  
7 plan if it's approved, they wanted a hundred percent of that  
8 cash in stock is what they would prefer.

9 The second column indicates again, the percentage of the  
10 liquidating trust interest that they are to receive under the  
11 plan if it's approved, that they would prefer instead to  
12 receive as common stock.

13 And the last column has to do with the pay over rights,  
14 and again, it's the percentage of common stock they would  
15 prefer to receive.

16 Q. And does this table show only beneficial owners who  
17 elected to receive at least some percentage of common stock  
18 instead of any of these categories? In other words, there's no  
19 zero, zero, zeros?

20 A. There were a few instances where there are going to be  
21 some zero, zero, zeros, and the reason for that would be that  
22 the nominee acting on behalf of the beneficial owner had  
23 tendered that beneficial owner's position into the exchange  
24 election Contra-CUSIP DTC, but then did not indicate any  
25 percentages that were requested.

1           So in that situation, they would just get the standard  
2           distribution under the plan.

3           Q.   Is there any way to tell from this exhibit or from  
4           anywhere in your declaration what percentage of the beneficial  
5           holders in Class 2, what percentage of the value elected to  
6           take the common stock as opposed to cash?

7           A.   I don't believe that calculation's been done yet.  I did  
8           not do that calculation.

9           Q.   And in just the Exhibit B Class 16 page, it's three or  
10          four pages further along, and could you also explain to the  
11          Court how these, the three columns on the right-hand side here  
12          are different from the other chart?

13          A.   The Class 16 election was different than the Class 2, 3,  
14          14, 15 and 21 election.  In that, under the plan, if approved,  
15          Class 16 holders would receive some common stock, some cash,  
16          and some liquidating trust,.

17                 So the exchange election for them was to indicate what  
18          percentage of each of those they preferred to receive instead.  
19          So the percentages would add up to a hundred percent in this  
20          case.

21                 MR. SARGENT:  Okay.  That's all the questions I have  
22          for this witness, thank you.

23   CROSS-EXAMINATION

24                 BY MR. STEINBERG:

25                 Q.   Hello, Mr. Sharp.  I'm Arthur Steinberg from King &

1 Spalding on behalf of the litigation tracking warrant holders,  
2 who are Class 21.

3 Your colleague, Mr. Klasmer (sic) talked about the  
4 solicitation for the registered names, and for Class 21 you did  
5 the solicitation for the unregistered names?

6 A. For any holders, but we call beneficial holders holding in  
7 street name or through the nominees.

8 Q. Do you know what percentage of the litigation tracking  
9 warrant holders are in street name versus registered name?

10 A. I couldn't give you an exact figure, but it would be the  
11 majority of holders hold through street name.

12 Q. Okay. Would it be more than seventy-five percent?

13 A. I couldn't accurately say without doing the calculations,  
14 but typically the large percentage of them hold in street name.

15 Q. Okay. And you in Exhibit C of your declaration, you did a  
16 report as to the number of litigation tracking warrant holders  
17 in street name who opted to give a release; is that correct?

18 A. Correct.

19 Q. And the report actually did a total for that, and  
20 approximately -- is that 15.845 million warrants opted to give  
21 their release?

22 A. Let me just find the page.

23 Q. I have it as page 12 on Exhibit C-1.

24 A. Yeah. The figure is 15,845,486 units --

25 Q. Right.

1 A. -- granted the release.

2 Q. And there 1103 holders who constitute that 15.845,486  
3 million warrants --

4 A. Correct.

5 Q. -- right?

6 A. Uh-huh.

7 Q. Do you know how many warrants are outstanding?

8 A. Not off the top of my head, no.

9 Q. Would it surprise you if I told you it was like 110, 112  
10 million warrants?

11 A. I honestly don't know off the top of my head, so.

12 Q. Do you have any belief as to whether this level of opting  
13 in by the litigation tracking warrant holders as the -- for the  
14 street holders is a large percentage or a small percentage?

15 A. Remember that the litigation trust warrant holders had the  
16 choice of either choosing to grant release now or not, and had  
17 a choice later on. So I think a fairly low percentage of them,  
18 of the total granted release.

19 Q. And the ramifications of giving a release was a cessation  
20 of trading in the warrant, right?

21 A. If they chose to grant the release at this time, their  
22 warrants were tendered into a Contra-CUSIP in which trading is  
23 prevented, that's correct.

24 Q. Okay. And Exhibit B is your list of those who took the  
25 stock election for Class 21, right?

1 A. Correct.

2 Q. And do you know how many of the litigation tracking  
3 warrant holders took the stock election of the people in street  
4 name?

5 A. Are you looking for a percentage?

6 Q. No, just an aggregate number of warrants.

7 A. Well, if it's totaled -- I don't have the total in front  
8 of me, no.

9 Q. Do you know what the total is?

10 A. Not off the top of my head.

11 Q. Any sense? If I told you it was under four million  
12 warrant holders, would you have a sense as to whether that's  
13 right or wrong?

14 A. It's possible. I would have to get a calculator and  
15 figure it out.

16 Q. Do you think that the people who opted for the stock is  
17 less than the people who decided to grant the release? Do you  
18 have any sense of that?

19 A. Potentially. Again --

20 Q. You just don't know?

21 A. -- I would have to get a calculator and --

22 Q. You don't know off the top of your head?

23 A. -- go over the percentages. No.

24 Q. Okay. If -- can you describe how you would deal with the  
25 circumstance if there was trading that was done after someone



1 had opted to give a stock election to be able to try to track  
2 that issue as to whether the new person should be bound by the  
3 stock election? How difficult would it be to do that?

4 A. If someone made the exchange election and were tendered  
5 into that Contra-CUSIP, they are not permitted to trade, so the  
6 units do not trade.

7 Q. Right.

8 A. If you decided to trade it anyway, the trade would fail at  
9 DTC, it would not be permitted. So we have no say as to what  
10 agreement you would personally make with somebody that you were  
11 trading improperly to, but it would not be affected through the  
12 system. The trade would fail.

13 Q. And why would it fail?

14 A. Because DTC does not allow trading in the Contra-CUSIPs.  
15 Once you're tendered into a Contra-CUSIP, there is no trading  
16 permitted.

17 Q. Could you have -- I know that's what the plan said, but  
18 could you have adjusted the circumstance to still allow  
19 trading, but still to track those people who had agreed to  
20 tender their shares of stock?

21 A. DTC does not allow trading in their Contra-CUSIPs.

22 Q. Is it the same issue for registered holders, too?

23 A. Registered holders are not held by the DTC system, they're  
24 held on the books and records of the transfer agent. So it's  
25 up to -- it would be, in that situation, up to the transfer

1 agent to monitor any trades.

2 Q. Does the transfer agent monitor trades now?

3 A. On registered holders, yes.

4 Q. Is there any reason why you believe that he wouldn't be  
5 able to monitor trades after someone tendered shares or not?

6 A. In registered form?

7 Q. Yeah.

8 A. You'd have to ask the transfer agent that. I see no  
9 reason that they couldn't, but that's -- those are registered  
10 holders not the street holders.

11 Q. Okay. Now, your report dealt with not just Class 21, but  
12 also all the security holders, Class 2, Class 16, correct?

13 A. Class 2, 3, 14, 15, 16, 20 and 21.

14 Q. All right. So did you ever do a report as to what  
15 percentage of the overall Class 2, 3 whatever they are, 16, 21,  
16 what percentage of people in those class opted for the stock  
17 election?

18 A. Not specifically the stock election, no.

19 Q. So do you have any sense at all as to who would be the  
20 largest shareholders based on the stockholder elections?

21 A. The -- once we -- what we're gathering is only the raw  
22 data for the stock elections, because there are a lot of other  
23 factors that go into determining exactly what based on those  
24 elections people are getting.

25 So what we do is we take that raw data from the ballots,

1 and we turn it over to Alvarez & Marsal who would be doing the  
2 actual calculations, because they're the only ones that know,  
3 for example, how much stock is permitted to go to Class 2 as  
4 opposed to Class 3. So we only are privy to the raw data that  
5 we hand over to someone else to do the calculations.

6 Q. All right. Do you know what the calculation is for the  
7 percentage of shares in the reorganized entity if this plan is  
8 approved that will be held by the Class 2 holders in the  
9 aggregate?

10 A. I have not seen any of the calculations at this point, no.

11 Q. Do you have any sense as to whether Class 2 would be the  
12 dominant holder of the shares?

13 A. I don't know, and that would be outside the scope of what  
14 I do.

15 Q. Okay. In Class 2 under the plan was entitled to a hundred  
16 percent of their principal plus through the benefit of  
17 subordination a hundred percent of their contractual interest,  
18 right?

19 A. Okay.

20 Q. Do you know that?

21 A. I know that they're entitled to a hundred percent cash.  
22 I'd have to look at the plan specifically to --

23 Q. And yet your report indicates that there are people in  
24 Class 2 who are otherwise offered to get all the cash they  
25 could possibly want, and instead have opted to take stock of

1 the reorganized entity, right?

2 A. There were members of Class 2 who chose to participate in  
3 the exchange election, and request stock in place of some of  
4 their potential distributions under the plan.

5 Q. I would imagine that they think that the stock is a good  
6 buy instead of passing up the cash?

7 A. I would not speculate on that.

8 THE COURT: Can we limit it to factual questions?

9 MR. STEINBERG: Okay.

10 BY MR. STEINBERG:

11 Q. Now, in your report on Exhibit B you report on the stock  
12 election and I didn't see Class 3. I only saw Class 2. Can  
13 you tell me where Class 3 is on what page?

14 I see Class 16, I see Class 14, and I see something  
15 labeled "AKES", page 1 of --

16 A. Yeah, I'm sorry, that should say Class 3. Those are the  
17 CUSIPs underneath that, or the CUSIPs representing the  
18 securities that are in Class 3.

19 Q. So --

20 A. So the CUSIP ending apple Edward three, apple Nancy three  
21 and apple yellow nine are the Class 3 security CUSIPs.

22 Q. Okay. So you meant to write Class 3 when you wrote AKES?

23 A. Correct.

24 Q. Okay.

25 MR. STEINBERG: I don't have any other questions, Your

1 Honor.

2 THE COURT: Thank you. Redirect?

3 MS. DIBLASI: Just one minute, Your Honor.

4 I have nothing, Your Honor.

5 THE COURT: All right. Thank you, Mr. Sharp, you may  
6 step down.

7 MS. DIBLASI: With the Court's permission, may Mr.  
8 Sharp and Mr. Klamser please be dismissed from the remainder of  
9 the proceedings?

10 THE COURT: Any objections?

11 All right. They may.

12 MS. DIBLASI: Thank you.

13 MR. ROSEN: Your Honor, also at this time we'd like to  
14 move for the admission of their declarations into evidence.

15 THE COURT: All right. They will be admitted.

16 (Declaration of Robert Klamser was hereby received into  
17 evidence)

18 (Declaration of David Sharp was hereby received into evidence)

19 MR. MASTANDO: Good morning, Your Honor, John Mastando  
20 from Weil Gotshal on behalf of the debtor. And the debtors now  
21 call Mr. James Carreon in support of confirmation.

22 THE COURT: All right.

23 MR. MASTANDO: Your Honor, may I approach with a  
24 binder of materials for Your Honor?

25 THE COURT: You may and he should take the stand so he

1 can be sworn.

2 JAMES E. CARREONO, WITNESS, SWORN

3 THE CLERK: Please state your name and spell your last  
4 name.

5 THE WITNESS: James Edward Carreon, C-a-r-r-e-o-n.

6 THE CLERK: Thank you.

7 DIRECT EXAMINATION

8 BY MR. MASTANDO:

9 Q. Good morning, Mr. Carreon.

10 A. Good morning.

11 Q. Can you please describe your educational background for  
12 the Court?

13 A. Certainly. I have a bachelors of science degree, and a  
14 bachelor of arts degree from the University of Southern  
15 California. A law degree from Southwestern University and an  
16 LLM in taxation from Golden Gate University.

17 Q. And where are you currently employed?

18 A. I'm a managing director with Alvarez & Marsal tax end.

19 Q. And how long have you held the position of managing  
20 director?

21 A. Almost three years.

22 Q. All right. Can you briefly describe the nature of your  
23 work in that role?

24 A. I provide tax advice mostly in the context of mergers and  
25 acquisitions and troubled company settings.

1 Q. Okay. And how long have you been advising troubled  
2 companies with respect to tax issues?

3 A. For more than ten years.

4 Q. All right. And what types of tax issues have you faced in  
5 your restructuring experience?

6 A. Generally concerns, NOLs, the application of Section 382,  
7 we'll touch upon Section 269, cancellation of indebtedness,  
8 income, consolidation, and rationalization.

9 Q. Could you please list for the Court a few of your  
10 representative restructuring engagements where you provided tax  
11 analysis?

12 A. In addition to Washington Mutual, I have provided analysis  
13 for Lehman, Tribune, Eddie Bauer.

14 Q. Okay. And can you describe your employment background  
15 prior to joining Alvarez?

16 MR. ROSEN: Excuse me one second. Excuse me a second.  
17 Your Honor, I believe that the equity committee has invoked the  
18 rule. We would ask Mr. Anderson to leave the courtroom.

19 MR. SARGENT: Mr. Anderson is an expert and we expect  
20 him to testify on the tax management with respect to the  
21 witness' testimony.

22 THE COURT: Yeah, I don't think he's a fact witness.

23 MR. ROSEN: Well then, they've asked previously from  
24 Mr. Zelin and others to leave also. He is an expert, so he  
25 could attend as well?

1 MR. SARGENT: Mr. Zelin can stay.

2 MR. ROSEN: Thank you.

3 THE COURT: Mr. Zelin may remain. Go ahead.

4 BY MR. MASTANDO:

5 Q. Mr. Carreon, I believe you were describing your prior  
6 employment background prior to joining Alvarez?

7 A. Yes, prior to A&M, I was in the tax practices of FTI  
8 Consulting, Sheppard, Mullin, Richter & Hampton, Ernst &  
9 Young's national office on the West Coast and Deloitte Touche.

10 THE REPORTER: I'm sorry, and?

11 THE WITNESS: Deloitte and Touche.

12 THE REPORTER: Could you just speak up a little bit?

13 BY MR. MASTANDO:

14 Q. Do you currently hold any academy posts?

15 A. Yes. I'm an adjunct tax professor at San Jose State  
16 University and Golden Gate University.

17 Q. And do you currently hold any position at Washington  
18 Mutual?

19 A. I am the vice-president and interim tax manager.

20 Q. Okay. And what are your responsibilities as interim tax  
21 manager of WMI?

22 A. I oversee the day-to-day tax function of WMI, resolve  
23 certain controversy matters, strategic planning.

24 Q. Okay. And in your role as interim tax manager, do you  
25 provide legal advice on tax issues?



1 A. No, I do not, although I have a law degree, I am a part of  
2 a consulting firm, so I am prohibited by state law from  
3 providing legal advice.

4 Q. Okay. Now, are you familiar with the plan of  
5 reorganization in these Chapter 11 cases?

6 A. I generally am.

7 Q. How did you become familiar with the plan?

8 A. I reviewed certain documents, had various discussions with  
9 the A&M restructuring team, as well as certain folks within  
10 WMI.

11 Q. Okay. Now, let's discuss certain features of the modified  
12 plan. Can you describe generally what happens to WMI's assets  
13 upon plan consummation?

14 A. Upon consummation, a portion of the assets are transferred  
15 to a liquidating trust for the benefit of certain creditors,  
16 and the balance remain with WMI, including the stock of  
17 Wimrick, the stock of WMI's canceled and stock of newly  
18 reorganized WMI is issued to certain creditors.

19 Q. Okay. Now, you mentioned Wimrick. What is Wimrick?

20 A. Wimrick is a captive reinsurance company that historically  
21 has provided reinsurance services to WNB and the banking  
22 subsidiaries. It is domiciled in the State of Hawaii and is  
23 currently in run-off mode.

24 Q. Okay. And under the modified plan, what happens to the  
25 stock of reorganized WMI?

1 A. Under the plan, the stock of reorganized WMI goes to  
2 certain creditors.

3 Q. Okay. And how does receiving reorganized common stock  
4 effect a creditor's recovery under the plan?

5 A. Creditors that elect to receive stock of reorganized WMI  
6 do so in lieu of cash and liquidating trust interests.

7 Q. Okay. And which creditors may receive shares of  
8 reorganized common stock pursuant to the modified plan?

9 A. Each of the creditor classes may elect to do so. So the  
10 senior noteholders, senior subordinated noteholders, general  
11 unsecured, CCBs, peers.

12 Q. Okay. And is the consideration provided by the plan, for  
13 instance, creditor cash, liquidating trust interest, and  
14 reorganized common stock, is that sufficient to satisfy the  
15 peers' claims?

16 A. No, it is not.

17 Q. Okay. And is it anticipated that there will be value in  
18 the estates to distribute to stakeholders junior to the peers?

19 A. No.

20 Q. And what are holders of subordinated claims entitled to  
21 receive under the modified plan?

22 A. Subordinating claim holders are entitled to contingent  
23 liquidating trust interest, in the event that the ultimate  
24 recovery is substantially greater than anticipated, such that  
25 it provides for recovery beyond the peers class.

1 Q. And how are existing equity holders treated under the  
2 modified plan?

3 A. Preferred equity holders receive these contingent  
4 liquidating trust interest, and no recovery is provided for the  
5 common shareholders.

6 Q. Let's discuss certain tax implications of the modified  
7 plan. Are you familiar with Section 382 of the Internal  
8 Revenue Code, which is entitled "Limitation on Net Operating  
9 Loss Carry Forwards and Certain Built In Losses Following  
10 Ownership Change"?

11 A. I am.

12 Q. Okay. And can you describe your experience with this  
13 section of the Code?

14 A. For the majority of my career, I have dealt with Section  
15 382. Initially, it was as part of a subpractice at the  
16 national office, dedicated to 382 currently is in the context  
17 of M&A transactions in troubled company settings.

18 Q. And what is your understanding of what a net operating  
19 loss is?

20 A. A net operating loss is a tax term that means that for any  
21 given tax year, the amount of deductions is greater than the  
22 amount of income such that on a net basis, the taxpayer is in a  
23 loss position.

24 Q. Okay. And generally speaking, what is the effect of  
25 Section 382?

1 A. Section 382 provides a tracking mechanism for taxpayers  
2 with NOLs that provides if there's a greater than fifty percent  
3 increase in equity ownership, then an ownership change has  
4 occurred, and the taxpayer's ability to use NOLs to offset  
5 taxable income is limited.

6 Q. Okay. And how might a company use net operating losses?

7 A. Net operating losses can generally be carried back to the  
8 two prior tax years to offset taxable income in those prior  
9 periods, and for the taxpayer to get a refund. It may also be  
10 carried forward for twenty years to offset future taxable  
11 income.

12 Q. Okay. And what is the significance of Section 382 with  
13 respect to these Chapter 11 cases?

14 A. Well, as a general matter, 382 provides for certain  
15 special rules for taxpayers in bankruptcy. But more  
16 specifically, we anticipate that the tax group will experience  
17 an ownership change as a result of the plan becoming effective.

18 Q. Okay. And when does an ownership change occur pursuant to  
19 Section 382?

20 A. It generally occurs when there's a greater percent --  
21 greater than fifty percent increase in equity ownership, new  
22 equity ownership, and a taxpayer that has NOLs.

23 Q. Okay. Now, have you reviewed the stock election results  
24 in these cases?

25 A. I have.

1 Q. And what is your understanding of the overall results of  
2 the stock elections?

3 A. My understanding is that the senior noteholders will  
4 receive approximately twenty-four million shares, and that the  
5 senior subordinated noteholders will receive approximately  
6 thirteen million shares, and that the peers claimants will  
7 receive approximately one hundred twenty-three million shares.

8 Q. Okay. And would that result in an ownership change under  
9 Section 382?

10 A. Yes, it would.

11 Q. Okay. And would there still be an ownership change if  
12 there were value in the estates to distribute to stakeholders  
13 junior to the peers?

14 A. Yes. That would still be the case, because the plan  
15 contemplates that any recovery beyond the peers class would be  
16 in the form of cash, and liquidating trust interest, and not in  
17 the form of a stock of reorganized WMI.

18 Q. Okay. Now, let's turn to your analysis of the net  
19 operating losses potential available to reorganized WMI. Did  
20 -- you have prepared a demonstrative, showing what amount of  
21 pre-2011 net operating losses might be available to reorganized  
22 WMI?

23 A. That is correct.

24 Q. Okay. And if I can pull up --

25 MR. MASTANDO: Kim, please.

1 Q. -- Demonstrative 1, which is entitled Pre-2011 Loss Carry  
2 Forward Potentially Available to Reorganized WMI while WMB is  
3 part of the tax group.

4 Is this the demonstrative that you had prepared?

5 A. Yes, it is.

6 Q. And from where is the information on this demonstrative  
7 taken?

8 A. It is taken from the disclosure statement, the plan, and  
9 Mr. Zelin's report.

10 Q. Okay. And if you take a look at the demonstrative, what  
11 information is contained in the first line of the  
12 demonstrative?

13 A. The first line is the amount of pre-2011 net operating  
14 loss carry forward in the amount of 17.7 billion dollars.

15 Q. And that's the amounts available to the WMI tax group?

16 A. That amount is currently available to the tax group  
17 because WMB is currently a member of the tax group.

18 Q. And what is the WMI tax group?

19 A. The WMI tax group is a group of affiliated corporations  
20 that files a consolidated return for federal income tax  
21 purposes, of which WMI is the common parent, WMB is currently a  
22 member of, and Wimrick is a member of.

23 Q. Okay. And under the plan, what limitations, if any, apply  
24 to the tax groups use of the 17.7 billion dollar NOL?

25 A. Well, taking into account August 31st, effective date and

1 change date, the tax group would experience an ownership change  
2 and its ability to use all of its pre-change losses would be  
3 subject to limitation under 382.

4 That, of course, assumes that WMB continues to be a member  
5 of the group, because the 17.7 billion dollars is almost  
6 exclusively attributable to WMB. And once WMB leaves the  
7 group, whether that's through abandonment or liquidation, the  
8 tax group would no longer have access to that 17.7 billion  
9 dollar NOL.

10 Q. And what durational limitations apply to the pre-2011 loss  
11 carry forward?

12 A. Well, in general, as I've stated, NOLs are subject to a  
13 twenty year carry forward period, but for practical purposes,  
14 the tax group will be limited to the period that WMB continues  
15 to be a member of the group.

16 Q. Okay. And you touched on this as well, but under what  
17 circumstances would WMB cease to be a member of the tax group?

18 A. Well, WMB will cease to be a member of the tax group upon  
19 abandonment, and it also would cease to be a member of the  
20 group upon its liquidation which would likely take place once  
21 the FDIC receivership winds down.

22 Q. Okay. Now, turning back to the demonstrative, what is the  
23 information contained in the second line item?

24 A. The second line item shows the market value of reorganized  
25 WMI, and that amount is 160 million. The next line item is the

1 long term tax exempt rate, which is 4.3 percent. And the final  
2 item is the 382 limitation, calculated for the August 31st  
3 change date of seven million dollars.

4 Q. Okay. So could you just explain, please, the calculation  
5 that is being done here, and why it's being done with these  
6 numbers?

7 A. Certainly. The Code provides that the 382 limitation is  
8 based on the equity value of the taxpayer multiplied by the  
9 appropriate long term exempt rate. Here again, because of the  
10 special rules, bankruptcy rules for Section 382, the equity  
11 value is immediately after the change date.

12 So it's the 160 million multiplied by the 4.3 percent,  
13 which provides for an annual limitation of almost seven million  
14 dollars. And so what that means is that the tax group's  
15 ability to use its losses prior -- generated prior to an August  
16 31st effective date is subject to a rate of seven million  
17 dollars per year.

18 Q. Okay. And is it in the best interests of the debtors'  
19 estates to attempt to preserve the pre-2011 loss carry forward  
20 by retaining the WMB stock?

21 A. I don't believe so because the WMB will not be a member of  
22 the tax group on a long term basis.

23 The debtor has before the Court a motion to abandon the  
24 stock prior to the effective date, so obviously if that were  
25 granted, then WMB would no longer be a part of the tax group.



1           WMB would also be liquidated upon the winding up of the  
2           FDIC receivership. So in either regard, WMB is not going to be  
3           a member of the tax group long term, and because of that, we  
4           have an opportunity here to, in a sense, control the timing of  
5           the worthless stock loss associated with the stock of WMB.

6           Q. So can you just explain what the tax benefit is of  
7           abandoning the investment in WMB prior to a July 31st or August  
8           31st effective date?

9           A. Right. Taking into account an August 31st effective date,  
10          the benefit associated with abandoning prior to that date, is  
11          that you would trigger the worthless stock loss. There are  
12          unique rules under 382 which provide that to the extent a  
13          taxpayer experiences an ownership change and in the same year,  
14          incurs a loss, these rules allow the taxpayer to allocate a  
15          portion of the loss to the pre-change period and a portion of  
16          the loss, more importantly, to the post-change period.

17          The portion of the changer in NOL that is allocated to the  
18          post-change period is not subject to the 382 limitation. So,  
19          for example, here, the portion of the loss allocated to the  
20          period after August 31st would not be subject to the August  
21          31st 382 limitation.

22          Q. Okay. Now, would that -- well, the stock loss, would that  
23          loss be subject to any provisions of the tax code that might  
24          limit it? I think you started to explain.

25          A. Well, certainly, you know, the stock loss would be subject

1 to continuing testing under 382. It could be potentially be  
2 subject to 269 and 384, Section 384 could possibly be a  
3 consideration as well.

4 Q. Now, before taking into account of any adjustments,  
5 approximately what amount of net operating losses would result  
6 from taking the worthless stock deduction?

7 A. We have calculated the amount of the worthless stock loss  
8 deduction to be at least 5.4 billion dollars.

9 Q. Okay. And what would be the impact, if any, of current  
10 year activity on the amount of available NOLs?

11 A. We are projecting current year activity to yield a gross  
12 loss of approximately 1.1 billion dollars. That amount would  
13 be reduced by the projected amount of cancellation of  
14 indebtedness income, which is approximately five hundred  
15 million dollars. That would yield a net loss of approximately  
16 six hundred million dollars.

17 That six hundred million dollars would be in addition to  
18 5.4 billion dollar worthless stock loss. So we're projecting  
19 in the aggregate a six billion dollar loss for the current  
20 year.

21 Q. Okay. And what would be the impact, if any, of any  
22 capital contributions deemed to occur under the global  
23 settlement agreement on the amount of available and net  
24 operating losses?

25 A. The global settlement agreement provides that certain

1 payments to JPMorgan Chase and to the FDIC shall be treated as  
2 capital contributions to WMB. If that were to be respected, it  
3 would increase the stock basis of WMB. That increased stock  
4 basis would translate to a larger worthless stock loss  
5 deduction.

6 Q. Okay. Now, just to be clear, what actions, if any, have  
7 the debtors taken to abandon the stock of WMB?

8 A. The debtors have filed a motion with the Court seeking  
9 approval to abandon the stock of WMB prior to the effective  
10 date to take advantage of the allocation ruled under 382.

11 Q. Okay. Now, you mentioned adjustments being made to the  
12 current year net operating loss, inclusive of the stock loss  
13 carry forward under 382 and 269. Generally, how does 382,  
14 Section 382 effect the ability to utilize the current year NOL?

15 A. Well, Section 382 to the extent an ownership change occurs  
16 would limit a taxpayer's ability to use the pre-change NOLs to  
17 offset post change taxable income.

18 Q. Okay. And which portion of the current year net operating  
19 loss would be subject to the Section 382 limitation?

20 A. It is the portion of the -- it's the pre-change portion of  
21 the changer NOL.

22 Q. And did you prepare a demonstrative showing the  
23 calculations of the limited versus the non-limited portions of  
24 the net operating loss?

25 A. I have.

1 Q. If I could have you take a look at Demonstrative 2  
2 entitled Calculation of Limited and Non-limited Portions of NOL  
3 Pursuant to Section 382. Is that the demonstrative that you  
4 had prepared?

5 A. Yes, it is.

6 Q. Okay. Now, if you take a look at the demonstrative, what  
7 is reflected by the blue and green bar graph on the top?

8 A. The bar graph reflects the allocation of the number of  
9 days between the pre-and-post change period taking into account  
10 an August 31st effective date and change date.

11 So if you were to look at the blue section of the graph,  
12 it shows 243 days. So under the general proration rule in  
13 Section 382, it provides that 243 days are allocated to the  
14 post-change period.

15 On the flip side, the green section of the bar graph shows  
16 the 122 days allocated to the post change period.

17 Q. Okay. And if you look at the box on the left-hand side of  
18 the demonstrative entitled limited portion of NOL, can you  
19 describe how you calculate the limited portion of the stock  
20 loss carry forward?

21 A. Certainly. The rule in 382 is the general proration rule.  
22 So if you were to look at line one, you take the number of days  
23 allocated to the pre-change period. So here it's 243. You  
24 divide that by the total number of days in the tax year. Here  
25 it's 365. That yields a percentage, here it's 66.6 percent.

1           You multiply that percentage by the stock loss, you also  
2 multiply that by the amount of other activity, which is  
3 approximately six hundred million dollars. That yields an  
4 aggregate number of approximately four billion dollars. So  
5 what that means is, you have a current year NOL of six billion  
6 dollars. Of that six billion dollars under the general  
7 proration rule, four billion of it will be allocated to the  
8 pre-change period, and subject to the August 31st 382  
9 limitation.

10           The final line shows that limitation to be seven million  
11 dollars a year. So that means that the tax group would have  
12 access to that four billion dollar pool of limited NOLs at a  
13 rate of seven million dollars per year.

14 Q.   Okay. And if you look at the box on the right-hand side  
15 of the demonstrative, how do you calculate the non-limited  
16 portion of the NOL?

17 A.   It's the mirror calculation. You take the number of days  
18 allocated to the post-change period. Looking at line number  
19 one, that's 122 days. Again, you divide that by the total  
20 number of days in the tax year to get a percentage. That  
21 percentage 33.4 percent is multiplied by the stock loss, as  
22 well as the other activity during the current year, and that  
23 yields an aggregate number of approximately two billion  
24 dollars.

25           So that means that the tax group would have two billion

1 dollars of unlimited or non-limited NOLs, based on the  
2 proration rule.

3 Q. Okay. So in total, how much of the estimated six billion  
4 dollar current year NOL would be available to reorganize WMI  
5 based on these two pieces of the chart?

6 A. The tax group would have essentially two layers of NOL.  
7 First it would have the two billion dollars of NOL that's  
8 allocated to the post-change period, and is not subject to the  
9 August 31st 382 limitation.

10 It would also have access to the four billion limited pool  
11 of NOLs at a rate of seven million dollars per year.

12 Q. Okay. Now, does Section 382 place any other limitations  
13 on reorganized WMI's ability to use 2011 NOLs?

14 A. It does; 382 has a provision that essentially provides  
15 that the taxpayer must continue its historic business for the  
16 two-year period after an ownership change, otherwise, it loses  
17 its ability to access those pre-change NOLs.

18 And, of course, the tax group would continue to be subject  
19 to the testing regime under Section 382, and there could  
20 possibly be a future ownership change, which would create an  
21 additional 382 limitation.

22 Q. Okay. And so that could be the effect of a subsequent  
23 ownership change, right?

24 A. Certainly. The effect of a subsequent ownership change  
25 would mean that the entire lot of NOLs would be separate to an

1 additional 382 limitation, and the amount of that limitation  
2 would be calculated on the equity value and appropriate rate at  
3 that time.

4 Q. And have you read the report prepared by the equity  
5 committee's tax counsel, Mr. Anderson?

6 MR. SARGENT: Your Honor, I'm going to object. His  
7 testimony is getting into areas that expert's testimony, has to  
8 do with how the NOL might be --

9 THE COURT: I can't hear you. I can't hear you.

10 MR. SARGENT: I'm sorry. I'm going to object. This  
11 area of testimony is getting into a subject that's going to be  
12 addressed by the experts. He's discussing how and whether the  
13 NOL can be exploited by the reorganized debtor after it  
14 emerges. It's not a subject for a fact witness, it's not  
15 something that he's got any basis to testify about.

16 MR. MASTANDO: Your Honor, he's the tax manager at  
17 WMI. He's certainly capable of talking about his understanding  
18 of these issues and how he sees them potentially going forward.

19 THE COURT: Is he being proffered as an expert?

20 MR. MASTANDO: No. But he's doing the calculation --

21 THE COURT: Well, I don't know that --

22 MR. MASTANDO: -- that he -- these are the --

23 THE COURT: I don't think he can opine on another  
24 expert's report then.

25 MR. MASTANDO: He can -- I think he can comment on his

1 understanding of the expert's calculation as they relate to  
2 this.

3 THE COURT: Well, why is that relevant? Why would I  
4 care? I assume the expert's going to tell me what that  
5 calculation is.

6 MR. MASTANDO: Okay.

7 BY MR. MASTANDO:

8 Q. Mr. Carreon, you mentioned other limitations on the  
9 ability of reorganized WMI to use the current year NOL, such as  
10 Section 269 of the Code. What limitations could apply under  
11 Section 269 as far as you understand?

12 MR. SARGENT: Your Honor, it's the same issue. He's  
13 talking about limitations on the use of the NOL by the future  
14 reorganized WMI. It's not a subject for fact testimony.

15 MR. MASTANDO: No, he -- no, Your Honor. He's the tax  
16 manager at WMI, who's testifying as to his understanding of  
17 what Section 269 is in connection with his role.

18 THE COURT: But that's not a fact.

19 MR. MASTANDO: It's factual from the perspective of  
20 what his understanding is in his role as the tax manager at  
21 WMI.

22 THE COURT: I disagree. I think that he has told us  
23 what the facts are, and as far as what the NOLs are applying  
24 the rules.

25 MR. MASTANDO: I don't think there's a prohibition on



1 a fact witness testifying as to his understanding of tax issues  
2 that he deals with in his everyday position. We're not  
3 offering him as an expert, but he's --

4 THE COURT: What is the question again?

5 MR. MASTANDO: What his understanding is of  
6 limitations that Section 269 imposes.

7 THE COURT: All right. I will allow it.

8 THE WITNESS: Section 269 generally provides that to  
9 the extent control is acquired directly or indirectly, where  
10 the principal purpose is tax avoidance, then the taxpayer's use  
11 of those NOLs, underlying NOLs are disallowed.

12 BY MR. MASTANDO:

13 Q. Okay. And will -- is it your understanding that  
14 consummation of the plan here will cause an acquisition of  
15 control for the purpose of Section 269?

16 A. I believe that to be the case.

17 Q. Okay. And what is your understanding of the factors that  
18 are considered in determining the principal purpose of an  
19 acquisition?

20 A. Well, the application of Section 269 is based on facts and  
21 circumstances, and --

22 MR. SARGENT: You can complete the answer, but I have  
23 an objection after you're done.

24 THE WITNESS: Okay. It's based on facts and  
25 circumstances, so it's highly subjective, and obviously there's

1 no bright line test. Things that are generally considered are  
2 the existence of management or employees, a business plan, the  
3 relative value of the taxed assets in relation to the non-tax  
4 assets, the composition of the parties acquiring control, and  
5 perhaps even subsequent actions by those parties.

6 MR. SARGENT: Okay. Your Honor, again, we're going to  
7 move to strike that answer and this line of testimony. This is  
8 exactly the subject that's being debated between two experts in  
9 this case, which is what are the limitations --

10 THE COURT: Well, I'll sustain it and strike the  
11 testimony.

12 BY MR. MASTANDO:

13 Q. Okay. Mr. Carreon, do you have any understanding of the  
14 potential consequence if the IRS were to find that the  
15 principal purpose of acquiring control was to obtain use of  
16 NOLs?

17 A. Ultimately if the IRS determines that Section 269 applies,  
18 then the taxpayer does not have use of the underlying NOLs.

19 MR. MASTANDO: Okay. Thank you, Mr. Carreon, nothing  
20 further.

21 THE COURT: Any cross?

22 CROSS-EXAMINATION

23 BY MR. SARGENT:

24 Q. Good morning, Mr. Carreon. Edgar Sargent, Sussman &  
25 Godfrey on behalf of the equity committee. I do just have a

1 couple of follow-up questions.

2 Mr. Mastando asked you if the assets of the estate are  
3 going to be sufficient to satisfy the claims of the peers in  
4 full, and you testified no, they would not. Do you recall that  
5 testimony?

6 A. I do recall that testimony.

7 Q. And you -- I just want to make it clear, you're testifying  
8 under the terms of the plan as proposed by the debtor, correct?

9 A. Right and under the terms of the plan.

10 Q. And you're assuming that the value of the reorganized  
11 debtor is the value that's assigned in the plan, correct?

12 A. I'm not sure I fully understand what you're asking me.

13 Q. When you conclude that the value being distributed by the  
14 estate is not going to be sufficient to satisfy the claims of  
15 the peers in full, that conclusion is based on the assumption  
16 that the value placed on Wimrick by the debtor's expert is  
17 correct; is it not?

18 A. Yes; I'm taking into consideration the 160 million dollar  
19 value placed on the reorganized WMI.

20 Q. And you're also assuming that as the debtor has proposed,  
21 interest will be paid out at the contract rate for post-  
22 petition interest, not federal judgment rate, correct?

23 A. No. I think under either circumstance that's the case.

24 Q. Your testimony is that under federal judgment rate  
25 interest, the assets of the estate will not be sufficient to

1 satisfy the claims of the peers in full?

2 A. I believe that's my understanding, yes.

3 Q. You testified some about the creation of this NOL. I just  
4 want to make it clear that you're not testifying about the  
5 reorganized debtor's ability to use that NOL in the future; is  
6 that correct?

7 A. No, I am not.

8 MR. MASTANDO: Objection, Your Honor, his testimony  
9 is --

10 THE COURT: Overruled. He answered.

11 THE WITNESS: Could you ask your -- repeat your  
12 question again, please?

13 BY MR. SARGENT:

14 Q. You're not testifying about the reorganized debtor's  
15 ability to use the NOL that you quantify, are you?

16 A. You mean with regard to the worthless stock loss and the  
17 resulting NOL?

18 Q. The resulting NOL and the reorganized debtor's ability to  
19 use that NOL in the future after it emerges from  
20 reorganization. You're not testifying about that.

21 MR. MASTANDO: Objection, Your Honor.

22 THE COURT: Overrule.

23 THE WITNESS: Well, I'm testifying that the trash (ph)  
24 group's ability to have access to the 17.7 billion dollars will  
25 go away once WMB ceases to be a member of the group. And that

1 that if the stock of WMB is abandoned prior to the effective  
2 date, that that will give rise to a worthless stock loss, and  
3 that will ultimately be prorated between a pre-and-post change  
4 period.

5 BY MR. SARGENT:

6 Q. And that will lead to a, I believe you testified,  
7 approximately two billion dollar NOL, that will reside in the  
8 reorganized debtor; isn't that correct?

9 A. Correct.

10 Q. But you're not testifying about the reorganized debtor's  
11 ability to use that two billion dollar NOL after it emerges,  
12 are you?

13 A. I have no idea how the reorganized WMI's going to use that  
14 two billion dollars. What I've testified to is that it would  
15 continue to be subject to the testing regime under Section 382.

16 Q. And you're not testifying about whether or not they're  
17 going to be able to use that NOL, are you?

18 A. The ability to use an NOL is -- has many different factors  
19 into it. So it's -- part of them are taxed, part of them are  
20 non-tax. I have no idea what the reorganized WMI is going to  
21 do with that NOL.

22 Q. And those factors are not part of your testimony, are  
23 they?

24 A. I'm not testifying to the business factors associated with  
25 the future use of the NOL.

1 Q. You're not testifying about the value of that NOL as it's  
2 going to reside in the reorganized debtor, are you?

3 MR. MASTANDO: Objection, Your Honor, he's testified  
4 as to amount.

5 THE COURT: Overrule.

6 THE WITNESS: I'm not a valuation expert, so I don't  
7 know what the economic value of that NOL would be. I'm  
8 testifying that at two billion dollars, assuming an effective  
9 date of August 31st and an abandonment before that date, that  
10 two billion dollars of the NOL would be allocated to the post  
11 change period.

12 BY MR. SARGENT:

13 Q. Well, let me just ask you. I mean, is it your testimony  
14 that this NOL will be worth two billion dollars in the hands of  
15 the owners of the reorganized WMI, is that your testimony?

16 A. No. Again, just to be clear, the ability to use an NOL is  
17 a fact that has many tax and non-tax factors. Certainly a  
18 subsequent ownership change could be a factor of the ability to  
19 generate taxable factors. I'm --

20 THE COURT: Please slow down.

21 THE REPORTER: Yeah.

22 THE WITNESS: Okay.

23 THE REPORTER: If you could please go back to non-tax  
24 factors, certainly a subsequent ownership change can be --

25 THE WITNESS: Obviously, a subsequent ownership change

1 can affect the ability to use an NOL, the ability to generate  
2 taxable income affects the ability to use the NOL. I'm  
3 testifying that if we abandon the stock of WMB prior to the  
4 August 31st effective date, then two billion of that under the  
5 382 apportionment rules will be allocated to the post-change  
6 period.

7 BY MR. SARGENT:

8 Q. And you're not testifying about what the value of that two  
9 billion dollar NOL will be in the hands of the reorganized WMI,  
10 I just want to make sure that I nail that down. That's  
11 correct, isn't it?

12 A. I can have no idea what the value of the NOL is in the  
13 hands of --

14 MR. SARGENT: That's all I have. Thank you. Thank  
15 you, Your Honor.

16 CROSS-EXAMINATION

17 BY MR. STEINBERG:

18 Q. Good morning, Mr. Carreon. I'm Arthur Steinberg. I  
19 represent the litigation and tracking warrant holders. I just  
20 had a few questions based on your testimony.

21 At some point in your testimony you rattled off numbers,  
22 and I just wanted to make sure I understood what those numbers  
23 were.

24 You said that the seniors would have twenty-four million  
25 shares, the senior subordinated would have thirteen million

1 shares, and the peers would have 123 million shares, and I  
2 think it was of the reorganized entity based on the stock  
3 election; is that correct?

4 A. Yes. That's my understanding of the stock elections.

5 Q. And those numbers add up to 160 million dollars, and is  
6 that because the debtor has put a value on the reorganized  
7 entity of 160 million dollars?

8 A. My understanding is that each share is worth a dollar.

9 Q. So what happened to the Class 21 shares that the  
10 shareholders elected, were they so small that they didn't even  
11 hit one percent?

12 A. I don't know what Class 21 shares -- I'm unaware of that.

13 Q. Litigation tracking warrant holders have the ability to  
14 make a stock election, some of them made a stock election --

15 A. Uh-huh.

16 Q. -- but you didn't give me a number for them.

17 MR. MASTANDO: Objection, Your Honor, Counsel's  
18 testifying and it's beyond the scope of his direct.

19 THE COURT: Overrule.

20 THE WITNESS: I'm sorry, sir, I do not know the  
21 results for that particular class.

22 BY MR. STEINBERG:

23 Q. If the value of the reorganized entity was, let's say, 200  
24 million dollars instead of 160 million dollars, would the  
25 numbers that you have given me adjust to reflect the fact that



1 the Court found that the reorganized entity had a greater  
2 value, and therefore people who made the election had to give  
3 up more of the value of their claim?

4 A. Well, I'm not sure I entirely understand the scope of your  
5 question, but I will say that if the value of reorganized WMI  
6 changes, then that would affect the 382 limitation.

7 Q. Yeah. But I was asking you if the value of the  
8 reorganized entity was 200 million dollars instead of 160,  
9 would the seniors still twenty-four million shares, or would  
10 they have more shares than that to reflect the change in value  
11 of the reorganized entity?

12 A. I'm unsure how a change in value would affect the election  
13 results.

14 Q. The election was a dollar per share of value?

15 A. That's my understanding.

16 Q. And you just don't know whether if the reorganized entity  
17 had a greater value that the shares would have to increase and  
18 the creditor give up on their claim would have to increase to  
19 reflect that?

20 A. I didn't perform the valuation analysis.

21 Q. Now, you said the peers had 123 million shares. Is that  
22 before subordination or after subordination?

23 A. I believe that is -- I'm unsure to be honest with you.

24 Q. Okay. And what happens if the peers did not have a 123  
25 million of value under the plan to buy these shares? How does

1 the plan account for that?

2 A. If the peers --

3 Q. If the peers' distribution is less than 123 million  
4 dollars, how would this whole thing work itself through?

5 A. I'm not entirely sure how -- what the consequence -- how  
6 it would affect the ultimate recoveries of the various classes  
7 to the extent that would be the case.

8 Q. Do you know what the aggregate amount of unresolved  
9 unsecured claims in this case is?

10 A. I do not know. I believe part of that is influx, but I do  
11 not know its exact number.

12 Q. Okay. I think the liquidation analysis had a number like  
13 fifty-five billion of still unresolved claims. Do you know  
14 whether that's a good number or a bad number?

15 A. I have no idea. I wasn't personally involved in the  
16 liquidation analysis.

17 Q. Okay. Do you know under the plan what is projected that  
18 the peers would get, assuming contractual subordination and  
19 assuming a contract rate of interest?

20 A. I don't know the exact number off the top of my head. I  
21 know it's less than their full amount.

22 Q. Do you know what the impact of the peers' distribution  
23 would be the litigation tracking warrant holders had an allowed  
24 claim of 337 million dollars?

25 A. I don't know the impact of that.

1 MR. STEINBERG: Okay. Nothing further.

2 THE COURT: Any re -- any further cross? I'm sorry.

3 MS. HAPER: Your Honor. I'm Bettina Haper, I'm a pro  
4 se objector.

5 CROSS-EXAMINATION

6 BY MS. HAPER:

7 Q. I just want to clear something up, I had a question about  
8 one piece of your testimony.

9 Mr. Carreon, did -- was it your testimony that a  
10 certification of no objection was filed on the motion to  
11 abandon the stock property?

12 A. I don't believe I testified to that.

13 Q. Okay. And what was your testimony to that?

14 A. I testified that there was a motion before the Court to  
15 abandon the stock of WMB prior to the effective date.

16 Q. Okay. So there is, in fact, no certification --

17 A. I have no idea --

18 Q. -- that you're aware of?

19 A. -- if that is the case.

20 Q. Okay.

21 MS. HAPER: All right. Thank you.

22 THE COURT: Any redirect?

23 MR. MASTANDO: Nothing further, Your Honor.

24 THE COURT: You may step down. How long will the  
25 direct on -- I'm sorry. Are you stepping up to say something?

1 MR. SARGENT: Your Honor, I'm sorry, this is Edgar  
2 Sargent from Sussman Godfrey on behalf of the equity committee.  
3 This is my colleague, Dan Walker, come up from the Seattle  
4 office. He's going to be handling the next witness.

5 THE COURT: All right. How long will direct of this  
6 witness be?

7 MR. WALKER: I think, Your Honor, no more than fifteen  
8 minutes.

9 THE COURT: All right. Let's proceed then. Thank  
10 you.

11 MR. MASTANDO: Your Honor, may Mr. Carreon be excused  
12 from the trial?

13 THE COURT: Any objection?  
14 He may.

15 MR. MASTANDO: Thank you, Your Honor.

16 MR. WALKER: Your Honor, the equity committee would  
17 like to call Kevin Anderson as its witness.

18 THE COURT: You may step up and be sworn by the clerk.

19 THE CLERK: Raise your right hand, please.

20 KEVIN ANDERSON, WITNESS, SWORN

21 THE CLERK: Be seated. Please state your name,  
22 spelling your last name.

23 THE WITNESS: My name is Kevin D. Anderson. And it's,  
24 last name is spelled A-n-d-e-r-s-o-n.

25 DIRECT EXAMINATION

1 BY MR. WALKER:

2 Q. Good morning, Mr. Anderson.

3 A. Good morning.

4 Q. Can you please tell the Court what you do for a living?

5 A. Yes. I am a partner in the national tax services practice  
6 of BDO USA LLP.

7 Q. And can you explain briefly what BDO USA LLP is?

8 A. It is a national accounting tax and consulting firm.

9 Q. And generally speaking, what do you do in your tax  
10 consulting practice at BDO?

11 A. In my tax consulting practice, I work on a variety of  
12 specialized tax matters that are generally above the capacity  
13 of the local practice offices to handle. I specialize in  
14 corporate tax consolidated returns, mergers and acquisitions,  
15 troubled company workouts and a variety of other related  
16 matters.

17 MR. WALKER: I would like to have the witness please  
18 direct his attention to Debtor's Exhibit 367. Is that  
19 available to him?

20 THE COURT: The debtor can pull up 367. Do you know  
21 what volume it's in?

22 Q. While we're waiting for you to get that, could you just  
23 please describe your relevant educational background for the  
24 Court?

25 THE COURT: Does the debtor have -- want to tell me in

1 what volume that exhibit is?

2 MR. WALKER: Your Honor, may I hand this to Mr.  
3 Anderson?

4 THE COURT: You may.

5 MR. MASTANDO: I believe Volume 8 of 13, Your Honor.

6 THE COURT: All right. I have it.

7 BY MR. WALKER:

8 Q. Mr. Anderson, can you identify what that exhibit is in  
9 front of you?

10 A. The exhibit is the expert report that I submitted, that  
11 the equity committee submitted it, and it is dated May 2, 2011.

12 Q. And did you write that expert report?

13 A. Yes, I did.

14 Q. And is that a true and correct copy of your expert report?

15 A. It appears to be, yes.

16 MR. WALKER: Your Honor, we'd like to move to admit  
17 that expert report into evidence.

18 MR. MASTANDO: Well, Your Honor, I'm going to object.  
19 I don't think he's been qualified as an expert, and I believe  
20 the report is hearsay unless counsel is going to agree that all  
21 expert reports come in.

22 THE COURT: Do you want --

23 MR. MASTANDO: Subject to his being qualified as well.

24 THE COURT: -- to do more on qualification before voir  
25 dire?

1 MR. WALKER: I'm sorry, could you --

2 THE COURT: Do you want to do more to qualify your  
3 witness before they voir dire?

4 MR. WALKER: Sure, I can do that.

5 BY MR. WALKER:

6 Q. Mr. Anderson, can you please describe for the Court your  
7 professional experience in tax consulting prior to your work at  
8 BDO?

9 A. Yes. But I may also say that there was an unanswered  
10 question about educational experience as well.

11 Q. Okay. Could you please describe your educational  
12 experience?

13 A. Yes. I have an accounting degree as an undergraduate from  
14 the University of Wisconsin at Whitewater. And I also have a  
15 law degree from the University of Michigan.

16 Q. Thank you.

17 Can you please also describe for the Court your  
18 professional experience in tax consulting prior to your work at  
19 BDO?

20 A. In chronological order from the oldest to the most recent,  
21 I graduated from law school in 1981, and at that time, I joined  
22 the Milwaukee law firm of Foley & Lardner. I was an associate  
23 first, and then a partner, and remained at that firm in its tax  
24 practice until 1995.

25 In 1995, I joined the Department of Treasury's office of

1 tax legislative counsel in Washington, D.C. where I was an  
2 attorney advisor first, and then an associate tax legislative  
3 counsel. In that role, I was working as an advisor to the  
4 assistant secretary for tax policy, working closely with the  
5 Internal Revenue Service, and also working closely with Capitol  
6 Hill legislative staffs on tax legislative matters, and on  
7 published guidance; regulations, rulings, and the like.

8 Beginning in 1999, I was a partner at Deloitte tax, in its  
9 national tax practice, national tax office, excuse me, in  
10 Washington. And I remained there until late 2006. And in that  
11 role, I was advising practice offices throughout the country on  
12 a variety of corporate tax matters, including Section 382,  
13 consolidated return matters, troubled company reorganizations,  
14 and mergers and acquisitions.

15 Then I remained there until 2006. And in early 2007, I  
16 joined BDO.

17 Q. And have you had any teaching positions related to tax --

18 A. Yes. I did serve for several years as an adjunct  
19 professor in the Georgetown University Law School LLM program  
20 in Washington.

21 Q. And in your professional experience and in your teaching  
22 experience, have you had occasion to consider the application  
23 of Sections 382 and 269 of the Internal Revenue Code?

24 A. Yes. I've been working on Section 382 issues extensively  
25 for the last decade, and Section 269 is just something to



1 consider in virtually every acquisition, so I've been thinking  
2 about Section 269 for probably thirty years.

3 Q. Okay. And, Mr. Anderson, what about Sections 383 and 384  
4 of the Internal Revenue Code?

5 A. Sections 383 and 384 are closely related to Section 382,  
6 and so they're really part and parcel of the consequences of  
7 ownership changes involving corporations with unused tax  
8 attributes.

9 Q. And are you a member of any relevant professional  
10 organizations?

11 A. Yes. I have been actively involved in the American Bar  
12 Association, Section of Taxation for more than twenty years.  
13 I'm currently serving -- I'm the counsel of the tax section  
14 which is essentially its board of directors.

15 I'm also currently a member of the Internal Revenue  
16 Service Advisory Council, and I'm also an active member of an  
17 organization within the American Institute of CPAs, the S  
18 Corporations Technical Resource Panel.

19 MR. WALKER: Okay. Your Honor, I'd like to move for  
20 admission of Debtor's Exhibit that I just handed up to the  
21 witness, is it 367?

22 THE COURT: Let me -- is there any voir dire?

23 MR. MASTANDO: Yes, Your Honor. May I please?

24 THE COURT: You may.

25 VOIR DIRE EXAMINATION

1 BY MR. MASTANDO:

2 Q. Good morning, Mr. Anderson.

3 A. Good morning.

4 Q. John Mastando from Weil Gotshal on behalf of the debtors.

5 We met a few weeks ago at your deposition.

6 You testified that you began your career at Foley &

7 Lardner, correct?

8 A. After law school, that is correct.

9 Q. Okay. And at Foley & Lardner, Section 269 issues were  
10 never front and center in the cases or matters you were working  
11 on; is that correct?

12 A. Always considered, never front and center.

13 Q. Okay. And after Foley & Lardner, you became an attorney  
14 adviser at the Department of Treasury in Washington I believe  
15 you testified, right?

16 A. That is correct.

17 Q. And you did not deal with any Section 269 issues at the  
18 Department of Treasury; isn't that correct?

19 A. That is correct. We work on matters that are on the  
20 guidance plan for Treasury.

21 Q. Okay. And you did not work on any guidance projects under  
22 Section 269 during your employment at Treasury; isn't that  
23 correct?

24 A. That is correct.

25 Q. Okay. And then you made a brief return to Foley & Lardner

1 after Treasury, right?

2 A. That is correct.

3 Q. And again, Section 269 issues were never front and center  
4 in the cases you dealt with at Foley & Lardner; isn't that  
5 correct?

6 A. Always a consideration, but never front and center.

7 Q. Okay. And in 1998, you became a member of the tax  
8 practice at Deloitte, right?

9 A. That is correct.

10 Q. And you started as part of the accounting methods and  
11 periods group I believe you testified at your deposition?

12 A. That is correct.

13 Q. And eventually you moved to the corporate tax group,  
14 correct?

15 A. Correct.

16 Q. The corporate tax group was responsible for Sections 301  
17 through 385, as well as Section 108 of the Code, correct?

18 A. That's not a complete analysis of what we were responsible  
19 for. We were responsible for all matters that dealt with  
20 corporate taxation, with restructurings and working out  
21 insolvency cases.

22 Q. And the area -- your area of practice at Deloitte was  
23 Section 283 practice; isn't that right?

24 A. I think there's an --

25 Q. I'm sorry, I'm sorry, your area of expertise at Deloitte

1 was Section 382 practice, correct?

2 A. 382 not 283.

3 Q. Right. 382, correct?

4 A. Yes.

5 Q. And Section 269 issues were not front in center in the  
6 matters you worked on at Deloitte; isn't that correct?

7 A. Always considered, never front and center.

8 Q. Well, let me show you your deposition transcript. Do you  
9 recall being deposed in my offices a few weeks ago?

10 A. Yes, I do.

11 Q. And if I could --

12 MR. MASTANDO: Your Honor, may we approach with a copy  
13 of the transcript?

14 THE COURT: You may.

15 Q. If I could direct you to page 33 of your transcript, line  
16 6:

17 "Q. And so in your -- in the matters that you worked on  
18 at Deloitte, Section 269 issues were not front and center; is  
19 that correct?

20 "A. That's correct."

21 Did I read that correctly, Mr. Anderson?

22 A. That is correct.

23 Q. And at Deloitte did you deal with any clients that were in  
24 restructurings?

25 A. Yes, I did.

1 Q. Okay. And you can't tell us what clients because that's  
2 confidential, correct?

3 A. That is correct.

4 Q. Okay. And after Deloitte you joined BDO, right?

5 A. Yes.

6 Q. Okay. And Section 269 issues have also not been front and  
7 center in any of the matters you've worked on at BDO; isn't  
8 that correct?

9 A. Always considered, never front and center.

10 Q. Okay. Well, let me show you your deposition again. If  
11 you could look at page 41 of your deposition, starting on line  
12 6, question was:

13 "Q. Has it been front and center in any of the matters  
14 you've dealt with at BDO, the Section 269 issues?

15 "A. No, it has not."

16 Did I read that correctly, Mr. Anderson?

17 A. Yes.

18 Q. Okay. Now, you consider your relevant experience with  
19 Section 269 issues to be your judgment as a professional; is  
20 that right?

21 A. Yes.

22 Q. Okay. And while you were at Foley & Lardner and at  
23 Deloitte you had occasion to research case law under Section  
24 269 about once a year; isn't that right?

25 A. That was my testimony, yes.

1 Q. Okay. And at BDO, you similarly researched case law under  
2 Section 269 approximately once a year; is that correct?

3 A. That is correct.

4 Q. And you've never been involved in a dispute with the IRS  
5 over the application of Section 269, correct?

6 A. That is correct.

7 Q. Okay. And other than advice you've applied to any  
8 particular client, you've never done any study analysis or  
9 report on the general applicability of Section 269; isn't that  
10 correct?

11 A. We have provided tax analyses to clients on the  
12 consequences of their transaction, and in -- whether we're  
13 giving tax opinions or extensive written tax advice those  
14 documents will from time to time include an identification of  
15 Section 269 as a possible risk, but in every case that I'm  
16 familiar with, we'll also conclude that Section 269 does not  
17 apply.

18 Q. Well, that wasn't my question, Mr. Anderson.

19 Other than any advice you've given to a particular client,  
20 you've never done any study, analysis, or report on the general  
21 applicability of Section 269; isn't that correct?

22 A. If your question is directed toward academic studies or  
23 other such things not involved in client service, the answer is  
24 no.

25 Q. And you can't share with us any advice you've given to any

1 particular client on Section 269 because that's confidential as  
2 well; isn't that correct?

3 A. That is correct.

4 Q. Okay. Do you think that because you've been thinking  
5 about Section 269 for thirty years that that makes you an  
6 expert in it?

7 A. I have been offered up as a tax expert on the overall  
8 consequences of the proposed plan of reorganization, and  
9 Section 269 is simply one of those considerations.

10 Q. Okay.

11 MR. MASTANDO: Your Honor, we object to the offer of  
12 Mr. Anderson as an expert on Section 269.

13 THE COURT: I'm going to overrule and accept him as an  
14 expert on the tax consequences of 28 -- excuse me, 382 and 269.

15 MR. WALKER: Thank you, Your Honor. And while we're  
16 at it, just to get it out of the way, I'd like to hand the  
17 witness exhibit -- Debtor's Exhibits 368 and 369. Have those  
18 Already been --

19 THE COURT: Give me the numbers again.

20 MR. WALKER: 368 and 369.

21 THE COURT: All right. I have them.

22 UNIDENTIFIED SPEAKER: Same binder, Your Honor.

23 THE COURT: I have them.

24 DIRECT EXAMINATION, CONTD.

25 BY MR. WALKER:

1 Q. And, Mr. Anderson, do you have copies of those in front of  
2 you?

3 A. No, I do not.

4 Q. Mr. Anderson, do you recognize Exhibit 368?

5 A. Yes, I do.

6 Q. What is Exhibit 368?

7 A. Exhibit 368 is a supplemental expert report that I  
8 prepared and dated June 23, 2011.

9 Q. And did you write that report?

10 A. Yes, I did.

11 Q. And is that a true and correct copy of that report?

12 A. Yes, it is.

13 Q. And Exhibit 369, could you please explain what that is?

14 A. That is a second supplemental expert report that I  
15 prepared dated June 30, 2011.

16 Q. And did you write that report?

17 A. Yes, I did.

18 Q. And is that a true and correct copy of your report?

19 A. Yes, it is.

20 MR. WALKER: Okay. Your Honor, I'd like to move for  
21 admission of those two reports as well, please.

22 THE COURT: All right. And just for the record, the  
23 prior report is also admitted.

24 (Debtors Exhibit 367, Kevin Anderson's Expert Report dated  
25 5/2/2011, was hereby received into evidence)



1 (Debtors Exhibit 368, Supplemental Report dated 6/23/2011, was  
2 hereby received into evidence)

3 (Debtors Exhibit 369, Second Supplemental Report dated  
4 6/30/2011, was hereby received into evidence)

5 MR. MASTANDO: Just note my same objections, Your  
6 Honor.

7 THE COURT: Yes.

8 MR. MASTANDO: Thank you.

9 BY MR. WALKER:

10 Q. While we're on it, Mr. Anderson, can you explain what you  
11 meant when you said in your thirty years of tax consulting that  
12 269 issues were always considered even if not front and center?

13 A. Yes. Section 269 is a provision that is almost seventy  
14 years old in the Internal Revenue Code, and it was originally  
15 enacted for the purpose of preventing trafficking in net  
16 operating losses and other tax attributes.

17 Within the last twenty-five years, in particular, the  
18 Internal Revenue Service now has more specific statutory tools  
19 to prevent such trafficking, and as a consequence, Section 269  
20 has taken a much more limited role in ascertaining the extent  
21 to which tax attributes may be used in any given transaction.

22 Q. And are you familiar with any test that the IRS would  
23 apply in applying Section 269 generally speaking?

24 A. Well, first of all, Section 269 applies to two different  
25 types of acquisitions, and in either case, it applies only in

1 the circumstances where the so-called principal purpose test is  
2 satisfied. That is a principal -- that is that there must be  
3 the principal purpose for the acquisition to secure the  
4 benefits of a loss, or deduction, or other allowance, and the  
5 principal purpose is evasion or avoidance through that means.

6 And so, yes, there are factors that the Internal Revenue  
7 Service has applied through the years and the courts have  
8 applied through the years as well.

9 Q. And without getting into them right now, we'll get into  
10 them later, are you familiar with those factors?

11 A. Yes, I am.

12 Q. And in your thirty years of providing tax advice to  
13 clients, have you had opportunity to apply those factors to any  
14 of the transactions you've offered advice on?

15 A. Yes, I have applied them.

16 Q. And is that what you meant when you said it is always  
17 considered?

18 A. It is always considered, yes.

19 Q. And you've -- over your thirty years, have you worked on a  
20 range of transactions, or only a narrow group of type of  
21 transactions?

22 A. I worked on a wide range of transactions including taxable  
23 acquisitions of stock and assets, tax-free acquisitions, tax-  
24 free reorganizations, and reorganizations of troubled  
25 companies, both inside and outside of bankruptcy.

1 Q. And have you had a chance to apply Section 269 across the  
2 broad range of transactions during your thirty years of  
3 practice?

4 A. I've had the chance to consider the application of Section  
5 269 to those transactions, yes.

6 Q. And what I meant was, have you had a chance to apply what  
7 you understand the factors in the principal purpose test to be  
8 to the facts, in that broad range of transactions you've worked  
9 on?

10 A. Yes, I have.

11 Q. Okay. And just because you can't share with us today  
12 specifics about confidential transactions you've worked on,  
13 have you been able to take lessons from those transactions to  
14 apply them to the facts in this case?

15 MR. MASTANDO: I'm going to object, Your Honor. He  
16 testified that he can't reveal what the advice is, so I don't  
17 think he should be testifying as to the lessons he learned.

18 MR. WALKER: Your Honor, if I can respond to that.  
19 I'm not -- my -- what he testified to is he can't talk about  
20 the specific transactions that he's worked on because they're  
21 confidential.

22 In his deposition, he testified and opined on the  
23 application of Section 269, and my question was, does your  
24 understanding of the application of 269 come from any lessons  
25 you've learned in working on these confidential transactions.

1 MR. MASTANDO: His testimony was also that he couldn't  
2 testify as to what any of the advice was that he'd given on  
3 transactions. So I don't think it's appropriate to ask him  
4 what the lessons he's learned were, if you can't test the  
5 underlying advice.

6 THE COURT: I -- oh, gosh. You're asking what lessons  
7 he learned from the work he performed?

8 MR. WALKER: I was asking him, Your Honor, I think, or  
9 I was intending to ask him if he was able to apply the lessons  
10 he learned from working on those confidential transactions, you  
11 know, the research, the application of the test to the facts in  
12 those confidential transactions to the facts he's been able to  
13 learn about this case.

14 THE COURT: All right. I will allow that.

15 MR. WALKER: Thank you, Your Honor.

16 THE WITNESS: Yes. That's what every tax advisor  
17 does, is to bring to bear the collective experience and  
18 judgment that one has in looking at transactions that are  
19 similar in understanding of the underlying law.

20 BY MR. WALKER:

21 Q. Okay. And, Mr. Anderson, what is your role in this case?

22 A. My role in this case is to provide opinions as to the  
23 debtor's ability to use net operating losses, and other tax  
24 attributes, as a result of the emergence, the confirmation of  
25 the plan, and on a going forward basis.

1 Q. And briefly speaking, what is your understanding regarding  
2 the debtors' potential net operating losses?

3 A. There are two categories of net operating losses to the  
4 best of my knowledge. One is a category from pre-2011 years,  
5 and that number I've seen estimated at 17.7 billion. There's  
6 another source of a net operating loss for the calendar year  
7 2011 only, and I've seen that number estimated at six billion  
8 in some cases, 6.6 billion in other documents.

9 Q. And generally speaking, what is the significance of net  
10 operating losses to a business?

11 A. When a corporation has a net operating loss, it may carry  
12 back that net operating loss to the two preceding taxable  
13 years, and offset taxable income in those years. And to the  
14 extent that those losses are not carried back to the two  
15 preceding years, they may be carried forward for up to twenty  
16 succeeding taxable years, and offset taxable income incurred or  
17 excuse me, realized in those years. And thus, reduce or  
18 eliminate the tax liability in either the carry back years or  
19 the subsequent years.

20 Q. And in your opinion, would reorganized WMI have all of its  
21 net operating losses available for use post-emergence?

22 A. Well, they're available for use, but a substantial portion  
23 of them are going to be subject to a Section 382 limitation.

24 Q. And do you address that Section 382 limitation in any of  
25 the reports in front of you?

1 A. Yes, I do. Based upon the information that had been  
2 available to us, the pre-2011 losses would be fully subject to  
3 the Section 382 limitation, and the anticipated net operating  
4 loss for 2011 is required to be split between the so-called  
5 pre-change period and the post-change period.

6 The loss with the pre-change period will be subject to a  
7 Section 382 limitation arising out of emergence, and the post-  
8 change portion of the losses will not be subject to that same  
9 Section 382 limitation.

10 Q. And very briefly, how did you reach your conclusions  
11 regarding the limitations imposed by Section 382?

12 A. Well, I first determined that the issuance of stock to the  
13 creditors of the debtor would constitute an ownership change  
14 under Section 382, because there would be either requisite  
15 increase in their percentages of stock ownership, compared with  
16 their historic low ownership percentages.

17 Because that constitutes an ownership change, then Section  
18 382 does impose a limitation which is a factor of the value of  
19 the stock of the corporation, in this case, immediately after  
20 the emergence, and an interest rate which is currently  
21 approximately four percent.

22 Q. Do you understand that the debtors also contend that  
23 Section 269 could impose limitations on the net operating  
24 losses available to reorganized WMI?

25 A. Yes, I do.

1 Q. And did you reach any conclusions regarding the  
2 application of Section 269 of the Internal Revenue Code?

3 A. Yes, I did. I believed that Section 269 would likely not  
4 apply to an acquisition of control of some subsequent  
5 profitable operations, simply because there would be or at  
6 least there could be sufficient business purposes, and other  
7 factors present in that acquisition to prevent the application  
8 of Section 269.

9 And because the net operating losses that the debtor will  
10 have, will be to the extent of two billion or 2.2 billion not  
11 be subject to a Section 382 limitation, those losses should be  
12 fully available to offset any future profits.

13 Q. And briefly speaking, from a federal tax perspective, what  
14 would be the reason you posited for reorganized WMI acquiring  
15 another profitable business after emergence?

16 A. Well, if reorganized WMI could raise enough capital  
17 through borrowing or through stock issuances to acquire such  
18 profitable businesses, then those businesses could be operated  
19 for a long period of time without incurring any federal income  
20 tax liability.

21 Q. And can you tell me, we mentioned earlier that there is a  
22 principal purpose test you said that the IRS applies. Can you  
23 tell me briefly what the principal purpose test is?

24 A. The principal purpose test is satisfied when the principal  
25 purpose for the acquisition of control or assets is the evasion

1 of federal income taxes through securing a deduction or loss or  
2 allowance that the taxpayer could not have otherwise obtained.

3 Q. And earlier you testified that you believed that Section  
4 269 would likely not apply to reorganized WMI; is that  
5 accurate?

6 MR. MASTANDO: Objection. Objection, Your Honor.

7 THE COURT: Sustained.

8 Q. In reaching your conclusions about Section 269, did you  
9 apply the principal purpose test?

10 A. Yes, I did.

11 Q. And I should clarify. In reaching the conclusions that  
12 you're offering in this case, you -- did you reach those after  
13 applying the principal purpose?

14 A. Yes, I did.

15 Q. And briefly, can you explain what the process is of the  
16 principal purpose test, or what process you went through in  
17 applying the principal purpose test?

18 A. Yes. The principal purpose test is a facts and  
19 circumstances determination that looks at a number of factors.  
20 Again, it is the purpose for acquiring control or assets of a  
21 corporation in certain specified transactions, and in deciding  
22 whether the principal purpose test is satisfied, the Internal  
23 Revenue Service and the courts have looked at a variety of  
24 factors including whether the parties were aware of the tax  
25 benefits, whether there were alternative forms for acquiring



1 the business, whether the business being acquired was an  
2 ongoing business, or as some authorities say, merely a shell  
3 corporation, would consider whether there were alternative  
4 forms for doing the transaction that what might produce  
5 different increased or decreased levels of tax benefits. Those  
6 are principal factors.

7 Q. And for those factors you talked about, are any of those  
8 factors contained in the Internal Revenue Code or the  
9 regulations to the Internal Revenue Code?

10 A. They're not contained in the Internal Revenue Code for the  
11 most part, they have emerged from decided cases in the area.

12 Q. And in terms of gathering facts to apply, what sources did  
13 you consult to gather facts?

14 A. Well, my focus had been on potential future acquisitions  
15 of profitable businesses. And so without having specific  
16 transactions in front of me, I concluded that there were at  
17 least a class of acquisitions that reorganized WMI could make  
18 without running afoul of Section 269.

19 Q. And of the factors you discussed earlier, are any of those  
20 factors alone dispositive of the principal purpose test?

21 A. There are no deciding factors. You simply weigh them all  
22 and make a judgment as to whether the principal purpose test is  
23 satisfied.

24 Q. And so based on the factors you considered, the relevant  
25 factors you considered, and based on the relevant facts you

1 gathered, what conclusions did you reach about the potential  
2 application of Section 269?

3 A. With respect to potential future acquisitions, I concluded  
4 that Section 382 would be a limitation on the use of the net  
5 operating losses, post emergence but that Section 269 would  
6 likely not apply to such acquisitions.

7 Q. And we've heard from the debtors that Section 269 limits  
8 the amount of money that may be invested into reorganized WMI,  
9 and that the amount is limited to the value of the existing  
10 non-tax assets of reorganized WMI, is that your opinion in this  
11 case?

12 MR. MASTANDO: Object to the form and the  
13 characterization, Your Honor.

14 THE COURT: Overrule.

15 THE WITNESS: No, that is not my opinion. There is no  
16 hard limit on the size of a business that may be acquired  
17 without running afoul of Section 269.

18 BY MR. WALKER:

19 Q. Is your assessment of the weight of that fact -- strike  
20 that question.

21 Does the IRS consider, as a factor, the size of a business  
22 being acquired?

23 A. I think it's a factor, but it's certainly not a  
24 dispositive factor and has to be weighed against all of the  
25 others.

1 Q. Have you ever seen any authority or experienced in your  
2 practice any suggestion that that is a primary factor that the  
3 IRS will consider?

4 A. I had not seen such an indication. I believe it is not a  
5 primary factor.

6 Q. In terms of assessing Section 269 risk, does there need to  
7 be an acquisition of control for 269 to apply?

8 A. Section 269 applies to an acquisition of control of a  
9 corporation. It can also apply independently to an acquisition  
10 of assets in certain tax free or carry-over basis transactions.

11 Q. And in this case, are there different acquisitions of  
12 control that one could consider in assessing Section 269 risk?

13 A. Yes, there are. Some of them could at least conceivably  
14 be subject to Section 269 while others are completely outside  
15 the scope of Section 269.

16 Q. And in terms of periods of time, you know, emergence and  
17 post-emergence, are there different acquisitions of control  
18 that one could consider in assessing the Section 269 risk?

19 A. Yes, there are. One is an acquisition of control that  
20 occurs simply because upon emergence the creditors will acquire  
21 control of the corporation, but then separately, there might be  
22 future acquisitions of control by reorganized WMI of other  
23 corporations.

24 Q. And which of those acquisitions of control did you focus  
25 on in your reports?

1 A. I had focused on the latter, the subsequent acquisitions  
2 of control.

3 Q. And why did you focus on the latter?

4 A. Because I thought it was more likely that the Internal  
5 Revenue Service would be seeking to apply Section 269 to such  
6 transactions and conversely less likely to be applying Section  
7 269 to emergence.

8 Q. And why --

9 MR. MASTANDO: Your Honor, I'm just going to object,  
10 that's not within the scope of his report, that opinion.

11 THE COURT: Overrule. You can raise this on cross.

12 MR. MASTANDO: Thank you.

13 BY MR. WALKER:

14 Q. And why did you reach that opinion?

15 A. Well, the Internal Revenue Service when it examines  
16 taxpayers is looking for understatements of tax liability and  
17 one way to understate an income tax liability is to overstate  
18 an allowable deduction. And because a net operating loss is an  
19 allowable deduction, the Service will be looking for means of  
20 disallowing it, a net operating loss at such time as the  
21 corporation returned to profitability, and I thought it  
22 would've turned to profitability only some years after  
23 emergence when it had acquired other profitable businesses.

24 Q. And in your opinion in assessing whether a future  
25 acquisition of control posed a Section 269 risk, what fact or

1 factors of this potential future acquisition did you focus on  
2 most in your analysis?

3 A. I think I focused primarily on any potential non-tax  
4 business reasons for making such acquisitions, whether it be  
5 for expansion, diversification, economies of scale, things of  
6 that nature, things that have nothing to do with tax.

7 Q. And are there, in your opinion, any future potential  
8 acquisitions by reorganized WMI that pose less of a risk under  
9 Section 269?

10 A. Well, two parts in response to that question. First of  
11 all, there may be certain acquisitions that are outside of the  
12 scope of Section 269 altogether, and so they pose absolutely no  
13 risk under Section 269.

14 Other types of acquisitions may be within the scope of  
15 Section 269, but then are subject to the principal purpose  
16 test. And it was my opinion that so long as reorganized WMI  
17 was making acquisitions within its own existing line of  
18 business, for example, there was a more credible argument that  
19 the transaction would be motivated by substantial non-tax  
20 purposes.

21 MR. WALKER: Thank you, Mr. Anderson.

22 CROSS-EXAMINATION

23 BY MR. MASTANDO:

24 Q. Good afternoon again, Mr. Anderson.

25 A. Good afternoon.

1 Q. Mr. Anderson, I believe you testified that you don't  
2 believe that there's any quantitative limitation on the size of  
3 an acquisition that reorganized WMI could make post bankruptcy;  
4 is that correct?

5 A. That is correct.

6 Q. Okay. And that's the reorganized entity going out and  
7 making acquisitions, correct?

8 A. That is correct.

9 Q. Now, in the course of your work, you discussed Section 269  
10 with Mr. Maxwell from P.J. Solomon, right?

11 A. Yes, I did.

12 Q. Okay. And prior to the finalization of his report, you  
13 discussed usually in a larger group, the general contours of  
14 Section 269, correct?

15 A. That is correct.

16 Q. And you discussed whether there were particular types of  
17 acquisitions that might raise serious 269 issues; isn't that  
18 correct?

19 A. I wouldn't characterize them as serious 269 issues. I  
20 would've characterized them as transactions that could be made  
21 without running afoul of Section 269 from a more positive  
22 perspective.

23 Q. Okay. If you'd take a look at your deposition, please,  
24 page 60, line 7:

25 "Q. Do you recall discussing or telling Mr. Maxwell

1 anything about Section 269 in your communications?

2 "A. Yes.

3 "Q. What did you tell him?

4 "A. To the best of my recollection we discussed usually  
5 in a larger group, the general contours of Section 269 and  
6 whether there were particular types of acquisitions that might  
7 raise serious Section 269 issues."

8 Did I read that correctly, Mr. Anderson?

9 A. Yes.

10 Q. And you advised the equity committee that Section 269  
11 would not be a significant impediment to subsequent  
12 acquisitions of ongoing businesses; isn't that correct?

13 A. Yes.

14 Q. Okay. But you did not discuss whether the creditor's  
15 acquisition of the stock of reorganized WMI under the plan  
16 posed a Section 269 risk; is that correct?

17 A. That is correct.

18 Q. And you did not advise Mr. Maxwell on Section 269 with  
19 respect to the creditor's potential acquisition of control  
20 under the plan; isn't that correct?

21 A. That is correct.

22 Q. Okay. And your May 2nd report, the -- I believe that's  
23 the first exhibit, 367, I believe it is. That does not discuss  
24 Section 269 with respect to the creditor's potential  
25 acquisition of control under the plan; isn't that correct?

1 A. That is correct.

2 Q. Okay. And if you look at page 17 of Exhibit 367, your  
3 first report, the third sentence in the top paragraph states,  
4 "In the case of a typical acquisition of assets or stock of a  
5 corporation, the IRS would likely rely on the more specific  
6 provisions of 382, 383 and 384 of the IRC rather than the fact-  
7 based principal purpose test of Section 269(a) of the IRC." Do  
8 you see that?

9 A. Yes, I do.

10 Q. And the typical acquisition that you're referring to there  
11 would be an acquisition by reorganized WMI itself post  
12 bankruptcy, correct?

13 A. Yes.

14 Q. Okay. Now, your June 23rd supplemental report, Exhibit  
15 368, that does not discuss Section 269 with respect to the  
16 creditor's potential acquisition of control under the current  
17 plan, correct?

18 A. That is correct.

19 Q. And your June 30th second supplemental report, Exhibit  
20 369, that also does not discuss Section 269 with respect to the  
21 creditor's potential acquisition of control under the current  
22 plan; isn't that correct?

23 A. That is correct --

24 Q. Okay.

25 A. -- but I'd also testified that it was less likely to be



1 invoked with respect to emergence.

2 Q. Correct. But your June 30th report, Exhibit 369 does not  
3 discuss Section 269 with respect to the creditor's potential  
4 acquisition of control under the plan, correct?

5 A. That is correct.

6 Q. Okay. And you are not offering an opinion on the  
7 creditor's acquisition of control under the current pending  
8 plan; isn't that correct?

9 A. Well, there are two aspects of that question. The first  
10 is whether there is an acquisition of control, and the second  
11 is whether the principal purpose test could be satisfied.

12 Q. Well, let's take a look at your deposition, Mr. Anderson,  
13 please, if I could direct you to page 71, line 12:

14 "And so you're not offering an opinion on the creditor's  
15 acquisition of control under the current pending plan; is that  
16 correct?

17 "A.

18 It is not in this report, so no, there was no  
19 opinion."

19 Did I read that correctly, Mr. Anderson?

20 A. Yes.

21 Q. Okay. And if you take a look at page 2 of Exhibit 369,  
22 your second supplemental report, in Roman numeral two, in the  
23 second sentence, you state, "The purpose of this expert report  
24 is to provide additional analysis regarding the potential  
25 application of Section 269 to potential acquisitions of assets

1 or control of another corporation by the debtors in response to  
2 Mr. Zelin."

3 Do you see that?

4 A. Yes.

5 Q. And this statement on page two in Roman numeral two of DX-  
6 369, that refers to acquisitions of assets or control of  
7 another corporation being obtained by reorganized WMI post  
8 emergence from bankruptcy; isn't that correct?

9 A. Yes.

10 Q. Okay. And in your June 30th second supplemental report,  
11 DX-369, you are not opining about the creditor's potential  
12 acquisition of control as part of the plan; isn't that correct?

13 A. That is correct.

14 Q. And you don't have a view on the principal purpose test as  
15 it might apply to the settlement noteholders potential  
16 acquisition of control under the current plan; isn't that  
17 correct?

18 A. Well, I've already stated that it was not in my report,  
19 but if you're asking me if I have a view, I do.

20 Q. Okay. If I could direct you to your deposition again,  
21 page 99, please, Mr. Anderson, line 21:

22 "Q. Is it your view that -- let me ask you this, do you  
23 have any opinion as to whether Section 269 might apply to the  
24 settlement noteholder's potential acquisition of control under  
25 the current plan.

1           "A. We had already discussed whether it was an  
2 acquisition of control, that is simply one criteria for  
3 applying Section 269 and I do not have a view on the principal  
4 purpose test."

5           Did I read that correctly, Mr. Anderson?

6           A. Yes, you did.

7           Q. Okay. Now, your June 30th second supplemental report was  
8 meant to respond to Mr. Zelin's report and his deposition  
9 testimony; isn't that correct?

10          A. Yes.

11          Q. Okay. And are you aware that Mr. Zelin is speaking to the  
12 potential applicability of Section 269 to the acquisition of  
13 the stock pursuant to the plan by the creditors?

14          A. No. I actually understood his conclusions to be focused  
15 on the potential for future capital raises and acquisitions of  
16 other businesses.

17          Q. Okay. Well, you read the updated Blackstone expert report  
18 in connection with preparing your June 30th second supplemental  
19 report, correct? Excuse me.

20          A. I believe that I did, yes.

21          Q. Okay. And if I could show you Debtor's Exhibit 341, it's  
22 the June 23rd updated expert report of Mr. Zelin, 341 --

23                   MR. MASTANDO: Your Honor, may we approach?

24                   THE COURT: If it's in the binder, I'll use the  
25 binder.

1 MR. MASTANDO: Okay. Thank you, Your Honor.

2 THE COURT: No, I'll use what I have. 341 I have it.

3 BY MR. MASTANDO:

4 Q. If you look on page 36 of 341, the updated Blackstone  
5 report, the first bullet states, "Blackstone has been advised  
6 that Section 269 of the Internal Revenue Code could potentially  
7 apply to the acquisition of the stock pursuant to the plan by  
8 the creditors, thus disallowing reorganized WMI's future use of  
9 any NOLs."

10 Did I read that correctly?

11 A. Yes.

12 Q. Okay. And if you could take a look at Debtor's Exhibit  
13 253-E, please. It's the valuation analysis from the March  
14 25th, 2011 revised supplemental disclosure statement.

15 THE COURT: Do you want to tell me what binder you're  
16 in?

17 MR. MASTANDO: I believe Binder 1, Your Honor.

18 THE COURT: Okay. I have it.

19 BY MR. MASTANDO:

20 Q. This is the summary of Blackstone's valuation analysis,  
21 correct?

22 A. It purports to be, yes.

23 Q. Okay. And you read the revised supplemental disclosure  
24 statement in connection with preparing your report, correct?

25 A. Yes.

1 Q. Okay. And if you look on page 3 of Exhibit E in the first  
2 full paragraph, the second-to-last sentence says, "Therefore,  
3 Blackstone believes that raising materially more capital than  
4 the estimated amount below unreasonably raises the likelihood  
5 for IRS scrutiny of the initial acquisition of reorganized WMI  
6 that could eliminate any use of the NOLs."

7 Did I read that correctly, Mr. Anderson?

8 A. Yes.

9 Q. If you could take a look back at Debtor's 367, your May  
10 2nd report. On page 5, the third line, it states that  
11 "reorganized WMI could raise substantial" -- it begins with,  
12 "It is further my opinion that the debtors could raise  
13 substantial additional funds through a combination of debt  
14 financing and stock issuances in order to generate taxable  
15 income not subject to current federal income tax taxation, due  
16 to the ability of the debtors to utilize a portion of their net  
17 operating losses, not subject to a Section 382 limitation,"  
18 correct?

19 A. Yes.

20 Q. But you're not opining on the likelihood that any such  
21 additional funds would be raised, correct?

22 A. That is not a tax issue, that is correct.

23 Q. Okay. And you're also not opining on the availability of  
24 those funds in the marketplace, correct?

25 A. That is not a tax issue. That is correct.

1 Q. Okay. And you haven't spoken with any potential investors  
2 about potentially investing in any way in reorganized WMI,  
3 correct?

4 A. That is correct.

5 Q. Okay. Now, it's your understanding that under Section 269  
6 of the Code, the IRS has the ability to completely disallow the  
7 use of the debtors' NOLs if the principal purpose of a  
8 corporate acquisition is to take advantage of an NOL, correct?

9 A. Your question is correct if we have an acquisition that is  
10 already subject to Section 269, that is correct.

11 Q. Okay. And you believed that you communicated to Mr.  
12 Maxwell that the IRS has the authority to disallow in their  
13 entirety the use of the NOLs if the other conditions for  
14 application of 269 are present, correct?

15 A. In theory, yes.

16 Q. Well, in theory, you communicated that to him or you  
17 communicated the theory to him?

18 A. Well, I communicated the theory to him that the Internal  
19 Revenue Service always has the ability to apply Section 269  
20 when its conditions for application are satisfied.

21 Q. And you communicated to him that the IRS has the authority  
22 to disallow in their entirety the use of the NOLs if the other  
23 conditions are met, correct?

24 A. I believe I did, yes.

25 Q. Okay. Mr. Anderson, I think we discussed earlier that you

1 advised the equity committee and its advisors on the  
2 limitations that applied under the Code, right?

3 A. That is correct.

4 Q. And you reviewed portions of Mr. Maxwell's report before  
5 it was finalized, correct?

6 A. That is correct.

7 Q. And the portions of his report that you reviewed  
8 summarized certain of the tax provisions and described the  
9 limitations that applied under the Code; isn't that right?

10 A. That's correct.

11 Q. And in reviewing his report, you focused on the portions  
12 of the report that dealt with the expected amount of net  
13 operating loss available to reorganized WMI after emerging from  
14 bankruptcy, correct?

15 A. Yes.

16 Q. And you focused on the portion of Mr. Maxwell's report  
17 that dealt with the portion of the NOL that would be free of a  
18 limitation under Section 382, correct?

19 A. Yes.

20 Q. Okay. And you advised Mr. Maxwell that you had no  
21 comments on the portions of his report that you reviewed,  
22 correct?

23 A. That is correct.

24 Q. And you're also aware of calculations that Mr. Maxwell ran  
25 in his report, right?

1 A. Yes, I am.

2 Q. And you're aware of the numbers for debt and equity raises  
3 that he hypothesizes on in his report, correct?

4 A. In general terms, yes.

5 Q. Okay. But you didn't focus on those numbers; isn't that  
6 right?

7 A. That is correct.

8 Q. Okay. And you don't consider yourself to have approved  
9 those numbers from a tax perspective; isn't that correct?

10 A. That is correct.

11 Q. Okay. And beyond the calculation of the Section 382  
12 limitation, you did not approve or sign off on any of the  
13 calculations in Mr. Maxwell's report from a tax perspective;  
14 isn't that correct?

15 A. There would not have been any other significant tax  
16 implications, so the answer to the question is no.

17 Q. Let me direct you to your deposition testimony, Mr.  
18 Anderson. Page 55, line 4:

19 "Q. And so beyond the calculation of the limitation that  
20 I think you referenced in your report, Anderson Exhibit 1,  
21 beyond that calculation, did you approve or sign off of any of  
22 the calculations in Mr. Maxwell's report from a tax  
23 perspective?

24 "A. No."

25 Did I read that correctly, Mr. Anderson?



1 A. Yes.

2 Q. Okay. Mr. Anderson, regarding the amount of limited and  
3 unlimited net operating losses, if the effective date of the  
4 plan is delayed beyond August 31st, then the unrestricted  
5 unlimited NOL is reduced, and the limited restricted net  
6 operating loss is increased; is that correct?

7 A. That is correct, assuming all of those things still happen  
8 in 2011.

9 Q. Okay. And if I could ask you to turn to, please, page 4  
10 of your May 2nd report, Exhibit 367.

11 Under Section 2, entitled Summary of Opinion, in the first  
12 sentence, you state, "It is my opinion that the debtors will  
13 sustain an ownership change under Section 382 of the IRC upon  
14 emergence from the Chapter 11 proceeding and the consummation  
15 of the transactions contemplated by the modified plan,"  
16 correct?

17 A. Yes.

18 Q. And then at your deposition I think you said you wanted to  
19 change that to highly likely that the debtors will sustain an  
20 ownership change under 382?

21 A. In response to a question from you, yes.

22 Q. And is that still the case?

23 A. That is still the case, yes.

24 Q. Okay. Now, it's your understanding based on the  
25 information you've seen, that the debtor's tax group has a pre-

1 2011 NOL of approximately 17.7 billion dollars, correct?

2 A. Those are the numbers I have seen, yes.

3 Q. And if you look -- I'm sorry. If you look back on page 4  
4 of DX-367 --

5 A. I'm sorry, is that it?

6 Q. Page 4 of 367. It's the May 2nd report.

7 A. All right. Yes.

8 Q. It states, "It is further my opinion that the net  
9 operating losses of the debtors for the 2011 taxable periods  
10 prior to 2011 as well as a portion of the net operating losses  
11 of the debtors for the 2011 taxable year will be subject to the  
12 limitations imposed by Section 382 of the IRC as a result of  
13 the 2011 ownership change," correct?

14 A. Yes.

15 Q. Okay. And it's your understanding that due to Section 382  
16 limitations, only a small portion of the approximately 17.7  
17 billion dollar pre-2000 NOLs will be available to reorganized  
18 WMI, correct?

19 A. If you meant to say pre-2011, yes, that's correct.

20 Q. Yes, that's what I meant.

21 A. Yes.

22 Q. And to the extent the pre-2011 NOL was attributable to  
23 WMB, when WMB ceases to be a member of the WMI tax group, the  
24 pre-2011 NOL will cease to be available to reorganized WMI,  
25 correct?

1 A. That is correct.

2 Q. Okay. And if you assume emergence in 2011, you would  
3 agree that if the debtors abandon their investment in WMB prior  
4 to the effective date, the NOL for the 2011 taxable year is  
5 expected to include a substantial loss from that abandonment,  
6 correct?

7 A. That is correct.

8 Q. Okay. And you agree it is highly likely that all of the  
9 net operating losses for the 2011 taxable periods prior to  
10 2011, as well as a portion of the NOL for the 2011 taxable year  
11 will be subject to limitations under 382, correct?

12 A. That is correct.

13 Q. And the 2011 net operating loss will be prorated into the  
14 pre-and-post-effective date portions, correct?

15 A. To the extent that there are no recognized built-in losses  
16 in those calculations, that is correct.

17 Q. And the pre-effective date portion is subject to  
18 limitation under 382, correct?

19 A. Yes, that is correct.

20 Q. Okay. And the post-effective date portion of the NOL  
21 would not be subject to limitation under 382 except to the  
22 extent that it consists of a recognized built-in loss, correct?

23 A. With respect to the ownership change that occurs upon  
24 emergence, yes, that is correct.

25 Q. And you do not currently anticipate that it will consist

1 of a recognized built-in loss; isn't that correct?

2 A. Based upon the assumptions and -- that I have seen, that  
3 is correct.

4 Q. Okay. And it's your understanding that the net operating  
5 loss resulting from the stock loss is at least five billion  
6 dollars, correct?

7 A. That is my understanding, correct.

8 Q. And if you assume an August 31st, 2011 effective date, the  
9 debtors may be able to use a substantial portion of the loss  
10 resulting from the abandonment of WMB stock to shield future  
11 income, correct?

12 A. Approximately one-third, yes.

13 Q. Okay. And you would agree that it makes sense in terms of  
14 tax planning for the debtors to abandon their stock in WMB  
15 prior to the effective date, correct?

16 A. Yes, I do.

17 Q. Okay. And the reason for abandoning the WMB stock prior  
18 to the effective date is to avoid the loss being considered a  
19 recognized built-in loss, correct?

20 A. That's correct.

21 Q. And if their loss resulting from the abandonment of the  
22 stock was considered a recognized built-in loss, then only a  
23 portion of reorganized WMI's other 2011 NOLs, which are  
24 significantly smaller in estimated amount, would be subject to  
25 proration, correct?

1 A. That is correct.

2 Q. And so you would agree that from a federal income tax  
3 perspective, having a roughly two billion dollar available net  
4 operating loss is more valuable than maintaining the stock  
5 interest in WMB, correct?

6 A. From a federal income tax perspective, yes.

7 Q. Okay. Now, you understand that it's currently  
8 contemplated that immediately post emergence, reorganized WMI  
9 will consist largely of the stock of Wimrick, correct?

10 A. That is my understanding, yes.

11 Q. And you understand that Wimrick is a reinsurance business  
12 in what is described as run-off mode, correct?

13 A. Yes.

14 Q. And it's your understanding that Wimrick currently does  
15 not have any source of new business, correct?

16 A. That is correct.

17 Q. And based on the facts you've seen, Wimrick is not seeking  
18 new business, it's managing its existing business, correct?

19 A. That is correct.

20 Q. Okay. And Wimrick currently is not doing anything other  
21 than collecting reinsurance run-off proceeds, to the best of  
22 your knowledge, correct?

23 A. To the best of my knowledge, yes.

24 Q. Okay. And you don't have any understanding as to whether  
25 Wimrick has a business plan, correct?

1 A. I have seen the -- I've seen projections, but I don't  
2 think that equates to a business plan.

3 Q. Okay. Now, a little more on Section 269.

4 An acquisition of control is one of the conditions for  
5 applying Section 269, correct?

6 A. That is one of the ways in which Section 269 can be  
7 invoked, yes.

8 Q. It's one of the factors for Section 269, right?

9 A. One of the criteria.

10 Q. Okay. And the creditor's potential acquisition of control  
11 of reorganized WMI following emergence could satisfy that  
12 criteria of Section 269, correct?

13 A. Yes.

14 Q. Okay. And if you take a look back at Exhibit 367, your  
15 May 2nd report, if you'd take a look at page 17. The first  
16 sentence says, "Thus where there is a substantial business  
17 purpose for an acquisition of assets or control of another  
18 corporation, Section 269 of the IRC will not apply." Do you  
19 see that?

20 A. Yes, I do.

21 Q. And you're not opining on whether there is a substantial  
22 business purpose for the acquisition of control of reorganized  
23 WMI by the creditors in connection with emergence, correct?

24 A. That was not included in my written report, correct.

25 Q. Okay. And to determine whether Section 269 applies, you

1 agree that you need to apply the principal purpose test, right?

2 A. If you have a transaction subject to Section 269, yes,  
3 that's correct.

4 Q. And the principal purpose under Section 269 has to be tax  
5 avoidance or tax evasion; isn't that correct?

6 A. Yes, that's correct.

7 Q. Okay. And the principal purpose test is a fact-based  
8 test, right?

9 A. Yes, it is.

10 Q. And you need to look at all the facts and circumstances of  
11 a particular situation, correct?

12 A. Yes.

13 Q. And present intention could be considered, right?

14 A. Yes, it could.

15 Q. And present intention can be manifested in future actions;  
16 isn't that correct?

17 A. Yes, it can. It can be corroborated by future actions,  
18 yes.

19 Q. Okay. And if subsequent facts corroborated the present  
20 intention, that could be considered under Section 269, correct?

21 A. Yes, it could, theoretically.

22 Q. Now, Mr. Anderson, you're aware that Courts have sustained  
23 the IRS' attempt to apply Section 269 to certain transactions,  
24 right?

25 A. Yes, of course.

1 Q. And you're familiar with the Swiss Colony case, for  
2 instance, correct?

3 A. Yes, I am.

4 Q. And in that case, the corporation foreclosed on the stock  
5 of another corporation, which had net operating losses,  
6 correct?

7 A. That's correct.

8 Q. And there, the acquiring corporation liquidated the target  
9 corporation, which had assets of little value, and little  
10 potential future usefulness; isn't that correct?

11 A. Those are the facts of the case, yes.

12 Q. And within a year after requiring control and liquidating  
13 the target corporation, the acquiring corporation admitted  
14 another fifty percent shareholder into the acquired business  
15 with just the good assets; isn't that right?

16 A. That is correct.

17 Q. And so in Swiss Colony, the Court considered the  
18 liquidation which occurred shortly after the original  
19 acquisition of control; isn't that correct?

20 A. Yes.

21 Q. And there, the Court found that the principal purpose was  
22 to avoid taxes by securing the benefits of a deduction, that  
23 the taxpayer would not otherwise have been entitled to enjoy,  
24 correct?

25 A. Yes. But it also did not have the current version of



1 Section 382 at its disposal.

2 Q. Okay. And in Swiss Colony, there was an acquisition of  
3 control that satisfied Section 269, correct?

4 A. That is correct.

5 Q. And in Swiss Colony, the taxpayer, which was the acquiring  
6 corporation argued in part that it's passive and involuntary  
7 repossession of stock was not an acquisition within the meaning  
8 of Section 269; isn't that correct?

9 A. I think that's correct, yes.

10 Q. And the Court found that it was upon repossession whether  
11 that act be defined as an active acquisition or a passive one,  
12 that the taxpayer obtain the essential attributes of control of  
13 the shares; isn't that correct?

14 A. I believe that's what the Court found, yes.

15 Q. Okay. And in Swiss Colony, the taxpayer also argued --

16 THE COURT: Excuse me.

17 MR. MASTANDO: I'm sorry, Your Honor?

18 THE COURT: Isn't this better for argument. I don't  
19 think you're going to get him to change his opinion based upon  
20 your recitation of the facts of Swiss Colony, are you?

21 MR. MASTANDO: Okay. Thank you, Your Honor.

22 THE COURT: All right.

23 BY MR. MASTANDO:

24 Q. Mr. Anderson, I'd like you to consider a hypothetical, if  
25 we can pull up the other demonstrative, please.

1 THE COURT: You may.

2 Q. In this hypothetical, individual X acquires all of the  
3 stock of Z, which has been engaged in the business of operating  
4 retail drug stores, and at the time of the acquisition Z had  
5 net operating loss carryovers aggregating 100,000 dollars and  
6 its net worth is 100,000 dollars.

7 After the acquisition, Z continues to engage in the  
8 business of operating retail drug stores, but the profits  
9 attributable to such business after the acquisition are not  
10 sufficient to absorb any substantial portion of the net  
11 operating loss carryovers.

12 Shortly after the acquisition, X causes to be transferred  
13 to Z the assets of a hardware business previously controlled by  
14 X, which business produces profits sufficient to absorb a  
15 substantial portion of Z corporation's net operating loss  
16 carryovers.

17 Do you see that hypothetical?

18 A. Yes, I do.

19 Q. Do you think that the transfer of the profitable business,  
20 which has the effect of using NOL carryovers to offset gains of  
21 a business unrelated to that which produced the losses  
22 indicates that the principal purpose for which the acquisition  
23 of control was made as evasion or avoidance of federal income  
24 tax?

25 A. Well, to the best of my knowledge, this is an example out

1 of some old Section 269 regulations, and I believe the  
2 regulations concluded that there could be a principal purpose  
3 under those circumstances.

4 Q. Okay. Let's take a look at 371, Exhibit 371. That's in  
5 your binder. You're familiar with this. It's Regulation  
6 1.269-3. Are you familiar with this regulation?

7 A. Yes, I am.

8 Q. And the title of the reg is "Instances in which 269-A  
9 disallows a deduction credit or other allowance," correct?

10 A. Yes.

11 Q. And if you'd take a look at Subsection B, acquisition of  
12 control, transactions indicative of purpose to evade or avoid  
13 taxes. Do you see that?

14 A. Yes.

15 Q. It states, "If the requisite acquisition of control within  
16 the meaning of paragraph one of 269-A exists, the transactions  
17 set forth in the following subparagraphs are among those which,  
18 in the absence of additional evidence to the contrary,  
19 ordinarily are indicative that the principal purpose for  
20 acquiring control was evasion or avoidance of federal income  
21 tax." Do you see that?

22 A. Yes.

23 Q. So Subsection B of the 269 reg provides examples of  
24 acquisitions of control that are indicative of a principal  
25 purpose of tax avoidance, right?

1 A. Ordinarily, according to the regulations.

2 Q. Okay. And the focus of subparagraph 1 of 1.269-3(b) is  
3 the acquisition of control of a corporation with NOLs followed  
4 by steps to make use of the NOLs; isn't that right?

5 A. That is correct.

6 Q. Okay. And the example we just looked at is, in fact, in  
7 the regulation, correct?

8 A. Yes.

9 Q. And if you look on the top of page 2 of the exhibit,  
10 following the hypothetical, the regulation says, "The transfer  
11 of the profitable business which has the affect of using net  
12 operating loss carryovers to offset gains of a business  
13 unrelated to that which produced the losses indicates that the  
14 principal purpose for which the acquisition of control was  
15 made, is evasion or avoidance of federal income tax;" isn't  
16 that correct?

17 A. I'm sorry. My exhibit only has one page with any text on  
18 it.

19 Q. I'm sorry. Do you have Exhibit 371?

20 A. That's where I am right now, yes.

21 Q. Okay.

22 MR. MASTANDO: I can give him my copy. May I  
23 approach, Your Honor.

24 THE WITNESS: I'm sorry. And your question was again?

25 Q. That the -- after the hypothetical in the regulation, it

1 indicates that the transfer of the profitable business, which  
2 has the affect of using net operating loss carryovers to offset  
3 gains of a business unrelated to that which produced the  
4 losses, indicates that the principal purpose for which the  
5 acquisition of control was made, is evasion or avoidance of  
6 federal income tax; isn't that correct?

7 A. Yes.

8 Q. Okay. And you agree with the statement in the Section 269  
9 regulation that if the purpose to evade or avoid federal income  
10 tax, it exceeds an importance or any other purpose, it is the  
11 principal purpose, correct?

12 A. Yes.

13 Q. And it's also your understanding that the determination of  
14 the purpose for which an acquisition was made requires a  
15 scrutiny of the entire circumstances in which the transaction  
16 or course of conduct occurred, in connection with the tax  
17 result claimed to arise there from, correct?

18 A. That's correct.

19 Q. And you're not attempting to scrutinize the entire  
20 circumstances that would apply to the creditor's potential  
21 acquisition of control under the plan; isn't that correct?

22 A. Well, as I had said before, the creditor's acquisition of  
23 control was not a focus of my expert report.

24 Q. Okay. Let me take you to your deposition, page 111, line  
25 13:

1           "Q. You're not attempting to scrutinize the entire  
2 circumstances that would apply to the settlement noteholder's  
3 potential acquisition of control under the plan -- under the  
4 current plan?

5           "A. That is correct."

6           Did I read that correct, Mr. Anderson?

7           A. Yes.

8           Q. Okay. Now, you've never advised a client that Section 269  
9 would apply but not be enforced, correct?

10          A. If your question implies that the service has authorities  
11 at its disposal and simply chooses not to apply them, the  
12 answer is correct. I would not have advised that.

13          Q. Well, let me take you to your deposition, page 42, if I  
14 could, line 17:

15               "Q. Have you ever advised the client that Section 269  
16 would apply but not be enforced?

17               "A. No."

18               Did I read that correctly?

19               A. I'm sorry, I'm still trying to find it.

20               Q. Oh, I'm sorry.

21                       THE COURT: Well, is that different from what he just  
22 said?

23                       MR. MASTANDO: I think it is slightly, Your Honor.

24               Q. Mr. Anderson --

25                       THE COURT: Did you turn the mic off?

1 MR. MASTANDO: Oh, sorry. Maybe someone is sending me  
2 a message. I only have one more question.

3 THE COURT: Well then talk into the other microphone.

4 MR. MASTANDO: Okay.

5 BY MR. MASTANDO:

6 Q. Mr. Anderson, if Section 269 were applicable, would you  
7 have no reason to think the IRS would ignore it, correct?

8 A. That is correct.

9 MR. MASTANDO: Excuse me, Your Honor.

10 (Pause)

11 THE COURT: Are you done?

12 MR. MASTANDO: Nothing further, Your Honor.

13 THE COURT: All right. I'm going to break for lunch,  
14 I don't know about the rest. Let's come back at 2:00, okay.  
15 You're subject to cross-examination, so you should not discuss  
16 your testimony with counsel, okay. We'll stand adjourned.

17 (Recessed at 12:52 p.m.; reconvened at 2:06 p.m.)

18 THE CLERK: All rise.

19 THE COURT: You may be seated. Good afternoon.

20 MR. JOHNSON: Good afternoon, Your Honor. Robert  
21 Johnson from Akin Gump on behalf of the official committee of  
22 unsecured creditors. I have a very short series of questions  
23 to ask Mr. Anderson.

24 THE COURT: All right. You should take the stand.

25 (Pause)

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CROSS-EXAMINATION

BY MR. JOHNSON:

Q. Good afternoon, Mr. Anderson. I'll remind you that you're still under oath.

Did you speak with your counsel about your testimony during the lunch break?

A. No.

Q. Thank you.

Now, you testified a little bit earlier about the operations of Wimrick, Washington Mutual Mortgage reinsurance company, that it's a reinsurance company, and that its portfolios are in run-off. Do you recall that testimony?

A. Yes, I do.

Q. How many people work there?

A. I don't have any information about employment.

Q. Okay. And you've testified you've never seen a business plan from Wimrick. You've seen some projections, but not a business plan.

A. That is correct.

Q. And these sort of details about the operations and the business plan of Wimrick didn't make their way into your expert reports, which we've marked as Debtor's Exhibits 367, 368 and 369; isn't that right?

A. That's correct.

Q. So these are more hypothetical reports about the



1 application of Section 269; is that right?

2 A. Well, as I had testified before, I had been focusing more  
3 on the subsequent acquisition of control of other corporations  
4 with profitable operations post emergence.

5 Q. And so those subsequent transactions have not yet  
6 happened?

7 A. That's correct.

8 Q. So they're hypothetical?

9 A. Yes.

10 Q. Okay. Now, you've also testified that Section 269 does  
11 not impose any per se limitation on the size of a transaction  
12 that reorganized WMI might pursue; is that right?

13 A. That is correct.

14 Q. Let's use an example. Let's say that reorganized WMI  
15 wants to utilize 100 million dollars of its NOLs. How much  
16 income would it need in order to utilize a hundred million  
17 dollars of NOLs?

18 A. It would need 100 million dollars of income.

19 Q. And how much in assets would it need in order to generate  
20 a hundred million dollars in income?

21 A. That's going to depend upon the nature of the business,  
22 and it's outside of my area of expertise.

23 Q. So you couldn't say how much it would be?

24 A. No.

25 Q. Could you say whether it could generate a hundred million

1 dollars using its existing assets?

2 A. The projections don't show that it will.

3 Q. Okay. Now, you've testified, and you've put in your  
4 report that reorganized WMI could issue new stock or take on  
5 new debt in order to acquire assets; is that right?

6 A. Yes.

7 Q. And when you make hypothetical conclusions in your report  
8 regarding Section 269, is it correct that you assume no  
9 ownership change subject to Section 382?

10 A. I assume that capital could be raised in such a way that  
11 there would not be another ownership change post emergence  
12 under Section 382.

13 Q. And you also assumed that there would be no ownership  
14 change within three years; is that right?

15 A. If properly structured, yes.

16 Q. Now, are you familiar with the aspect of Mr. Maxwell's  
17 report where he testified or where he puts in his report that a  
18 value of residual WMI could be in the range of 239 to 278  
19 million by doing a debtor equity raise?

20 A. Yes, I am.

21 Q. How much debtor equity would reorganized WMI have to raise  
22 in order to realize that much value by utilizing NOLs?

23 A. Could you repeat the question, I'm sorry?

24 Q. My question is, how much debtor equity would it take to do  
25 that?

1 A. I don't really think that that's a tax question. It would  
2 really be outside of my area of expertise.

3 Q. Okay. And if reorganized WMI was going to do such a  
4 transaction in order to obtain such a value, would one of the  
5 purposes of the transaction be to take advantage of the NOLs?

6 A. It could theoretically be one among many, yes.

7 Q. Now, Section 269 says that the principal purpose of a  
8 transaction cannot be evasion or avoidance of federal income  
9 taxation; is that right?

10 A. That is correct.

11 Q. What does principal purpose mean in this context?

12 A. Well, first of all, keep in mind that the statute is  
13 drafted so as to require that the purpose of taxable avoidance  
14 or evasion be the principal purpose. And in this context, what  
15 that means is that, the purpose of evasion or avoidance is more  
16 significant, more important, more prominent than any other  
17 purpose.

18 Q. So tax avoidance could be one of the purposes, so long as  
19 it's not the principal purpose?

20 A. As Section 269 is drafted, that is correct.

21 Q. And would you agree that the value of the run-off business  
22 is in the range of 129 to 135 million?

23 A. That's a valuation question and it's really outside the  
24 scope of my expertise.

25 Q. Okay. Now, I believe that you said earlier that it was

1 your view that Section 269 was not likely to apply to a  
2 transaction that reorganized WMI might be able to do in order  
3 to utilize more of its NOLs?

4 A. That is correct.

5 Q. Okay. If you were advising a client that Section 269 was  
6 not likely to apply, would you expect the client to discount  
7 its valuation of that transaction?

8 A. Discount the valuation compared with what?

9 Q. If you had been able to offer an opinion that Section 269  
10 would not apply?

11 A. The two comparisons are that Section 269 would not apply  
12 or -- and that 269 would not -- would likely not apply? I'm a  
13 little bit confused by your question, I'm sorry.

14 Q. I was trying to juxtapose Section 269 would not apply to  
15 one transaction, and Section 269 was not likely to apply to the  
16 other transaction. Would you see a difference between the two?

17 A. Well, to say that it would not apply is to give virtually  
18 an absolute guarantee that it would not apply. Tax lawyers  
19 don't necessarily deal in absolutes. We deal in shades of  
20 gray.

21 Q. Have you ever been involved in a transaction in which you  
22 thought Section 269 might apply?

23 A. Not one that went forward, no.

24 Q. Have you ever advised a client regarding acquisition of  
25 control of a company where the NOLs at issue were subject to

1 court proceedings, such as these, for more than two years?

2 A. Not to my knowledge, no.

3 Q. Now, you were asked some questions during your deposition  
4 about a hypothetical transaction. And the question you were  
5 asked about was GEICO Insurance Company. You were asked  
6 hypothetically whether reorganized WMI could acquire GEICO  
7 Insurance Company. And I believe your testimony was that based  
8 on certain assumptions Section 269 should not apply. Do you  
9 recall that testimony?

10 A. Yes, I do.

11 Q. And when you offered that opinion, isn't it correct that  
12 you had to assume that there was not yet another ownership  
13 change under Section 382?

14 A. That is correct.

15 Q. In order to do an acquisition of that size, wouldn't  
16 reorganized WMI have to undergo another ownership change under  
17 Section 382?

18 A. Not necessarily. There are ways of raising capital  
19 through other means that would not result in another ownership  
20 change.

21 Q. What other means?

22 A. The money could be borrowed. The money could be -- the  
23 capital could be raised through the issuance of what tax  
24 professionals call plain vanilla preferred stock, preferred  
25 stock that is not convertible, does not vote, does not

1 participate in corporate growth to any significant extent.

2 Those are not considered as stock for purposes of determining  
3 whether an ownership change has occurred under Section 382.

4 Q. Isn't the scope of your opinion as to whether reorganized  
5 WMI as it exists will be able to undergo such a transaction as  
6 the one you've just described?

7 A. I don't really -- the feasibility of such a transaction is  
8 really not a tax issue, so I did not have a view on that.

9 MR. JOHNSON: Okay. Thank you. No further questions.

10 THE COURT: Any further cross?

11 All right. Redirect.

12 REDIRECT EXAMINATION

13 BY MR. WALKER:

14 Q. I only have a couple of minutes, Mr. Anderson, of  
15 questions.

16 MR. WALKER: Your Honor, could I -- is ELMO turned on,  
17 is that -- is there some --

18 THE COURT: Is there a switch? I think you turned it  
19 off. Did you?

20 MR. WALKER: Oh, it was on.

21 THE COURT: There it is.

22 MR. WALKER: Thank you.

23 BY MR. WALKER:

24 Q. Mr. Anderson, on page -- Mr. Mastando directed you to page  
25 55 of your deposition, where he asked you if you approved of

1 calculations done by Mr. Solomon, and you answered no, you  
2 didn't approve or sign off.

3 And I just wanted to make clear, you didn't disapprove of  
4 any of his calculations, did you?

5 MR. MASTANDO: Your Honor, I'm just going to object.  
6 I don't think it's appropriate to show him his deposition on  
7 redirect.

8 THE COURT: Well, I'll overrule. I think --

9 Q. I just want to clarify the question -- he asked you the  
10 question about that section right there, "Did you approve or  
11 sign off of any of the calculation in Mr. Maxwell's report from  
12 a tax perspective," "No," and he just -- Mr. Mastando just  
13 asked you is that an accurate reflection of what the record  
14 said.

15 And I just want to clarify, were you talking about, by  
16 answering no, did you disapprove of Mr. Solomon's calculations?

17 MR. MASTANDO: I'm just going to object, Your Honor,  
18 and note the deposition speaks for itself.

19 THE COURT: Overrule. He's allowed to follow-up on  
20 redirect. You can answer.

21 THE WITNESS: I believe what I said in the deposition  
22 is that if I had an objection, if I thought that there was  
23 something incorrect about the report, I would've raised the  
24 objection.

25 BY MR. WALKER:

1 Q. And when you were discussing, when Mr. Mastando was taking  
2 you through this Swiss Colony case, you made some mention of  
3 Section 382. What relevance is Section 382 to the holding of  
4 the Swiss Colony case?

5 A. Well, at that particular time, at the time that the Swiss  
6 Colony case was decided, Section 382 in its then current form  
7 would not have restricted the taxpayer's ability to use the  
8 acquired net operating losses, and because the Internal Revenue  
9 Service had Section 269 as its primary authority for the  
10 taxable years involved in that case, that is the authority that  
11 they used.

12 Because Section 382 in its current form would have  
13 severely limited those net operating losses, the Section 382  
14 limitations would be applied first, and would be considered by  
15 the Internal Revenue Service to be relevant in determining  
16 whether the principal purpose test under Section 269 had been  
17 satisfied.

18 Q. Okay. Mr. Anderson, do you still have Exhibit DX-253-E in  
19 front of you? I believe Mr. Mastando asked you a question  
20 about that exhibit.

21 THE COURT: Say it again.

22 MR. WALKER: 253-E. It's in notebook 1, I believe,  
23 Your Honor, Volume 1.

24 THE WITNESS: I have it.

25 BY MR. WALKER:



1 Q. And Mr. Mastando read you a sentence that says,  
2 "Therefore, Blackstone believes that raising materially more  
3 capital than the estimated amount below unreasonably raises the  
4 likelihood for IRS scrutiny of the initial acquisition of  
5 reorganized WMI that could eliminate any use of the NOLs," do  
6 you see that?

7 A. I'm sorry, what page?

8 Q. It's on page 3.

9 A. 3.

10 Q. The second-to-last sentence of the first full paragraph,  
11 starting "therefore".

12 A. Yes, I do see it.

13 Q. I was wondering if it was clear to you whether the initial  
14 acquisition refers to the acquisition by the creditors through  
15 the plan or whether that applies to the initial acquisition  
16 post emergence?

17 A. Well, the language of this sentence is that it refers to  
18 the initial acquisition of reorganized WMI. And so in context,  
19 I think that that refers to the effects of confirmation and  
20 emergence from bankruptcy.

21 Q. Are there any transactions available to reorganized WMI  
22 that do not come within Section 269 at all, such as the  
23 principal purpose test would not apply at all?

24 A. Yes, there are. Reorganized WMI could acquire the assets  
25 of a profitable business in a taxable transaction, and Section

1 269 would not apply. Reorganized WMI could make an acquisition  
2 of stock, and make an election to treat the acquisition as a  
3 taxable acquisition of assets, and Section 269 would not apply.

4 And then I think also in my third report concluded that  
5 there could be acquisitions of assets from non-corporate  
6 persons that would be outside of the scope of Section 269.

7 MR. MASTANDO: Your Honor, I'm just going to object.  
8 I believe it was beyond the scope of cross.

9 THE COURT: Overrule. I'll allow it.

10 MR. WALKER: I have no further questions. Thank you.

11 RE-CROSS-EXAMINATION

12 BY MR. MASTANDO:

13 Q. Good afternoon, Mr. Anderson. John Mastando again from  
14 Weil Gotshal on behalf of the debtors.

15 You were discussing Swiss Colony again a minute ago on  
16 redirect. Here, the post change net operating loss, at least  
17 a significant portion, is not limited by Section 382; isn't  
18 that correct?

19 A. Here meaning in the case --

20 Q. Assuming confirmation of the plan.

21 A. That is correct.

22 Q. Okay. And are you aware of a hypothetical situation Mr.  
23 Maxwell posed where sufficient income would be generated by  
24 reorganized WMI to shield 273 million dollars in income per  
25 year?

1 A. In general terms, yes.

2 Q. If you take a look at your deposition on page 114, line  
3 23, the question was:

4 "Mr. Anderson, are you aware of a hypothetical situation  
5 Mr. Maxwell posed where sufficient income would be generated by  
6 reorganized WMI to shield 273 million dollars in income per  
7 year?

8 "A. I'm not specifically familiar with that hypothetical,  
9 no."

10 Did I read that correctly?

11 A. Yes.

12 MR. MASTANDO: Nothing further, Your Honor.

13 MR. WALKER: I've got nothing, Your Honor.

14 THE COURT: All right. Thank you. You may step down.

15 MR. WALKER: Your Honor, is the witness excused from  
16 the trial -- from the hearing?

17 THE COURT: Any objection?

18 He may be excused.

19 MR. MASTANDO: Your Honor, at this time, the debtors  
20 would like to call Mr. Rick Reinhold to the stand in support of  
21 confirmation.

22 THE COURT: All right.

23 THE CLERK: Sir, raise your right hand, place your  
24 left hand on the Bible.

25 RICHARD REINHOLD, WITNESS, SWORN

1 THE CLERK: Please state your full name, spelling your  
2 last name.

3 THE WITNESS: My name is Richard L. Reinhold, R-e-i-n-  
4 h-o-l-d.

5 DIRECT EXAMINATION

6 BY MR. MASTANDO:

7 Q. Good afternoon, Mr. Reinhold.

8 A. Good afternoon.

9 Q. Where are you currently employed?

10 A. I am a partner at Willkie Farr & Gallagher in New York.  
11 I'm head of the firm's tax department.

12 Q. Okay. Can you please describe your educational background  
13 for the Court?

14 A. I have a BA degree from Cornell University, and a JD  
15 degree from the State University at Buffalo.

16 Q. Okay. And how long have you been a partner at Willkie?

17 A. Since October 1998.

18 Q. And can you please describe your tax practice generally?

19 A. I have a general business tax practice. I advise on  
20 mergers and acquisitions, restructurings, bankruptcy  
21 restructurings, financing transactions, cross porter  
22 structures, and other sort of frequently seen business  
23 transactions.

24 Q. Okay. And does your practice include advising on Section  
25 382 that we've been discussing here today?

1 A. It does.

2 Q. And does your practice also include advising on Section  
3 269?

4 A. It does.

5 Q. Okay. And how did you become knowledgeable as to Sections  
6 382 and 269?

7 A. When I started out practicing tax law, I became familiar  
8 with Section 382 as then in effect, Section 269, and since that  
9 time, I have made it my business to stay current with changes  
10 in the tax law, the adoption of new regulations, cases that  
11 have come down interpreting those sections, rulings, other  
12 guidance provided by the Internal Revenue Service.

13 Q. And can you please name some of the publicly disclosed tax  
14 matters that you have advised on?

15 A. I was the principal tax advisor in the Adelphia  
16 Communications Chapter 11 bankruptcy restructuring, and also in  
17 the National Energy Group, which is a -- their bankruptcy  
18 restructuring, that's a subsidiary -- the Merchant Energy  
19 subsidiary of Pacific Gas and Electric, and I advised Donald  
20 Trump in the Trump Hotels and Casino Resorts restructuring.

21 Q. And do you regularly advise on bankruptcy matters?

22 A. I do. I do.

23 Q. Can you briefly describe your employment background prior  
24 to joining Willkie?

25 A. From January 1985 until September 1998, I was a partner

1 practicing in the tax area at Cahill, Gordon & Reindel. From  
2 January 1981 until December 1984, I worked at the Treasury  
3 Department in Washington in the office of tax legislative  
4 counsel, and prior to that time, I was a tax associate at the  
5 Hutchinson Ross Law Firm (ph) in Buffalo.

6 Q. And do you hold any academic positions?

7 A. Yes. I teach in the graduate tax program at the NYU Law  
8 School.

9 Q. And do you -- are you involved in any bar associations?

10 A. Yes. I have been involved with the New York State Bar  
11 Association tax section for quite a while. I headed several  
12 committees of the bar association. I was chair of the  
13 corporations committee for several years, and I was chair of  
14 the overall tax section during the period 1996 to 1997.

15 Q. Okay.

16 MR. MASTANDO: Your Honor, I would like to tender Mr.  
17 Reinhold as an expert in corporate taxation, including Sections  
18 382 and 269 of the Internal Revenue Code.

19 THE COURT: Okay. Any voir dire?

20 MR. WALKER: No, ma'am, we're not going to.

21 THE COURT: All right. He will be accepted as such an  
22 expert.

23 BY MR. MASTANDO:

24 Q. Mr. Reinhold, how did you become involved in these Chapter  
25 11 cases?

1 A. I was -- I and my firm were retained by Blackstone in  
2 April of last year.

3 Q. And is Willkie being compensated for its services?

4 A. It is.

5 Q. At what rate?

6 A. We're being compensated at our normal hourly rates.

7 Q. Okay. What were you hired by Blackstone to do here?

8 A. We were hired to advise Blackstone regarding the tax  
9 treatment of the issuance of shares of reorganized WMI to the  
10 creditors pursuant to the proposed plan.

11 Q. And which tax consequences were relevant to your advice to  
12 Blackstone?

13 A. Principally Section 382 which imposes -- in general,  
14 imposes a limitation on the use of tax laws as following an  
15 ownership change, and Section 269 which can eliminate  
16 altogether losses following the acquisition of a loss company  
17 if that acquisition is considered motivated by tax avoidance or  
18 tax evasion.

19 Q. And have you prepared an expert report in this matter?

20 A. I did.

21 Q. If I can show you Debtor's Exhibit 404.

22 UNIDENTIFIED SPEAKER: 13.

23 MR. MASTANDO: Binder 13, Your Honor.

24 Q. Do you recognize Exhibit 404, Mr. Reinhold?

25 A. Yes.

1 Q. And is that your rebuttal expert report?

2 A. It is.

3 MR. MASTANDO: Your Honor, I would like to offer  
4 Debtor's Exhibit 404 into evidence.

5 THE COURT: It's admitted.

6 (Debtor's Exhibit 404, Rebuttal Expert Report of Richard  
7 Reinhold, was hereby received into evidence)

8 BY MR. MASTANDO:

9 Q. Mr. Reinhold, what is your understanding of the purpose of  
10 Section 269?

11 A. Section 269 was adopted in the 1940s to prevent companies  
12 from trafficking in tax attributes principally net operating  
13 losses. That is to say to transfer those losses in tax  
14 motivated transactions, in which case Section 269 can act to  
15 eliminate those tax attributes.

16 Q. And what are the elements of Section 269?

17 A. There are two elements to Section 269. There's a -- the  
18 initial requirement is that there be an acquisition of control  
19 of a loss corporation by one or more persons for the purpose of  
20 securing tax benefits that would not otherwise be enjoyed,  
21 that's the first requirement, acquisition of control.

22 The second requirement is a purpose test which asks  
23 whether the principal purpose, not a purpose, but the principal  
24 purpose of the acquisition is to avoid or evade federal income  
25 taxes.



1 Q. Okay. Now, what is your understanding of control as it  
2 relates to Section 269?

3 A. Control is defined as the acquisition of stock that  
4 represents at least fifty percent of the voting power or fifty  
5 percent of the value of the stock of the loss corporation.

6 Q. And did you reach any conclusions regarding whether an  
7 acquisition of control may occur under Section 269 in this  
8 case?

9 A. Yes. I concluded that the issuance of shares of  
10 reorganized WMI to the creditors, pursuant to the plan would be  
11 an acquisition of control, and that depending on the purpose,  
12 which will depend on some other things, that acquisition could  
13 bring -- could satisfy the purpose test as well. And if the  
14 purpose test was satisfied, then all of the company's losses  
15 would be eliminated upon the acquisition by the creditors.

16 Q. Okay. And just so we're clear, what acquisition of  
17 control are you considering?

18 A. The transfer of the shares of reorganized WMI pursuant to  
19 the plan.

20 Q. And why don't you opine on any post emergence acquisitions  
21 of control?

22 A. Those aren't -- we weren't hired by Blackstone to do that,  
23 and moreover those transactions are not really relevant to the  
24 consummation of the bankruptcy plan.

25 Q. Now, you mentioned the second element of Section 269 is

1 the principal purpose test, can you describe that test?

2 A. The purpose test asks again whether the principal purpose  
3 for the acquisition of control of the loss corporation is  
4 motivated by tax avoidance or tax evasion, by a purpose to  
5 avoid taxes or to evade taxes.

6 Q. And can you --

7 A. And --

8 Q. I'm sorry.

9 A. And I was just going to say that, under the case  
10 authorities, that is a determination of the subjective  
11 intention of the acquirer but since it's not possible to  
12 determine subjective intention, what the case authorities and  
13 interpretations by the Revenue Service have done is to look at  
14 the objective facts of the -- and circumstances to infer the  
15 intention of the acquirers of the loss corporation, including  
16 by reference to future events.

17 Q. Okay. And can you describe some of the factors that are  
18 considered under the principal purpose test?

19 A. I think you could summarize the factors. Again, it's a  
20 facts and circumstances test. In every case, you must look at  
21 all the facts and circumstances that are relevant, but I think  
22 you could summarize the factors as being four principal  
23 factors.

24 The first is the amount of the net operating loss. There  
25 could be other tax attributes, but here we're talking about net

1 operating losses, and that's what I'll refer to. So you would  
2 look at the amount of the loss, and especially in the case  
3 where that loss is very significant in relation to the value of  
4 the company's other assets, that factor would be important.

5 The second factor is the awareness of the acquirer of the  
6 availability of these tax attributes, the consciousness of the  
7 acquirer. And again, as mentioned that will often have to be  
8 determined by reference to the objective facts.

9 The third principal factor is the nature of the business  
10 that the company carries on, with particular reference to the  
11 degree of activity involved in that business, so that on the  
12 one hand, you might have a very active vibrant operating  
13 business, and then the other end of the continuum, you might  
14 have an extremely passive or even shell operation, and the  
15 degree of activity in the company is of great relevance.

16 And fourth, the fourth principal factor is the acquirer's  
17 non-tax commercial motivations for acquiring the company, which  
18 again is going to have to be determined by reference to the  
19 facts and circumstances.

20 And then under a fifth heading or a residual heading, you  
21 could group other factors that might be relevant in a  
22 particular case, such as whether there was another way to  
23 acquire the -- to obtain the benefits, the tax benefits in  
24 question without a Section 269 acquisition, but factors like  
25 that are not present here.

1 Q. Okay. Now, what facts did you consider in applying the  
2 principal purpose test?

3 A. In this case, in this case, there are a couple of factors  
4 that are of real significance in evaluating the application of  
5 the purpose test. First, is the amount of the net operating  
6 loss that would be available subsequent to emergence if Section  
7 269 does not apply. And as I understand it and Blackstone  
8 assumed, there would be about 2.8 billion dollars of losses  
9 available in the period after emergence, based on the worthless  
10 stock deduction, and that's obviously a very significant amount  
11 of loss, especially in relation to the magnitude of the non-tax  
12 asset, which is basically the insurance operation and run-off.

13 So that's one fact. A second important fact is the nature  
14 of the business. As I mentioned, the degree of activity is of  
15 importance. One of the factors that was specifically singled  
16 out in the enactment of Section 269 was the possibility that a  
17 shell corporation with significant tax attributes could be  
18 acquired, and the acquirer would then have the opportunity to  
19 shelter income from an unrelated operation.

20 And so it -- in making an analysis of the facts here, one  
21 would have to think about how much Wimrick represents a shell  
22 corporation. Obviously, there is a degree of activity, but on  
23 the continuum, it is certainly closer to a shell than to an  
24 active operating company.

25 And then the third factor, which in effect would pull

1 those two together, would focus on the extent to which capital  
2 is raised by the acquiring owners of reorganized WMI, the point  
3 being that the more capital they raise, the more suggestive it  
4 is that their purpose in receiving the shares was to avoid tax.

5 That is to say, if you accept that reorganized WMI does  
6 not have any need for additional capital, the assets that it  
7 has on hand today, according to both the debtors and  
8 Blackstone, are sufficient to meet the purposes of running its  
9 business, the insurance run-off operation.

10 So therefore, if more cash is put into the company, it's  
11 strongly suggestive that that purpose of putting that cash in,  
12 is to generate earnings that could then be sheltered by the net  
13 operating loss carryovers.

14 At some point, that purpose becomes the predominant  
15 purpose, and if the purpose of accessing the net operating loss  
16 carryovers, which are not limited in amount, is the predominant  
17 purpose, then I think both tests for the application of Section  
18 269 have been met, and at that point, there would certainly be  
19 a greater degree of risk that Section 269 would come into play  
20 and eliminate the net operating loss carryovers.

21 Q. So I think you've mentioned three main facts. Any other  
22 facts that you considered, including the participants in  
23 developing the plan?

24 A. Right. Well, yeah. So the fact that the creditors  
25 participated in the -- in drafting the plan obviously reflects

1 consciousness of the availability of the tax benefits. That's  
2 an important element for the application of Section 269.

3 Another is that the parties receiving the shares were not  
4 historic owners of the company's shares, and you know, finally  
5 and perhaps it falls into the heading of the obvious, that the  
6 potential tax savings that can be generated here because  
7 Section 382 doesn't apply to such a large amount of loss,  
8 certainly creates the possibility that tax losses here are by  
9 far the most valuable asset in the corporation, and therefore,  
10 could be a -- give rise to a principal motivation to acquire  
11 the company.

12 Q. Now, you mentioned Wimrick, do you have an understanding  
13 of what steps Wimrick would need to take before it could start  
14 writing new business?

15 A. As I understand it, the company today does nothing more  
16 than collect premiums, pay claims, and invest its portfolio.  
17 So it's not a very active business.

18 To become an active business operation, it would first of  
19 all have to develop a business plan, and then it would have to  
20 execute that plan, hire employees, and take other steps in  
21 furtherance of that plan.

22 Q. Okay. And do you have an understanding of the valuation  
23 of reorganized WMI's non-tax assets?

24 A. Yes. As I understand it, Blackstone preformed a valuation  
25 that concluded that the non-tax assets had a value within a

1 range and I believe the midpoint of that range was 127.5  
2 million dollars, and I also understand that Peter J. Solomon  
3 performed a valuation on those assets, and my memory is that  
4 their valuation was 130 to 135 million dollars. I may be off  
5 by a million dollars or so there.

6 Q. And what is your understanding of the net operating losses  
7 potentially available to reorganized WMI? I believe you  
8 mentioned it.

9 A. Yeah. Again, if the stock of the bank is abandoned just  
10 prior to the consummation of the plan, which I think is the  
11 intention here, then a portion of that loss would be allocated  
12 to the period after the consummation of the plan, and it is my  
13 understanding that if the plan is consummated on -- assuming  
14 the plan is consummated on August 31, then the amount of loss  
15 allocable to the period after the consummation would be about  
16 2.8 billion dollars, and that amount, as I understand it, would  
17 not be subject to any Section 382 limitation at all. It'd be  
18 unlimited loss available for use, subject to Section 269.

19 Q. Do you have an understanding of who will own reorganized  
20 WMI after consummation of the modified plan?

21 A. The creditors of the -- the present creditors of the  
22 company would become the owners of reorganized WMI.

23 Q. And are the creditor parties the historic owners of the  
24 debt of WMI?

25 A. I understand that they are not.

1 Q. Okay. Now, after considering these facts that you've  
2 mentioned and these factors, what conclusions did you reach?

3 A. I reached the conclusion that the amount of capital that  
4 the company raises subsequent to the acquisition of the shares,  
5 pursuant to the plan, will be a critical element in indicating  
6 whether the purpose for the acquisition is thought to be tax  
7 motivated.

8 If the amount is less than the value of the non-tax  
9 assets, so that is to say that if the capital raised subsequent  
10 to the emergence is less than a hundred and twenty-seven and a  
11 half million dollars, I'll use that as the proxy for the value.  
12 Obviously, the value will have to be determined.

13 If the amount of capital that's raised is less than that,  
14 then I think the taxpayer has -- the company has quite a good  
15 argument that Section 269 will not be brought into play because  
16 the principal purpose for the acquisition of the shares would  
17 not be considered tax avoidance.

18 And reflective of that, I would be prepared to give advice  
19 at the level of more likely than not, that Section 269 would  
20 not apply. And I think it's fair to say that I think other tax  
21 advisors who are knowledgeable would reach a similar  
22 conclusion.

23 Conversely, if the amount of capital that's raised is in  
24 excess of that 127 million -- 127.5 million amount, again using  
25 it as a proxy, then I think there is greater risk,



1 significantly greater risk that the Internal Revenue Service  
2 would find, and a Court would uphold them that the acquisition  
3 of shares, you know, in the consummation of the bankruptcy plan  
4 was principally tax motivated.

5 And at that point, I would not be able to give advice at a  
6 more likely than not level that the plan was not principally  
7 tax motivated.

8 Q. Okay. Now, why might the amount of capital that  
9 reorganized WMI raises post emergence, why might that affect  
10 whether the principal purpose of the acquisition of control  
11 under the plan was tax avoidance?

12 A. I think there are two analytical steps. The first is to  
13 recognize that the objective facts are what, relating to the  
14 conduct of the company's business and operations, are what a  
15 Court and the Revenue Service are going to look at in figuring  
16 out the deemed intention of the acquirer.

17 The capital raised subsequent to the acquisition will  
18 suggest the purpose for the acquisition. That is to say, if  
19 the amount raised were in excess of a hundred and twenty-seven  
20 and a half million dollars, it would suggest that the parties  
21 acquired the shares with the purpose, principally for the  
22 purpose of acquiring accessing that the tax benefits. So I  
23 think it's a matter of drawing an inference, a factual  
24 inference from the proposition that the capital raised is above  
25 a certain level.

1           And with that factual inference, taking -- looking at all  
2           the facts and all the circumstances of this, you know, the  
3           emergence from bankruptcy with a company in this situation and  
4           all the rest, I think the likelihood is, as I say,  
5           significantly greater that the taxpayer would not prevail in  
6           that case.

7           Q.    And is the advice that you've described here generally the  
8           advice you gave to Blackstone in connection with Section 269?

9           A.    Yes.

10          Q.    Okay.  Now, did you read the expert reports prepared by  
11          Mr. Anderson in this case?

12          A.    I did.

13          Q.    And did you read his deposition transcript?

14          A.    Yes.

15          Q.    Generally speaking, what disagreements do you have with  
16          Mr. Anderson's reports?

17          A.    The first disagreement is really to observe that the  
18          failure on his part to address the possible application of  
19          Section 269 to the issuance of shares on the emergence means  
20          that the principal tax issue in this case has not been  
21          addressed.  So it's an omission that I'm observing, rather than  
22          a disagreement.

23                 The second is that I think there is in what he says a  
24          mischaracterization of the advice that I've given, and I think  
25          it's important, it's not just language.  He says that I apply a

1 per se rule that if capital raised exceeds the value of the  
2 non-tax assets, then the losses are unavailable. And that  
3 sounds like the kind of rule you might find in a regulation or  
4 the statute. And he says since he finds no such regulation or  
5 statute that he can't agree with me. And I think it's  
6 important to say that I have, in my no per se rule instead, I  
7 think that as I said, there's a factual inference to be drawn  
8 from a capital raised above the value of the non-tax assets  
9 that the parties' principal motivation is tax.

10 Q. And does the Blackstone report, as far as you understand,  
11 consider the acquisition of control under the modified plan or  
12 a post emergence acquisition of control?

13 A. The Blackstone report deals only with the first. It deals  
14 with the transfer of shares by the company, pursuant to the  
15 plan to the company's creditors. I -- it does not address  
16 subsequent acquisition transactions that the company might  
17 undertake.

18 Q. And what is your understanding of the acquisition of  
19 control that's considered in Mr. Anderson's second supplemental  
20 report?

21 A. So he is looking at transactions in which the reorganized  
22 WMI after the bankruptcy proceeding might go out and buy the,  
23 or acquire, the stock of a third company. And that has little  
24 to do with the subject that I think we're here to discuss.

25 Q. And did Mr. Anderson apply the principal purpose test to

1 the creditor's acquisition of control of reorganized WMI?

2 A. He did not.

3 Q. And if Section 269 is found to apply here what, if any,  
4 impact would that have on reorganized WMI's ability to use the  
5 net operating losses?

6 A. Those losses would be eliminated.

7 Q. In their entirety?

8 A. Yes. They would likely be eliminated in their entirety.  
9 There's some ambiguity about the application of Section 267(c),  
10 but I think that the more likely outcome is that all of the  
11 losses would be eliminated.

12 MR. MASTANDO: Okay. Thank you, Mr. Reinhold.

13 Nothing further, Your Honor.

14 CROSS-EXAMINATION

15 BY MR. WALKER:

16 Q. Mr. Reinhold, you've been providing -- you testified  
17 you've been providing tax advice to Blackstone in connection  
18 with this bankruptcy, correct?

19 A. That's right.

20 Q. And you were retained in April of 2010; is that correct?

21 A. Yes.

22 Q. And when did you receive Mr. Anderson's first expert  
23 report, do you recall?

24 A. I believe it's dated May 2, but I don't remember when I  
25 first saw it, no.

1 Q. And how about his second expert report, do you recall when  
2 you first saw that?

3 A. I don't think I do remember, no.

4 Q. And his third expert report, do you recall when you first  
5 saw that?

6 A. Same answer, no.

7 Q. And you submitted an expert report -- an expert opinion in  
8 this case last Friday, correct?

9 A. That's right, yeah.

10 Q. Okay. And it's titled a rebuttal report, but you have no  
11 opening report, correct? That's your only report you've  
12 submitted in this case?

13 A. That's right. The report that addresses my disagreement  
14 with what Mr. Anderson has to say.

15 Q. And your report was limited solely to the application of  
16 Section 269 of the Internal Revenue Code; is that right?

17 A. That's right.

18 Q. You don't offer any opinion in this case in the  
19 application of Section 382; is that correct?

20 A. Could I just ask you to repeat that question, please?

21 Q. You've not offered an expert opinion in this case on the  
22 application of Section 382 of the Internal Revenue Code; is  
23 that right?

24 A. Well, I didn't submit an expert report, but certainly we  
25 have advised Blackstone on that subject.

1 Q. And you've advised Blackstone on the application of  
2 Section 269; is that right?

3 A. Yes.

4 Q. And you also have not offered an opinion on the  
5 application of Section 269 to post emergence acquisitions of  
6 control of another company by reorganized WMI, have you?

7 A. No. As I mentioned, Blackstone did not hire us for that  
8 purpose, and that seemed right because I didn't think it was  
9 relevant to what was being discussed here.

10 Q. So is it your testimony that the tax consequences of a  
11 post emergence acquisition by reorganized WMI is not relevant  
12 to the issues in this case?

13 A. Largely. The one exception to that is that to the extent  
14 capital is raised to fund such an acquisition, then it could  
15 obviously have an implication for the analysis that I've  
16 outlined regarding the application of the principal purpose  
17 test, but confined to that.

18 Q. So are you testifying today that if reorganized WMI could  
19 go out post emergence and acquire a third company to take  
20 advantage of net operating losses, that's not relevant to any  
21 other issue in this case?

22 A. Well, let me see if I can answer that this way, and you'll  
23 tell me if I've responded. I think the first thing I would say  
24 is it's possible that Section 269 would apply if reorganized  
25 WMI went out and bought a third company. It's possible it

1 could be a transaction that implicated Section 269. I don't  
2 think it's terribly likely, but it could happen.

3 But as I say, I think that the fact that is important, is  
4 to focus on where the capital came from to fund that  
5 acquisition, because again I do think that's important in terms  
6 of applying the purpose test. That is to say, to analyze  
7 capital raises that occur subsequent to the acquisition of the  
8 shares under the plan.

9 Q. Well, we're talking relevance here I think, and you  
10 testified earlier to Mr. Mastando's questions that you think  
11 that a discussion of post emergence acquisitions, of another  
12 profitable company are not relevant, which is why you didn't  
13 consider that.

14 And so I'm just asking you, is it your testimony today  
15 that if reorganized WMI could go out and acquire a third  
16 company, another company to take advantage of those net  
17 operating losses without running afoul of Section 269, is it  
18 your opinion that that is not relevant in any way to the issues  
19 in this case?

20 A. Let me see if I can say it this way, the fact of  
21 reorganized WMI closing on the purchase of a third company some  
22 time subsequent to the emergence, in and of itself isn't what  
23 is relevant to the discussion here.

24 But reorganized WMI had to get the cash to make that  
25 acquisition from some place. And so that fact could be highly

1 relevant to what we're talking about today. But you asked only  
2 about the acquisition itself. And so if you confine it to an  
3 analysis of the closing of the purchase of that transaction,  
4 that's not going to be relevant. But the financing or the  
5 funding of that acquisition which is indirect would be  
6 relevant.

7 Q. Other than criticizing Mr. Anderson's failure in your view  
8 to look at the acquisition of control being at the time the  
9 creditors acquire control through the plan, you don't disagree  
10 with the conclusions Mr. Anderson reached; isn't that right?

11 A. Well, I think his observation about the fact that a  
12 subsequent acquisition is not likely to bump into problems  
13 under Sections 269, that's probably true, and I can agree with  
14 that.

15 And also he goes about analyzing Section 382, as it would  
16 apply to the consummation of this plan, and I don't have any  
17 great disagreement with what he has to say about Section 382.

18 MR. WALKER: Your Honor, can I approach and hand out a  
19 deposition transcript?

20 THE COURT: You may.

21 THE WITNESS: Thank you.

22 BY MR. WALKER:

23 Q. You recall I took your deposition yesterday, is that  
24 right, Mr. Reinhold?

25 A. I do recall.



1 Q. If you could turn to page 93 of the transcript, line 4.

2 MR. WALKER: Is the ELMO switched on? Do you mind  
3 switching that on for me.

4 Q. So you say, Mr. Reinhold at line 4:

5 "What Anderson says is that reorganized WMI could go out  
6 and acquire a third company without concern for Section 269. I  
7 think that's generally what he says, and as far as it goes, I  
8 think that's generally an accurate statement."

9 Did I read that correctly?

10 A. (No audible response).

11 Q. And you go on then to say --

12 MR. MASTANDO: Sorry. Your Honor, I would just note  
13 that the whole answer wasn't read for the record.

14 MR. WALKER: Okay. Fine. We'll --

15 THE COURT: Yeah. Did he answer the question?  
16 Because I think I need a verbal answer.

17 THE WITNESS: I'm sorry. Yes, that -- you've  
18 accurately read the first paragraph of that two paragraph  
19 answer.

20 BY MR. WALKER:

21 Q. Right. And in the next paragraph, in the next paragraph  
22 you then go on to criticize Mr. Anderson for not looking at the  
23 acquisition of control by the creditors through the  
24 reorganization; is that right?

25 A. Well, I might cavil over the use of the word criticize,

1 but the point is, it doesn't address what I think is a very  
2 important issue, which is how the cash got raised.

3 Q. Sure. And I just want to be clear that as you testified  
4 to yesterday, you don't disagree with the analysis Mr. Anderson  
5 conducts in his expert reports; is that correct?

6 A. I mean, that's a very broad statement. I think I've said  
7 here today that I'm in general agreement with his assertion  
8 that 269 is not going to apply when a third company is bought  
9 in the future, and that statement, I think, is reflected in the  
10 first paragraph of my deposition from yesterday.

11 But then as I said yesterday and as I said again here  
12 earlier today, that you still have to address the question of  
13 how the cash is raised to finance that acquisition, and I do  
14 think that cash -- that fundraising exercise could bring  
15 Section 269 into play, as it relates to the consummation of the  
16 plan.

17 Q. So turn to page 92 of your deposition, your earlier  
18 answer. I asked you if you reached any opinions on the issue  
19 in your report of whether subsequent acquisitions by  
20 reorganized WMI would potentially implicate any Section 269  
21 concerns, and in answer to my question whether you considered  
22 that, you said, "I don't think we disagreed with his  
23 conclusion. I just didn't think we thought that stuff was  
24 relevant."

25 Did I read that correctly?

1 A. You're talking about the language in lines 19 through 21?

2 Q. That's correct.

3 A. Yeah. I mean, I think it's the same thing I'm saying here  
4 now.

5 Q. And you testified that you have been involved in providing  
6 tax advice for about thirty years; is that correct?

7 A. No less than that.

8 Q. No less than thirty years. And over the past thirty  
9 years, a substantial part of your practice has involved  
10 providing tax advice to parties on a broad range of  
11 transactions, that's correct?

12 A. That's right.

13 Q. And part of your practice has also involved seeking  
14 rulings from the IRS on tax issues in advance of transactions  
15 on behalf of clients; is that correct?

16 A. Yes.

17 Q. And as part of your practice as a tax lawyer, you have  
18 represented clients in tax controversies with the IRS; is that  
19 right?

20 A. That's right.

21 Q. And that includes litigating in Tax Court; is that  
22 correct?

23 A. Yes.

24 Q. And you also spent some time at the Treasury Department  
25 providing tax advice to the Treasury Department; is that

1 correct

2 A. That's right, yeah.

3 Q. And you testified that you cannot recall a single instance  
4 in your career in which you were involved in a transaction  
5 where the IRS later raised the challenge under Section 269; is  
6 that right?

7 A. Yeah. Well, let me just say the number of transactions  
8 that I've advised on where the Service later raised an  
9 objection is a pretty small number. And in that limited number  
10 of circumstances, there was no 269 issue raised. That is a  
11 true statement.

12 Q. And you also testified that over the course of your entire  
13 career, you have never sought a ruling from the IRS as to the  
14 applicability of Section 269 to a transaction; isn't that  
15 right?

16 A. That's right.

17 Q. And getting a ruling from the IRS in advance of a  
18 transaction is one way to establish with certainty whether  
19 Section 269 would be applied to a particular transaction; isn't  
20 that correct?

21 A. The Internal Revenue Service will not provide an advanced  
22 ruling on Section 269 issues.

23 Q. And you also testified that during the course of your  
24 career, you have never represented a client in a controversy  
25 with the IRS regarding the application of Section 269?

1 A. I can't recall when I've -- I've certainly had a lot of  
2 issues and a lot of audits, and I can't say that 269 was never  
3 raised, but I cannot recall one, that is true.

4 Q. And you also testified that you don't recall any instances  
5 during your time at the Treasury Department where you assisted  
6 in the formulation of policy regarding 269; isn't that correct?

7 A. It's the nature of work at the Treasury that you focus on  
8 the issues that are involved in legislation of regulations  
9 while you're in the office. And while I was in the office for  
10 that three-year period, nothing relevant to Section -- to the  
11 269 statute of regulations came up with.

12 Whether there were individual corporate tax problems that  
13 we discussed where a 269 was an element of it, I'm guessing  
14 there were, because it's often part of a conversation relating  
15 to the application of corporate tax rules, but I don't recall  
16 specific issues that I addressed at Treasury relating to  
17 Section -- the application of Section 269.

18 Q. And you also testified that although you worked on  
19 formulating published revenue rulings during your time at  
20 Treasury, you don't recall any of them having to do with  
21 Section 269; isn't that correct?

22 A. That's my recollection, yes.

23 Q. And for Section 269 to apply, there must be an acquisition  
24 of control; is that correct?

25 A. Yes, that's right.

1 Q. If you'll turn to your report, Mr. Reinhold.

2 MR. WALKER: Your Honor, do you have a copy of Mr.  
3 Reinhold's report?

4 THE COURT: I do.

5 MR. WALKER: Okay. Thanks.

6 BY MR. WALKER:

7 Q. Do you address the issue of acquisition of control in this  
8 report?

9 A. Yes.

10 Q. And I believe you testified that the total analysis  
11 contained in your report on that, on the issue of the  
12 acquisition of control is the first sentence of the summary of  
13 advice regarding Section 269 on page 4, and then the two  
14 sentence paragraph on page 5; is that accurate? Isn't that  
15 right?

16 A. That sounds right. I could go back and confirm, but --

17 THE COURT: Say that again. What's your question?

18 MR. WALKER: My question was the sum total of his  
19 analysis of the issue of acquisition of control is contained in  
20 the first sentence on page 4 under the heading summary of  
21 advice regarding 269.

22 THE COURT: Okay.

23 BY MR. WALKER:

24 Q. And the first full paragraph, the two sentence paragraph  
25 on page 5, and I just wanted to --

1 A. Well, you know, I make take issue with --

2 Q. -- confirm that.

3 A. -- the word analysis, and the only point is that this  
4 report was designed to be a brief user friendly presentation  
5 that encompassed a pretty broad range of factual situations,  
6 and if I were writing a memorandum of law on the subject such  
7 as for this Court to, you know, consider an issue that was in  
8 doubt, I could have said more.

9 But to my mind, there's not much more to say. There's a  
10 regulation directly on point that says the creditor's receipt  
11 of the shares pursuant to a Chapter 11 plan is an acquisition  
12 for purposes of 269, and we all know that under the plan that  
13 creditors will get more than half of the voting power in the  
14 value of those shares.

15 So it's brief, but I think it says what it needs to say.  
16 There's not more to be said.

17 Q. For reorganized WMI to take advantage of its net operating  
18 losses, it would have to acquire assets that produced taxable  
19 income; isn't that right?

20 A. That's right.

21 Q. So at the time that -- at the time of the reorganization  
22 when the creditors come out, let's assume they come out with  
23 control, come out having acquired control --

24 A. Sure.

25 Q. -- at that point in time, it's your opinion, isn't it,

1 that there's no Section 269 risk?

2 A. No. I don't think that's the case. I think it depends on  
3 knowing more facts, such as how much capital is raised by them  
4 in the future. So I don't think you can make a decision on  
5 that date.

6 Q. Well, that's my point. Looking at that alone before  
7 there's any infusion of capital and any use of that capital to  
8 acquire taxable income producing assets, at the point that the  
9 creditors come out of reorganization with control, there's no  
10 Section 269 risk at that point; isn't that right?

11 A. Let me explain what I mean. The tax law has a concept of  
12 a plan, and all the steps that are taken pursuant to a single  
13 overall plan are considered to happen at the same time, even  
14 though that's obviously a fiction, because those steps don't  
15 all happen at the same time.

16 So as, you know, the regulation that I think Mr. Mastando  
17 discussed with Keith Anderson earlier today talked about a  
18 transfer of assets subsequent to the acquisition of a loss  
19 corporation. Here, there could be a capital infusion  
20 subsequent to the time of the acquisition of the shares that  
21 would be considered to happen at the time of the acquisition of  
22 the shares under this fictional tax construct.

23 So in a sense the answer is, you don't know, but in  
24 another sense, once the facts are all in, you will know, but  
25 only retroactively.



1 Q. It's not until the later infusion of capital after  
2 acquisition of control that, in your opinion, Section 269 risks  
3 arise; isn't that right?

4 A. You know, I don't think that's true. For example, if the  
5 closing happened on -- the emergence consummation happened on  
6 August 31, and the company then later had a capital infusion of  
7 the requisite magnitude so that there was doubt about the  
8 survival of the NOLs, I think a tax return that included the  
9 period September 1 would have to reflect those later facts.

10 So I don't think that the event only happens once the --  
11 the 269 violation occurs only once the later capital raise  
12 happens. But unfortunately, you have to wait. Not  
13 unfortunately, under the tax law, you have to wait until that  
14 later event occurs to know what all of the steps of the plan  
15 are.

16 Q. The infusion of capital post emergence would not be  
17 taxable income to reorganized WMI?

18 A. Should not.

19 Q. Yeah, should not. And just to be clear, you admit that  
20 Section 269 does not impose any per se limitation on the amount  
21 of money that could be invested into reorganized WMI, correct?

22 A. There is no per se limitation in Section 269, only the  
23 application of the facts and circumstances test.

24 Q. One of the principal factors you considered in analyzing  
25 the principal purpose test was the non-tax purposes for the

1 transaction, correct?

2 A. That's right.

3 Q. And you testified that the non-tax business purpose for  
4 the transaction is key to figuring out whether it's a tax  
5 avoidance purpose for the acquisition, didn't you?

6 A. Yeah. That's right. That's the nature of the principal  
7 purpose test to sort the tax purpose and the non-tax purpose  
8 and to balance the two.

9 Q. And when I asked you in your deposition for support for  
10 that position, you said you had looked at and considered the  
11 Section 269 purpose cases, decisions by courts; isn't that  
12 correct?

13 A. Right. We started with the statute, which uses the phrase  
14 "the principal purpose." I looked at the regulations which  
15 explain what the principal purpose is, that it's the purpose  
16 that exceeds an importance of all other purposes. And then I  
17 looked at the rulings in cases that apply Section 269 to inform  
18 how those tests are applied to actual situations that come  
19 before the courts.

20 Q. And do you recall at your deposition I asked you which of  
21 the cases had the most analogous facts to provide the most  
22 guidance to you in rendering this opinion we're talking about,  
23 and you offered two cases. Do you recall this discussion?

24 A. I recall a discussion where we talked about some cases  
25 relevant to particular factors, but no, I don't recall just the

1 way you say it, no.

2 Q. Okay. Well, I -- we can turn to your deposition.

3 A. Uh-huh.

4 Q. You want to turn to page 53. One of the cases you  
5 discussed is Canaveral.

6 A. Uh-huh.

7 Q. That was the first case you mentioned in your discussion  
8 of when you said what you would consider to be reasonably  
9 close. Do you see that? I think the Canaveral case is  
10 probably a reasonably close case. And you said that that --  
11 that was the first case that came to mind as one that you  
12 relied on in helping you reach the conclusions you did about  
13 non-tax purposes.

14 A. Right. Canaveral was a case where essentially the  
15 taxpayer focused solely on the acquisition of the net operating  
16 loss, and you know, the difficulty in any facts and  
17 circumstances case, is that you have to look at all the facts  
18 and all the circumstances, and the precedents are never right  
19 on point, so you have to look at an overall theme and figure  
20 out how a Court's likely to focus on the aspects of the  
21 particular transaction.

22 Canaveral is interesting and relevant because it focuses  
23 on a case where the parties -- it focuses on facts where the  
24 parties were -- had structured the transaction essentially  
25 solely for the purpose of obtaining the benefit of the net

1 operating loss, of a built-in loss, analogous to a net  
2 operating loss, and that's a helpful analogy here.

3 Q. In your deposition yesterday, you offered this case as the  
4 one that you thought was the best support for the conclusions  
5 you reached on whether the non-tax purposes for entering into  
6 the transaction in this case favored or disfavored application  
7 of 269.

8 And do you recall that at least as of yesterday, you  
9 couldn't actually even remember what the non-tax purposes for  
10 entering in the transaction were in Canaveral.

11 A. I don't think there were very good non-tax purposes for  
12 entering into that transaction, but I'm not sure I agree with  
13 your characterization of what I said I was getting out of that  
14 case. It was a case in which the tax motivation was plain, and  
15 that is helpful in analyzing the facts here.

16 Q. Well, I asked you at the deposition what cases you could  
17 identify that --

18 THE COURT: Is this really an appropriate way to use  
19 the deposition? I mean, are you using it to attack what he's  
20 saying today? I don't want to read his whole deposition, and  
21 really, I'm going to apply the same rule that I applied to  
22 counsel for the debtor. If this is a discussion of the facts  
23 of specific cases, I don't know that you're going to get him to  
24 change his opinion.

25 MR. WALKER: Your Honor, it's not a discussion of the

1 facts of Canaveral. I promise I will not get into that here.

2 THE COURT: What is your purpose?

3 MR. WALKER: What I want to do is establish that as he  
4 testified that the case law is important here, important  
5 guidance for him in the conclusions he reached, but he couldn't  
6 identify any cases that were actually relevant.

7 THE COURT: Well, why don't you ask him if he knows of  
8 any cases that are directly on point.

9 BY MR. WALKER:

10 Q. Are you aware of any cases, Mr. Reinhold, that are  
11 directly on point?

12 A. There are a lot of cases in the 269 area that are both  
13 relevant and helpful to understanding how you would treat the  
14 issuance of stock upon emergence, but no, I think you're right,  
15 there is not a case that's directly on point involving a run-  
16 off company issuing shares and so on, no.

17 Q. One of the factors you also testified that you considered  
18 is the -- whether the acquirer is aware of the tax benefits;  
19 isn't that right?

20 A. That's right.

21 Q. And in your hypothetical situation, the acquirer are the  
22 creditors; is that correct?

23 A. That's right.

24 Q. All right. And did you discuss with any of the creditors  
25 whether they are aware of the tax implications in the -- of the

1 plan?

2 A. No. But I don't think it matters, because the  
3 determination of intention is a subjective determination which  
4 has to be determined by reference to objective facts. And we  
5 don't yet have all of the objective facts, although we have  
6 some. We know that the company's in run-off and so on. We  
7 don't know how much capital the creditors will determine to  
8 raise.

9 Once those facts are all in, then I think you can  
10 determine how the Internal Revenue Service or a Court would  
11 judge their intention. Their statements today would not be --  
12 would not get a lot of credence, certainly with the Revenue  
13 Service, perhaps with the Court, because it's obviously self-  
14 interested. And there's 269 cases that plainly say that. So  
15 it doesn't matter I don't think.

16 Q. And in assessing whether the motivations of the acquirer  
17 are tax or non-tax, it's the -- in this instance, it would be  
18 the motivations of the creditors, correct?

19 A. Yes, it is, and it would be, yes.

20 Q. And again, you've not spoken with the creditors about  
21 their motivations for their entering into the plan; is that  
22 correct?

23 A. I'm sorry. I thought I just answered that exact same  
24 question. If that's not the case, please let me know what  
25 different question is being asked.

1 Q. Let's just stick with answering the question, that'll  
2 probably be quicker.

3 In assessing the non-tax motivations, you look at the  
4 motivations of the acquirer, correct?

5 A. That's right.

6 Q. And the acquirer here is the creditor?

7 A. That's right, creditors plural.

8 Q. Creditors, excuse me. And I just want to be clear that  
9 you never spoke with the creditors about their motivations for  
10 entering into the plan as they did.

11 A. Yeah. I mean, I'll just resay that I don't think it's all  
12 relevant --

13 THE COURT: First answer yes or no, then you can  
14 explain.

15 THE WITNESS: Fine. I did not speak to any creditors  
16 for the reason I said a moment ago, I don't think that's  
17 relevant, and I don't think the Service or a Court would find  
18 it relevant.

19 Q. If you'll turn to your report, Mr. Reinhold. I'll direct  
20 your attention to page 4, the section entitled summary of  
21 advice regarding Section 269. I want to direct your attention  
22 to the sentence starting "conversely".

23 You say, "Conversely if reorganized WMI raises additional  
24 capital in an amount that exceeds the value of its existing  
25 non-tax assets, I could no longer determine based on the facts

1 and circumstances to date, that it is more likely than not that  
2 a Court would determine that the principal purpose of the  
3 acquisition of reorganized WMI was not tax avoidance."

4 And I just want to be clear. You are not testifying that  
5 if reorganized WMI raises capital above the value of the  
6 existing non-tax assets, that the IRS is more likely than not  
7 to apply Section 269?

8 A. Yeah. That's right. I mean, I am saying that the degree  
9 of risk increases significantly, but I am not saying that it's  
10 by any means clear that the Service would choose to take on  
11 this case, or that if they litigated that they would, you know,  
12 more likely than not lose the case.

13 Q. And you --

14 A. I mean, I couldn't give an opinion that the taxpayer's  
15 more likely than not to win. Sorry.

16 Q. And you testified also, didn't you, that the only ways to  
17 test the accuracy of your hypothesis here, would be to seek a  
18 private letter ruling or to litigate the issue, or to seek a  
19 ruling, excuse me, or to litigate the issue; is that correct?

20 A. I mean, yeah, as with virtually all legal advice, that  
21 would be the case here as well.

22 Q. And the debtors have not sought a ruling from the IRS on  
23 whether Section 269 applies; is that correct?

24 A. No. As I mentioned under the revenue procedure that the  
25 Internal Revenue Service puts out regarding advanced guidance,



1 they have said plainly that they will not rule on Section 269  
2 issues.

3 Q. And, Mr. Reinhold, one of the last factors you mentioned  
4 that you would consider relevant to the principal purpose test  
5 is whether there are alternative means of accomplishing the  
6 acquisition; is that correct?

7 A. Yes.

8 Q. And obviously one of the options for accomplishing the  
9 acquisition of control you looked at is what was in the  
10 reorganized -- or what was in the plan of reorganization; is  
11 that correct?

12 A. Maybe it's clear and I'm just not understanding, but I  
13 don't understand your question.

14 Q. My question was for your report --

15 A. Uh-huh.

16 Q. -- you obviously looked at one of the alternatives for the  
17 acquisition to go forward, one of the alternatives you looked  
18 at was the actual plan of reorganization, correct?

19 A. Yeah, obviously, yeah.

20 Q. And can you remember what other alternatives you looked at  
21 in assessing this material consideration?

22 A. Right. I don't think there is another way to get the  
23 stock of reorganized WMI to the company's creditors. In some  
24 cases, there are alternative means. Here, I don't think there  
25 is one. I can't think of one.

1 Q. And you testified in your deposition, right, that  
2 liquidation would've been an obvious alternative, but you don't  
3 recall whether it was discussed or not; is that accurate?

4 A. Well, it depends on what you mean by this transaction, in  
5 the sense that if the objective is to get the shares of  
6 reorganized WMI to the creditors, then liquidation of the  
7 company would be inconsistent with that objective.

8 Q. The amount of the -- do you have an opinion on whether the  
9 amount of the net operating losses potentially available to  
10 reorganized WMI affects the valuation of reorganized WMI?

11 A. Sure. It's a -- those losses represent a corporate asset  
12 and would be taken into account in valuing the -- I mean, this  
13 is not tax advice, I don't suppose, but you know, I guess it  
14 falls into the heading of the self-evident, so I would answer  
15 it on that basis.

16 Q. I just wanted to make sure we had the same understanding  
17 of what relevance means, so I'm glad that you clarified that.

18 Now, you're not offering an expert opinion, are you, on  
19 what Wimrick would have to do to become a viable business post  
20 reorganization, are you?

21 A. Well, let me say this, I don't know how relevant it is to  
22 the Section 269 analysis, what business activity Wimrick  
23 engages in beyond continuing the run-off and, you know,  
24 acquiring some level, I guess, of reinsurance assets. But, no,  
25 I don't have a view on that subject.

1 MR. WALKER: I have no further questions. Thanks,  
2 Your Honor.

3 THE COURT: Thank you.

4 MR. WALKER: Thank you, Mr. Reinhold.

5 THE WITNESS: You're welcome.

6 MR. MASTANDO: Oh, you want to? I'm sorry. I didn't  
7 mean to jump.

8 CROSS-EXAMINATION

9 BY MR. STEINBERG:

10 Q. Mr. Reinhold, I'm Arthur Steinberg. I represent the  
11 litigation tracking warrant holders.

12 As I understood your direct testimony is that you've  
13 expressed a concern that Section 269 may apply to the structure  
14 of this plan, and the creditors becoming the shareholders of  
15 the reorganized entity; is that correct?

16 A. That's right, and I made it a bit more particular by  
17 saying that depending on the level of the capital raised, I or  
18 another tax advisor I thought, would be in a position to render  
19 more likely than not advice that the losses would not be  
20 disallowed if the subsequent capital raised was not more than  
21 the value of the non-tax assets.

22 Q. But the reason why you've had this Section 269 discussion  
23 is to sort of minimize what otherwise would be the value of a  
24 two billion dollar NOL that could be used by a company; isn't  
25 that right?

1 A. Well, I mean, the tax law has this overriding rule that  
2 when a company is acquired for the principal purpose of  
3 accessing tax assets, then those assets are eliminated, and  
4 it's not like the losses aren't real or anything of that  
5 nature, it's just that there is this rule, the equivalent of a  
6 blue law in the tax area that says you can't acquire a company  
7 for the purpose of getting tax assets, if that's your principal  
8 motivation.

9 Q. So the risk of potentially losing all of the NOLs is a  
10 factor upon which the valuation of the NOL asset is taken into  
11 account for purposes of this case; isn't that right?

12 A. Well, again, that's the valuation realm, and I certainly  
13 understand what you're saying, but that's not what I've been  
14 hired to advise on, if you know what I mean. It's not a tax  
15 question is my only point.

16 Q. Well, why are you here then?

17 A. My purpose here, my purpose here is to explain the tax  
18 advice that I gave Blackstone, which formed the basis for the  
19 valuation advice that they gave.

20 Q. All right. Are you familiar with Section 1129(d) of the  
21 Bankruptcy Code?

22 A. I'm aware of that section.

23 Q. And is Section 1129(d) sort of like an analog to Section  
24 269 that you've been talking about?

25 A. You know, I haven't thought about it in those terms. I

1 know that it does -- it can get in the way of the confirmation  
2 of a plan, but I can't say that I've studied the 1129(d)  
3 precedence --

4 Q. All right.

5 A. -- so I wouldn't want to express a view.

6 Q. All right. I'm going to read to you Section 1129(d) and  
7 maybe that'll help --

8 A. Okay.

9 Q. -- focus you in.

10 "Notwithstanding any other provision of this section, on  
11 the request of a party in interest that is a governmental unit,  
12 the Court may not confirm a plan if the principal purpose of  
13 the plan is the avoidance of taxes," and then it goes on to the  
14 avoidance of Section 5 of the Securities Act of 1933.

15 So my question to you is, is the language of 1129(d) which  
16 talks about the principal purpose of the plan being the  
17 avoidance of taxes, the same inquiry and analysis that you do  
18 when you do a Section 269 analysis?

19 MR. MASTANDO: Your Honor, objection. It's  
20 argumentative and beyond the scope of the witness' testimony  
21 and expertise.

22 THE COURT: Overrule. If he can answer.

23 THE WITNESS: I can't deny that the words "the  
24 principal purpose" are in both statutes, but context matters,  
25 and I just, I'm sorry to say to you, that I just haven't

1 thought about how 1129(d) might come into play, whether the  
2 Internal Revenue Service is urging its application or anything  
3 of that nature.

4 BY MR. STEINBERG:

5 Q. Well, if it was someone from the Internal Revenue Service  
6 in the courtroom listening to your testimony, he may be  
7 concerned or she may be concerned that the purpose of this plan  
8 is as you've warned, the principal purpose may be the avoidance  
9 of taxes, isn't it?

10 A. I haven't done the work I would want to do to be able to  
11 express a view on Section 1129(d).

12 Q. All right. I think you said you were retained in April of  
13 2010.

14 A. Yes, sir.

15 Q. So you've been involved in this case for over a year,  
16 right?

17 A. That's right.

18 Q. And you were involved in the case when the prior plan that  
19 was -- came up for confirmation in early December was  
20 structured, right?

21 A. Yes, I was.

22 Q. Okay. And under that prior plan, the creditors helped  
23 structure the plan, right?

24 A. I would have to say I assume so.

25 Q. Okay. And under that prior plan, there was an election

1 for only a certain creditor group to become the shareholders of  
2 the new company, right? It wasn't given to everyone. That was  
3 one of the infirmities that the Court found in the confirmation  
4 of payment, right?

5 A. It doesn't sound wrong, but I did not review that in  
6 preparation for coming here today, so.

7 Q. Is the fact that the creditors may have structured the  
8 plan, and they have skewed who could be the beneficiary of  
9 being the shareholder of the reorganized entity, a good fact or  
10 a bad fact for the Section 269 analysis or potentially  
11 irrelevant?

12 A. As I said, I think it's -- the idea that the creditors had  
13 a role in structuring the plan with the consciousness of the  
14 tax attributes that were available, I think is an argument that  
15 you would expect the Internal Revenue Service to make, and I  
16 think a Court would pay some attention to it under the  
17 precedence.

18 Q. But doesn't it even make it worse that in structuring the  
19 plan, they tried to park their benefits only to a select  
20 creditor group and not everyone? Doesn't that make it worse?

21 A. I don't see why that is, no.

22 Q. It doesn't show an emphasis on the way they've structured  
23 the plan for their own personal benefit to try to achieve the  
24 benefits of the NOLs? That doesn't strike you as a concern, as  
25 a tax lawyer of thirty years?

1 A. I can't say that if I knew more facts, I might not feel  
2 differently, but nothing that I'm aware of suggests to me that  
3 that's answer.

4 Q. Okay. Let's throw another factor in. That same plan  
5 provided that the same creditor group could participate in a  
6 registration rights offering for a hundred million dollars of  
7 financing for the new entity to take advantage of the NOL. Is  
8 that a good fact or a bad fact for your 269 analysis?

9 MR. MASTANDO: Objection, Your Honor. It's  
10 argumentative and beyond the scope of the witness' testimony  
11 and then counsel's testifying.

12 THE COURT: Well, overrule. I think that he can add  
13 some facts to his hypothetical and ask him for his opinion.

14 THE WITNESS: Could I just ask you to repeat it,  
15 because I'm not sure I knew these facts.

16 BY MR. STEINBERG:

17 Q. If the same creditor group that was trying to get the  
18 benefits of being the shareholder of the reorganized entity  
19 which has all this valuable NOL is also the same person  
20 providing financing under the plan for a registration rights  
21 agreement in contributing up to a hundred million dollars to  
22 this otherwise moribund run-off insurance company? Good fact  
23 or a bad fact for purposes of your 269 analysis?

24 A. Again, maybe if I thought about it more, I would reach a  
25 different conclusion, but as I sit here today, I don't see why



1 it's different.

2 Q. Okay. Let's talk about the -- this plan and the  
3 shareholder election that took place here. Creditors who  
4 otherwise were entitled to get a hundred cents in cash have  
5 opted to take stock of the reorganized entity.

6 A. Uh-huh.

7 Q. Now, the reorganized entity has basically two assets, I  
8 think you said. One is the moribund insurance company who's  
9 running off collecting just premiums over an eight-year period  
10 of time, and the second is the NOL, right? Are you aware of  
11 any other assets?

12 A. I don't think I said that, but by the same token, I am not  
13 aware of any other material assets, no.

14 Q. Well, there's the insurance company, right? Were you  
15 quibbling with me on the insurance company description or the  
16 NOL description?

17 A. I'm sorry. I wasn't meaning to quibble, I just don't --  
18 there may be some other assets, but I don't believe they're  
19 material.

20 Q. Okay. Because I think you said in your testimony that the  
21 insurance company was close, in a 269 analysis, to almost like  
22 a shell company, you can make that argument, right?

23 A. That there is an analogy to be drawn.

24 Q. Okay. And I think you also said that the -- in the battle  
25 of the experts when they came to value the insurance company,

1 they were within a fairly tight range, almost within like ten  
2 million dollars of each other, right?

3 A. Oh, wait, those are the non-tax assets, and I'm not  
4 certainly knowledgeable about that subject.

5 Q. Well, neither am I. I'm just saying that you were -- I'm  
6 just trying to repeat what you said, when you analyzed the  
7 reports, that your expert and his expert basically were between  
8 a 125 and 135 million dollars for the Wimrick asset, right?  
9 I'm expressing no view of about what it is either, I'm just  
10 trying to try to summarize a point.

11 A. I think that's a generally correct statement about what  
12 the Blackstone report and the Peter J. Solomon report did in  
13 valuing the non-tax assets, yes.

14 Q. And the valuation that the debtor was proffering is that  
15 the reorganized entity is 160 million dollars, right?

16 A. That doesn't sound wrong, but I don't have that number at  
17 hand.

18 Q. All right. Well, the difference between the Wimrick asset  
19 and the valuation the debtor has is the valuation that someone  
20 gave to the NOL, right?

21 A. That's not a tax question, but that is my understanding.  
22 That is more or less my understanding of --

23 Q. And would you agree with me --

24 A. -- what the report says. Sorry.

25 Q. Would you agree with me as a hypothetical that if someone

1 made a stock election instead of taking cash, they'd probably  
2 believe that the stock is worth more than cash?

3 A. It is not a tax question.

4 Q. Well, I know, but I'm trying to make it as a tax point. I  
5 promise I'll tie it in, and then you can jump in and answer.  
6 But would you agree with that as a general proposition?

7 A. I certainly see why you would say it, but again, it's not  
8 here what I'm do.

9 Q. I understand. But sometimes we have to --

10 THE COURT: He can assume that fact --

11 MR. STEINBERG: Okay.

12 THE COURT: -- for purposes of your next question.

13 MR. STEINBERG: Okay.

14 BY MR. STEINBERG:

15 Q. So if you assume that the -- that people have taken a  
16 stock election for something greater than cash, they either  
17 value the insurance company asset to be more than what  
18 Blackstone has valued, or they assume that the utilization of  
19 the NOL would be more than what Blackstone has analyzed; isn't  
20 that correct?

21 A. Again, it's not a tax question, but it would be consistent  
22 with the assumption.

23 Q. And if you assume that people are fairly comfortable with  
24 the range of a run-off entity, would it be fair to say that the  
25 variable that people are expressing for purpose of taking the

1 stockholder election is the utilization of the NOL?

2 A. You know I'm sorry, I -- again, I have read the Blackstone  
3 report. I think I understand it. I understand the point that  
4 you're making, and you know, what I get paid to do, is to think  
5 about the tax law.

6 Q. Okay. But someone who's making the stockholder election  
7 is also probably thinking about the tax attributes and the  
8 ability to utilize the tax attributes; isn't that true?

9 MR. MASTANDO: I'll try one more time, Your Honor.

10 THE COURT: Yeah. We are now getting into argument.  
11 He's not going to answer your question.

12 MR. STEINBERG: I was getting him to agree with me,  
13 Your Honor, I thought I was going to continue on.

14 BY MR. STEINBERG:

15 Q. Would it be fair to say that if 269 applied and the NOLs  
16 were thrown out, that anybody who made a stockholder election  
17 for a company that's worth 125 million dollars made a bad  
18 decision?

19 MR. MASTANDO: Same objection, Your Honor.

20 THE COURT: Sustained.

21 MR. STEINBERG: Okay.

22 Q. Now, I think you said that one of the things that you need  
23 to do to express the -- to do a fair, a more complete analysis  
24 on 269 is to address the fundraising activity that is  
25 contemplated.

1 A. You would need to understand that in order to form a  
2 judgment about the principal purpose, and obviously those are  
3 activities that will happen at some point in the future.

4 Q. Do you know anything about what the fundraising activity  
5 is for this reorganized entity?

6 A. I do not know.

7 Q. Ever asked the question to anybody, in order so you could  
8 do a better tax analysis?

9 A. I think we made it apparent to Blackstone that if there  
10 were information available on the subject, it would be highly  
11 relevant to the analysis we're doing, so I would have to say I  
12 assume that information would've been shared with us.

13 Q. And you think if there's two billion dollars of NOL to be  
14 utilized, if someone's trying to raise funds in order to be  
15 able to utilize it?

16 A. Again --

17 MR. MASTANDO: Same objection, Your Honor.

18 THE COURT: Sustained.

19 Q. Okay. I think you said you worked on Adelphia and  
20 National Energy from a tax aspect of 382 and 269. Could you  
21 tell me in Adelphia, whether there was a 269 issue or a 269  
22 concern?

23 A. I don't recall.

24 Q. Okay. In Adelphia they sold all of their assets, I think  
25 it was the Time Warner as part of before the -- or as part of

1 the plan or before the plan?

2 A. I -- all the assets, I don't remember. I would need to go  
3 back, it's been a couple of years and relook at the plan.

4 Q. Okay.

5 A. I'm sure if there was a 269 issue, I'd like to believe we  
6 saw it and discussed it.

7 Q. Do you remember what the NOL was in -- with Adelphia that  
8 was -- that emerged after the bankruptcy?

9 A. I don't off hand, I'm sorry.

10 Q. Do you remember whether the creditors got the advantage of  
11 the NOL as part of the Adelphia plan?

12 A. I don't recall.

13 Q. Okay. Maybe you have a better recollection with National  
14 Energy. Do you remember whether there was a 269 issue there?

15 A. I don't recall, as I sit here now, no.

16 Q. Do you remember what the NOL was for National Energy?

17 A. I could be remembering wrong, but I thought that whether  
18 there would be enough losses to shelter the income from sale of  
19 the properties was actually a question in that bankruptcy, but  
20 I have certainly not reviewed it in connection with coming here  
21 today.

22 MR. STEINBERG: I don't have any other questions.

23 THE COURT: Thank you.

24 MR. JOHNSON: Your Honor, just two questions. For the  
25 record, it's Robert Johnson from Akin Gump on behalf of the

1 creditor's committee.

2 CROSS-EXAMINATION

3 BY MR. JOHNSON:

4 Q. Mr. Reinhold, assume that reorganized WMI raises 130  
5 million dollars in new capital and acquires a profitable  
6 company. Isn't the fact that we are having these proceedings  
7 here today in open court, under the watchful eyes of the press,  
8 in the biggest bank holding company bankruptcy in the history  
9 of the nation, like waiving a big red flag at the IRS?

10 A. I could certainly see why you would ask that question.

11 THE COURT: Is the answer yes or no?

12 Q. In this scenario, in your professional opinion, do you  
13 think it likely that the service will scrutinize any such  
14 acquisition by reorganized WMI very carefully to determine  
15 whether the transaction was done with the principal purpose of  
16 tax avoidance?

17 A. You know, I hesitate to predict what the Internal Revenue  
18 Service does. You don't necessarily understand what they're  
19 thinking at any given time, but again, I think that's -- that  
20 plainly would be a concern.

21 MR. JOHNSON: Thank you.

22 THE COURT: Anybody else?

23 Redirect?

24 MR. MASTANDO: Nothing further, Your Honor.

25 THE COURT: Thank you. You may step down. Let's talk

1 about what we have remaining.

2 MR. MASTANDO: Your Honor, the debtors were next going  
3 to call Mr. Zelin from Blackstone. I would imagine his direct  
4 would be about an hour.

5 THE COURT: Uh-huh. We don't -- let me give you  
6 availability. I do not have any availability tomorrow morning.  
7 But my two o'clock case has come off. So I would have tomorrow  
8 afternoon and we have Friday. Are we going to finish all  
9 testimony in that period of time?

10 MR. MASTANDO: I'll defer to Mr. Rosen.

11 MR. ROSEN: I'll give it a shot. Thank you.

12 Your Honor, as Mr. Mastando said, we believe that Mr.  
13 Zelin's testimony, his direct testimony will be about an hour.  
14 We're unclear as to obviously how long the cross-examination  
15 will be.

16 After that, we have been told that -- well, we have  
17 Mr. Goulding and his direct examination will probably be around  
18 forty-five minutes. I do not know what the cross-examination  
19 will be.

20 After that, Your Honor, we get to the tranche 3, and  
21 while we do not know what the -- I'm sorry, I apologize. Thank  
22 you, then Maxwell, and I don't know what his direct will be,  
23 but I know that the cross will be of -- at least an hour?

24 UNIDENTIFIED SPEAKER: Probably.

25 MR. ROSEN: About an hour. And when we get to tranche



1 3, Your Honor, although I do not know what the directs will be,  
2 Mr. Sargent previously informed me that the four settlement  
3 noteholders' cross-examination will be approximately four  
4 hours, excuse me, five hours; two for the first person he  
5 thought, and three for each of the subsequent. I don't know if  
6 that has changed, but that was last week's thought process.

7 And then I -- with Mr. Kostoros, his direct, Your  
8 Honor, we believe that that will probably be around thirty-five  
9 minutes to forty-five minutes, and I do not know what the cross  
10 will be.

11 So in answer to your question, Your Honor, assuming  
12 that to be the case, we may be close to finishing Friday  
13 afternoon, but I cannot guarantee it, because I don't know what  
14 the great unknown or the variables are.

15 And then, Your Honor, we had talked with your chambers  
16 about a continuation of next week, and we were told that we  
17 were looking at Tuesday afternoon and Wednesday.

18 I'm sorry?

19 MR. HOROWITZ: I'm sorry, I have to say something.

20 MR. ROSEN: Go ahead.

21 MR. HOROWITZ: Excuse me, Your Honor, I never  
22 introduced myself. Gregory Horowitz from Kramer Levin on  
23 behalf of Aurelius today. But I'm standing now because I just  
24 learned something. I'm going -- I was going to appear before  
25 you on Monday on behalf of the creditor's committee in Magna

1 (ph), we had a one-day claim objection hearing. No, we did not  
2 settle, but I just got an e-mail from the claimant saying that  
3 his principal's son is going through emergency surgery on  
4 Monday, and begging me to try and get a new date. So Monday  
5 may be opening up for you.

6 MR. ROSEN: I only asked about the settlement since  
7 I'm debtor's counsel in Magna, so I --

8 MR. HOROWITZ: Right. I wish that it settled as well,  
9 but I thought that was pertinent news I would bring to your  
10 attention, Your Honor.

11 THE COURT: Well, Mr. Rosen, do you agree to the  
12 continuance of the Magna trial because of the emergency  
13 surgery?

14 MR. ROSEN: Oh, it is fine with us. While we are the  
15 debtor's counsel, it is primarily a creditor's committee fight  
16 with the claimants, so whatever they want to do is fine.

17 MR. HOROWITZ: Yes. I'm primarily handling it, Your  
18 Honor, and we're not crazy about this because as you know, the  
19 distributions have been held up for over a year on this, but I  
20 don't know that I can ask the Court to deny an adjournment  
21 under circumstances like that. It does create certain  
22 problems, Your Honor.

23 THE COURT: Yes, it does. Well then, we have Monday,  
24 Tuesday by the way is probably cleared up. Wednesday, I do  
25 have matters on Wednesday. So I'd prefer to go Monday,

1 Tuesday. Monday, finish up testimony, and argument Tuesday, is  
2 that what the parties --

3 MR. ROSEN: I would think that would work, Your Honor.  
4 It'll give us a little bit of time if we finish early on Monday  
5 to try and put together all of the evidence.

6 MR. STEINBERG: Your Honor, I know you have lots of  
7 lawyers with lots of schedules, but it would be very, very  
8 helpful for me if we do whatever my involvement in this  
9 proceeding would be, to be finished by Monday, because I have  
10 previous commitments starting on Tuesday.

11 So I'm happy to stay later to do Mr. Zelin today, to  
12 work whatever's necessary, and to deal with whatever the  
13 closing argument is in written form, but it would be really  
14 hard for me to take this past Monday. So to the extent that  
15 all counsel want to move this along fast, they can all take  
16 notice of the burn rate of the case, then we would -- I would  
17 personally appreciate seeing how this could be moved up.

18 THE COURT: Well, I can't promise anything, but I can  
19 do Zelin today, and we'll see --

20 MR. STEINBERG: Now, I will say, Your Honor --

21 THE COURT: -- how much we can finish.

22 MR. STEINBERG: -- that I do not anticipate  
23 participating in what they've been calling the tranche 3, so for  
24 whatever that's worth.

25 THE COURT: But you do want to do argument.

1 MR. STEINBERG: I do. And it may be that I could do  
2 my argument in writing. If not, it may be through the squawk  
3 box.

4 MR. ROSEN: Your Honor, that's fine. So we will do  
5 Mr. Zelin today and we will start with Mr. Goulding tomorrow,  
6 and then Mr. Maxwell. Because some of the other people who are  
7 in tranch 3 I believe are going to be traveling in for  
8 tomorrow, what time are we starting tomorrow?

9 I know that you had some -- a calendar in the morning  
10 with respect to your Virgin Islands' cases.

11 THE COURT: Yeah, and then I have an 11:30. So I  
12 suggest we start at 1:00 tomorrow.

13 MR. ROSEN: Thank you, Your Honor.

14 THE COURT: We'll go 1:00 to 5:00 tomorrow.

15 MR. ROSEN: And I think that'll probably handle Mr.  
16 Goulding and Mr. Maxwell and maybe get to the first witness in  
17 tranch 3.

18 THE COURT: All right. Well, let's take a short break  
19 and then we'll go ahead with Mr. Zelin.

20 (Recessed at 3:55 p.m.; reconvened at 4:09 p.m.)

21 THE COURT: All right. You may go ahead with Mr.  
22 Zelin.

23 MR. MASTANDO: Good afternoon, Your Honor, John  
24 Mastando on behalf of the debtors. Your Honor, the debtors  
25 would like to call Mr. Steven Zelin to the stand in support of

1 confirmation.

2 THE CLERK: Please raise your right hand.

3 STEVEN ZELIN, DEBTOR'S WITNESS, SWORN

4 THE CLERK: Please state and spell your name for the  
5 record.

6 THE WITNESS: Steven Mark Zelin, Z-e-l-i-n.

7 MR. MASTANDO: Your Honor, I apologize. Before we  
8 begin could Mr. Reinhold be released from the courtroom?

9 THE COURT: Yes, any objection? You may.

10 MR. REINHOLD: Thank you, Your Honor.

11 DIRECT EXAMINATION

12 BY MR. MASTANDO:

13 Q. Good afternoon, Mr. Zelin.

14 A. Good afternoon.

15 Q. Could you please describe your educational background for  
16 the court?

17 A. Yes, I have an undergraduate degree in accounting from the  
18 University Albany, which I received in 1984 and I have an MBA  
19 in finance that I received from the Sterns School of Business  
20 at NYU in 1991.

21 Q. And do you have any continued involvement with those  
22 schools?

23 A. Yes, I continue to serve on the Board of the University of  
24 Albany Business School and I am the dean -- I'm sorry, the  
25 Chair of the Dean's Executive Board at the Sterns School of

1 Business.

2 Q. And do you have any professional certifications?

3 A. I am a CPA, yes.

4 Q. Okay. Now where are you currently employed?

5 A. Blackstone Advisory Partners.

6 Q. And can you generally describe Blackstone's business?

7 A. Blackstone is a publicly traded financial advisory and  
8 investment firm. We have as two principals lines of business,  
9 money management and investing and financial advisory, and I  
10 work in the financial advisory side of that business.

11 Q. And how long have you been employed at Blackstone?

12 A. I joined Blackstone in January of 1998.

13 Q. And what is your current position at Blackstone?

14 A. I am a senior managing director.

15 Q. And how long have you held that position?

16 A. Since 2001.

17 Q. And what are your responsibilities as a senior managing  
18 director at Blackstone?

19 A. As it relates to client service I am typically the deal  
20 team leader on advisory assignments that I work on.

21 Q. Now can you just briefly describe your employment history  
22 prior to joining Blackstone?

23 A. Yes, upon graduation from undergraduate school in 1984 I  
24 joined the accounting firm of Ernst & Whinney, as an accounting  
25 auditor and tax advisor. I spent four years in that capacity

1 and then transferred over to Ernst & Whinney, or it may have  
2 been Ernst & Young by then, to Arthur Newman's restructuring  
3 group that was resident at Ernest & Young. And I left that  
4 firm as a partner in 1997 to join Blackstone in 1998.

5 Q. And can you briefly describe some of the publicly  
6 disclosed assignments on which you've provided restructuring  
7 services?

8 A. I've advised mostly debtors, but debtors and creditors in  
9 restructuring transactions. And my principal debtor  
10 assignments have been Enron Corporation, General Motors,  
11 Abitibi Bowater, SEM Group, Centor Gaming (ph), some informal  
12 clients needing restructurings included Ford Motor Company,  
13 Xerox Corporation, Goodyear Corporation, there are many others.

14 Q. And have you previously been qualified as an expert in  
15 valuation?

16 A. I have testified on many occasions in bankruptcy court on  
17 valuation and have been qualified as an expert in many of those  
18 situations.

19 MR. MASTANDO: Your Honor, I would like to tender Mr.  
20 Zelin as an expert in valuation.

21 MR. ARD: No objection.

22 THE COURT: All right. You will be so qualified.

23 MR. MASTRANDO: Thank you.

24 BY MR. MASTRANDO:

25 Q. Mr. Zelin, is Blackstone being compensated for its

1 services?

2 A. Yes, we are.

3 Q. And at what rate?

4 A. We received in two installments a fee of one million 350  
5 for issuing our initial valuation report back last year, and  
6 since September 2010 we have received a monthly fee of seventy-  
7 five thousand which continues today.

8 Q. Okay. Now can you describe the tasks that the debtors  
9 retained Blackstone to perform here?

10 A. Yes. When we were contacted by the debtors in March or  
11 April of 2010, we were asked to provide pursuant to our  
12 mandate, valuation advice with respect to the securities and  
13 assets that would be resident within reorganized WMI.

14 Q. Okay. And what is your understanding of what reorganized  
15 WMI is?

16 A. It is today principally a run-off reinsurance company.

17 Q. And what do you understand the name, what the name of that  
18 company is?

19 A. Yes. It's called Wimrick.

20 Q. And what's your understanding of what reorganized WMI will  
21 be post emergence?

22 A. Upon emergence I do not believe that its business plan  
23 suggests that any change from what it is today, which is a run-  
24 off -- it will be continued to be managed as a run-off  
25 reinsurance company.



1 Q. Now did the debtors give you any specific instructions as  
2 to how to value reorganized WMI?

3 A. No, they just asked me to come in and provide our  
4 independent view on valuation.

5 Q. And can you describe your personal involvement in  
6 Blackstone's valuation?

7 A. Yes. As I am in all restructuring assignments, as an SND  
8 in the firm, I'm the team leader, so it was my responsibility  
9 to lead all of those -- all the projects Blackstone undertook  
10 in reaching its -- reaching my valuation conclusion.

11 Q. Okay. And what items did Blackstone review in connection  
12 with this valuation?

13 A. It reviewed plans and disclosure statements that were  
14 available at that time and subsequently available. We reviewed  
15 the projections prepared by management of the company, or  
16 Alvarez & Marsal, I should say. We prepared the supporting  
17 documents that fed into those projections predominantly  
18 actuarial analysis prepared by Milliman, the company's  
19 actuarial advisor. We spent hours in discussion with Alvarez &  
20 Marsal and with Willkie Farr & Gallagher, Rick Reinhold, who  
21 just testified here who we had hired as our tax advisor. And  
22 we then just looked at other publicly available information  
23 that we deemed relevant to our assignment.

24 Q. And did you review the debtors' analysis of certain net  
25 operating losses potentially available?

1 A. Yes. And an analysis was provided to us.

2 Q. Okay. Now you mentioned that Blackstone was retained to  
3 prepare a valuation, did you prepare any such report in  
4 November of 2010?

5 A. Yes, we did.

6 Q. And did you prepare a report in June 2011?

7 A. Yes.

8 Q. And if I could ask you to take a look at Debtors' Exhibit  
9 341, which should be in front of you on your binder.

10 A. I have it in front of me and in many places around me.

11 Q. Do you recognize Debtors' 341?

12 A. I do.

13 Q. And what is it?

14 A. This looks to be a copy of the valuation report I prepared  
15 dated as of June 23, 2011.

16 MR. MASTANDO: Your Honor, I'd like to offer Debtors'  
17 342 into evidence.

18 THE COURT: Any objection?

19 MR. ARD: No objection.

20 THE COURT: It's admitted.

21 (Debtors' Exhibit 341, Valuation Report dated June 23, 2011,  
22 was hereby received into evidence)

23 MR. MASTANDO: Thank you, Your Honor.

24 BY MR. MASTANDO:

25 Q. Mr. Zelin, can you please describe your understanding of

1 Wimrick's current business for the court?

2 A. Yes.

3 Q. I know you touched on it already.

4 A. Yes. I'll cover it again.

5 Wimrick is a captive reinsurance company within WMI. It  
6 is currently in a runoff today and has been in runoff frankly  
7 since around the time of the bankruptcy. It's a business that  
8 even prior to bankruptcy was not an independent reinsurance  
9 company, meaning it received all of the reinsurance policies or  
10 business it entered into from its sister company.

11 So it had no independent management. It had no  
12 independent sales force, and it really had no ability to  
13 function on a stand-alone basis, as an active reinsurer and  
14 since it has entered into no new reinsurance contracts in the  
15 last two-and-a-half to three years, it continues to operate now  
16 in principally run-off mode.

17 Q. And what is your understanding of when the majority of  
18 policies that Wimrick is reinsuring, when those were issued?

19 A. They are typically ten year policies so the most recent  
20 policies entered into right prior to the bankruptcy would take  
21 approximately ten years to runoff, and the majority would  
22 runoff by 2018 or 2019.

23 Q. Okay. Does Wimrick currently have any employees?

24 A. It does not.

25 Q. Now you mentioned that Wimrick has not written new

1 business since around September 2008. Prior to that time, can  
2 you just explain again, your understanding of how it generated  
3 business?

4 A. Yes, again as a -- not unlike most captive reinsurers, as  
5 a captive reinsurance company the substantial, in fact, all of  
6 the policies it underwrote were really policies that were given  
7 to it as part of the insurance activities entered into or  
8 engaged in by its former sister company, which was in the  
9 business of writing underlying mortgages.

10 So it had no independent source of obtaining reinsurance  
11 contracts. It solely obtained those contracts through business  
12 activities with its sister company.

13 Q. Okay. And does Wimrick currently generate income?

14 A. It does generate income.

15 Q. How does it do that?

16 A. It continues to collect as part of the management of the  
17 runoff insurance premiums, it makes payments as it is required  
18 to make under those contracts. It has some level of cost and  
19 overhead that it incurs, and assuming the revenues collected  
20 are more than costs incurred it will make some money.

21 Q. And does Wimrick have any other source of income?

22 A. Aside from the investment income it earns on the monies  
23 that it invested, it has no other principal source of income.

24 Q. Okay. Now you mentioned that Blackstone reviewed  
25 projected financial and operational data provided by the

1 debtors regarding the post-emergence reorganized WMI, can you  
2 describe generally the projections that were prepared by the  
3 debtors?

4 A. The debtors prepared, because this is a subsidiary or a  
5 business in runoff and its asset base is relatively a known  
6 quantity, Alvarez & Marsal, with the assistance of Milliman  
7 prepared a ten-year, if you will, projection of the revenues  
8 and disbursements that would be made as the contracts -- the  
9 reinsurance contracts runoff over time, and that was provided  
10 to us by Alvarez & Marsal.

11 Q. And so the fiscal years covered by the projections are  
12 approximately 2011 through 2019?

13 A. That's correct.

14 Q. Okay. What, if any, assumptions underlie the debtors'  
15 projections regarding Wimrick's post-emergence business?

16 A. Again, it's a business fundamentally built on contracts so  
17 there is a known set of contracts that the company currently  
18 has in activity, but given that the nature of the business is  
19 kind of a reinsurance and reinsurance business, the primary  
20 source of payments it will make has to do with, was driven by,  
21 in essence, actuarial assumptions based upon the performance of  
22 the underlying mortgage contacts that Wimrick actually has  
23 reinsured.

24 So the primary source, the driver of the income and  
25 disbursements really are driven by actuarial analysis prepared

1 by Milliman, the debtors' actuarial advisors.

2 Q. Okay. Did you discuss with the debtors the assumption  
3 that Wimrick would continue to operate as a runoff?

4 A. Yes, we did.

5 Q. Can you just describe those discussions briefly?

6 A. In our early due diligence we tried to understand the  
7 nature of the business and the nature of what Wimrick is, and  
8 in those discussions we've come to understand why the company  
9 was, in fact, being run as a runoff -- again because it had no  
10 independent ability to source or acquire reinsurance contracts  
11 given the nature of its prefiling operation.

12 Q. Okay. And why did the projections for organized WMI end  
13 in 2019?

14 A. Again the contracts that were entered into were in  
15 existence as of the date or around the time of filing, have a  
16 defined life, they are typically ten-year contracts. So by  
17 2019, within ten years of the filing, the last of those  
18 contracts should come to its conclusion.

19 Q. Does Wimrick generate any positive cash flow?

20 A. It does and it is projected to generate positive cash  
21 flow.

22 Q. Okay. What did the projections assume with respect to  
23 that cash flow?

24 A. The projections are assumed that because it is a regulated  
25 company, while it may generate cash flow, it's ability to

1 actually distribute those cash flows to its parent and its  
2 shareholders is largely driven in part by performance, but also  
3 by regulatory oversight and permission from regulators. But  
4 the projections do assume that over time, as cash is freed up  
5 based upon the projected performance that that cash flow will  
6 be distributed to the stake holders of reorganized WMI.

7 Q. And do you have an understanding of how the debtors'  
8 determined the amount of required reinsurance reserves in their  
9 projections?

10 A. That was based upon the advice and analysis of Milliman,  
11 who again are the independent actuarial consultants that have  
12 been employed, since I've been involved in the case.

13 Q. What diligence, if any, did you perform with respect to  
14 Milliman's actuarial analysis?

15 A. I don't profess to be an actuary, but we did have some  
16 phone conversation discussions with Milliman to understand the  
17 logic and the methodology they employed just so we had a  
18 baseline understanding of what they were assuming as time went  
19 on.

20 Q. Okay. If I could ask you to take a look in one of the  
21 binders in front of you at Debtors' Exhibits 277 through 282,  
22 the Milliman analyses, and ask if you generally recognize  
23 those?

24 THE COURT: The exhibit number again?

25 MR. MASTANDO: I'm sorry, your Honor. It's Debtors'

1 277 through 282.

2 THE COURT: Thank you.

3 A. Yes, these are copies -- not having flipped every page,  
4 but these are generally the copies of the reports Milliman  
5 would prepare in its assignment.

6 Q. And are these the reports that you reviewed and discussed  
7 with the debtors and Milliman?

8 A. Me and members of my team, yes.

9 MR. MASTANDO: Your Honor, I would like to offer  
10 Debtors' 277 through 282 into evidence.

11 MR. ARD: I'd object, Your Honor, they're hearsay.  
12 They weren't prepared by him.

13 THE COURT: Well can't an expert rely on hearsay?

14 MR. ARD: Not -- it shouldn't --

15 THE COURT: I can't --

16 MR. ARD: -- be used to prove the matter asserted.

17 THE COURT: I can't hear you.

18 MR. ARD: It shouldn't be usable for evidence for the  
19 truth of the matter asserted. He can rely on it, but tender  
20 into evidence as evidence for anything in the case --

21 THE COURT: Why are they offered?

22 MR. MASTANDO: They're offered because they're part  
23 of the materials he relied on. He's testified he received them  
24 from the debtors and Milliman, and they formed the basis for  
25 the projections. And clearly they are materials he can rely on



1 and I think there's sufficient basis to admit them into  
2 evidence.

3 THE COURT: All right. I'll admit them for that  
4 purpose only.

5 (Debtors' Exhibits 277 through 282, Milliman Reports, were  
6 hereby received into evidence)

7 MR. MASTANDO: Thank you, Your Honor.

8 BY MR. MASTANDO:

9 Q. Mr. Zelin, have the debtors' projections been updated  
10 since the last confirmation hearing?

11 A. Yes, they have.

12 Q. And can you describe generally what types of updates were  
13 made to the projections?

14 A. Yes. Since the current hearings are obviously many months  
15 after the hearings in December, they've been updated initially  
16 for actual results between then and now, to the extent  
17 available. They also reflect updated views of Milliman's  
18 actuarial analysis, and as a result the revenue has come down a  
19 little bit and the assumed payments on account of reinsurance  
20 contract losses have been adjusted upward a little bit.  
21 There's also an additional analysis that Alvarez & Marsal had  
22 prepared with respect to overhead. So the overhead has been  
23 adjusted in the projections as well.

24 And then as part of the actual results there was a  
25 litigation settlement that was entered into between December

1 and today, that's reflected in the actual cash numbers.

2 Q. Okay. And what is generally the net effect that these  
3 updates have had on the projections?

4 A. They've generally resulted in a deterioration or reduction  
5 in the cash flow projected in the Alvarez & Marsal or debtors'  
6 projections.

7 Q. Okay. And has Blackstone incorporated the updated  
8 projections into its analysis?

9 A. Yes, we have. Our June 23rd -- my June 23rd expert report  
10 is premised upon the most recent financial projections  
11 prepared.

12 Q. Okay. And if I could ask you to take a look at Debtors'  
13 Exhibit 340, it's the updated financial model underlying the  
14 valuation. I'd ask if you recognize that document?

15 A. Yes. This is a summary, this is the printout actually of  
16 the detailed model prepared by the debtors that has been  
17 provided to Blackstone.

18 MR. MASTANDO: Your Honor, I'd like to offer Debtors'  
19 340 into evidence as well.

20 THE COURT: Okay. It will be admitted.

21 (Debtors' Exhibit 340, Detailed Model Printout prepared by  
22 Debtors, was hereby received into evidence)

23 MR. MASTANDO: Thank you, Your Honor.

24 BY MR. MASTANDO:

25 Q. Mr. Zelin, did you use any other sets of projections to

1 perform your valuation of reorganized WMI?

2 A. Yes, we did.

3 Q. What other projections did you use?

4 A. Consistent with what we did back in our December or  
5 November report, we had asked the debtor for assistance in  
6 sensitizing the company's base financial projections to reflect  
7 an assumption that there would be an improved performance in  
8 the debtors' business. And what we choose to do is to adjust  
9 the financial projections and the underlying assumptions,  
10 assuming a ten percent improvement in the performance in the  
11 underlying mortgage contracts, and therefore the reinsurance  
12 contracts that reorganized WMI has, will have and what Wimrick  
13 has today. And we based part of our valuation upon those  
14 projections as well.

15 Q. Okay. If I could direct you to page 8 of Debtors' Exhibit  
16 341. Your report.

17 A. I have it in front me.

18 Q. Can you just briefly summarize what the components are of  
19 reorganized WMI's enterprise value based on this page?

20 A. Yes. The total value we have for reorganized WMI is  
21 summarized in the bottom blue line which is 135 to 185, and  
22 there are three principal components to that valuation. The  
23 top blue box, which is, has a heading called "excluding NOLs"  
24 is fundamentally our view of the value of the existing runoff  
25 portfolio of Wimrick under the assumption that it will have no

1 NOLs at all available to it, to shelter any taxable income  
2 generated during the runoff period.

3 So it assumes that Wimrick will be, reorganized WMI will  
4 be a full taxpayer based upon the projections and actuarial  
5 analyses that factored into those projections.

6 We then separately valued two components of the net  
7 operating losses. There will, I think, as there has been much  
8 testimony, there will be some significant net operating losses  
9 available to reorganized WMI upon emergence.

10 We first looked at what the value would be of those net  
11 operating losses that would be available and would be used to  
12 shelter income, the taxable income generated from the existing  
13 portfolio and that on a precedent value basis generated the  
14 value of ten to twenty million dollars.

15 So it's the sum of the top two lines that in essence gives  
16 you the full value of reorganized WMI Wimrick of the runoff  
17 portfolio itself, broken into two pieces; the base portfolio  
18 and the value of the tax shelter coming out of the NOL or the  
19 incremental cash flows generated by the use of the NOL.

20 That third yellow line, the third component of the overall  
21 valuation is our view of the value, my view of the value, of  
22 what we referred to as the corporate opportunity. What that  
23 arises from is the fact that reorganized WMI Wimrick cannot use  
24 the entirety of the net operating losses it will have available  
25 to it to shelter income on the existing portfolio.

1           So we made an assumption and looked into whether we could  
2 afford any value to the balance of the NOLs that, for which  
3 there was no income resident in reorganized WMI to apply to.  
4 And our view of the value of this third bucket, the second  
5 bucket of NOLs but the third component of value was ten to  
6 twenty-five million dollars and those three components sum to  
7 the 135 to 185 we have on the bottom of the page.

8           Q.    Okay.  And can you describe a summary of the methodology  
9 that you used to value reorganized WMI as indicated under the  
10 methodology column on page 8?

11          A.    Sure.  With respect to the top blue line, the excluding  
12 NOL line, we describe in general and then have more detail  
13 later in the report that the principal methodology that we used  
14 to value reorganized WMI or Wimrick's runoff portfolio is a  
15 discounted cash flow methodology.

16                We did consider precedent transactions but to a much  
17 lesser extent, discounted cash flow was our principal  
18 methodology and that is fundamentally present value into today,  
19 the projected cash flow streams that reorganized WMI will  
20 generate.

21                   UNIDENTIFIED SPEAKER:  Say again?

22                   THE WITNESS:  Reorganized WMI.

23                   UNIDENTIFIED SPEAKER:  Oh, thank you.

24                   THE WITNESS:  Will generate.

25          A.    The second component of value which is the NOLs and the

1 value coming out of the NOLs when the existing NOLs are applied  
2 to shelter to taxable income were principally valued, and  
3 frankly solely valued on a discounted cash flow basis, again by  
4 applying the NOLs reorganized WMI will avoid having to pay  
5 taxes through the use of the net operating losses, that  
6 generates additional cash flow and the present value of that  
7 additional flow is the ten to twenty you see.

8 And then with respect to the tax savings -- I'm sorry,  
9 this corporate opportunity, the third component of value or the  
10 second component of NOL value, that was also premised upon a  
11 discounted cash flow of an assumed level of tax savings  
12 adjusted for other risks we saw inherent in attempting to value  
13 that third component or the excess NOL.

14 Q. Now you mentioned the discounted cash flow analysis, what  
15 cash flows did you consider in the discounted cash flow  
16 analysis that you performed?

17 A. We considered two basic sets of, two basic sets of cash  
18 flow. We considered the cash flows generated under the  
19 projections provided to us by the debtors, again grounded in  
20 the Milliman actuarial analysis, but we also looked at and  
21 prepared and had prepared a second set of cash flow projections  
22 that reflected this ten percent improvement in the performance  
23 of the reinsurance contracts based upon the improved  
24 performance of the underlying mortgages, and that's what we  
25 refer to as the adjusted financial projections.

1           So we looked predominately at two sets of financial  
2 projections.

3           Q.    Okay.  And if you could take a look at page 17 of your  
4 report, it's entitled "Weighted average cost of capital", what  
5 information is this intended to reflect?

6           A.    Yes.  In the application of a discounted cash flow it  
7 fundamentally is calculating the present value of those cash  
8 flows at an assumed discount rate.  The discount rate is  
9 technically referred to as the weighted average cost of  
10 capital.

11           There are a number of methodologies; two methodologies in  
12 particular we employed in estimating the weighted average cost  
13 of capital through reorganized WMI and what is summarized on  
14 page 17 is some of the detailed analysis we prepared in looking  
15 at and using market information for two types of reinsurance  
16 and insurance companies in driving our view or our view of what  
17 the right weighted average cost of capital should be used and  
18 employed for valuing reorganized WMI.

19           Q.    And what discount rate did you apply?

20           A.    Based upon all the information available to us and some  
21 analysis and judgment that we prepared, as you'll see in the  
22 bottom yellow shaded box on the page, our conclusion was that  
23 it would make sense to present value those cash flows using the  
24 rate of thirteen to fifteen percent.

25           Q.    And can you describe how based on these charts on page 17

1 how you arrived at that thirteen to fifteen percent rate?

2 A. Yes. We looked at a number of different weighted average  
3 cost of capital factors and we applied in essence the discount  
4 rates or the weighted average cost of capitals derived in --  
5 there are two boxed sets of percentages on the bottom of the  
6 page, the top right corner of the right-hand side of those  
7 boxes, which is fundamentally a five-year average of observed  
8 information in the marketplace to come up with our weighted  
9 average cost of capital range.

10 And you can see in that box thirteen percent is somewhere  
11 in kind of the middle of that range, and we rounded or skewed  
12 the higher discounted factor up to fifteen percent to reflect  
13 our judgments based upon what acquirers of these types of  
14 portfolios might look for as a rate of return.

15 Q. And what types of companies did you determine were  
16 appropriate to include in the weighted average cost of capital?

17 A. We looked at the universe of insurance companies. We  
18 broke them into two categories; the top hand, the top five or  
19 so what we call the distressed insurers, those insurers who  
20 really suffered dramatically from the financial crisis in the  
21 last few years and then we called the diversified insurers  
22 which are a larger, better capitalized and were better able to  
23 withstand the financial crisis.

24 We didn't rely on any one company in particular but with  
25 the weighted average cost of capital technique tries to blend,



1 if you will, the universe of companies that were used in  
2 driving the factors in the analysis and we basically relied  
3 upon, in coming up with the thirteen to fifteen percent, kind  
4 of a blended five-year average for all the insurers on the  
5 piece of paper, not considering this either a distressed  
6 insurer or a diversified insurer.

7 Q. And once you have this discount rate, can you describe the  
8 next step in the discounted cash flow analysis?

9 A. Yes. Once we derive the thirteen to fifteen percent, we  
10 then apply those discount rates to the projected cash flows to  
11 be generated by reorganized WMI and I think we show that  
12 calculation on --

13 Q. Page 16?

14 A. -- page 16.

15 Q. And based on this analysis, as the title indicates, the  
16 title on the page, "discounted cash flow calculation excluding  
17 NOLs", based on this analysis what is your conclusion as to the  
18 range of values for reorganized WMI's enterprise value?

19 A. Using solely the discounted cash flow analysis our range  
20 of value was 110 to 130 million dollars.

21 Q. And how did you calculate the low end of the enterprise  
22 value excluding NOLs?

23 A. If you see, Your Honor, on the page, you'll see the  
24 reference to the financial model and then the adjusted  
25 financial model on the bottom. In each, the financial model

1 again was the model given to us by the company. The adjusted  
2 financial model reflects the incorporation of the ten percent  
3 improvement in performance.

4 For purposes of calculating the lower end of the range, we  
5 looked at applying the fifteen percent weighted average cost of  
6 capital discount factor to the financial model which shows a  
7 lower projected cash flow stream, and you'll see that five  
8 lines down from the top of the page you'll see the present  
9 values and the various amounts of cash flows that will be  
10 generated, coming to a 109 million dollar number.

11 So we used the lower projected cash flow stream and  
12 applied the higher discount rate to get to the low end of our  
13 valuation range.

14 Q. Okay.

15 A. And similarly with respect to the high end of our  
16 valuation range of 130 million dollars we again applied the  
17 thirteen percent discount factor, of the lower discount factor,  
18 therefore meaning a higher present value. We applied the lower  
19 discount factor to the adjusted cash flow projections and to  
20 get a sense of the impact of the adjustments you can just  
21 compare the projected dividend streams on the top of the page  
22 to the projected dividend streams midway through the page.

23 You can see they're a little bit higher so we have a  
24 higher set of cash flows reflecting the improved -- the  
25 assumption of improved performance and that gave rise to a 128

1 million dollar number which formed the 130 million dollar  
2 conclusion with respect to the high end of our valuation range  
3 on a discounted cash flow basis.

4 Q. Okay. And what weight did you assign to the discounted  
5 cash flow analysis?

6 A. We gave that analysis substantially all our weight in  
7 valuing reorganized WMI, we did consider precedent transaction  
8 analysis to a certain extent but it was predominantly  
9 discounted cash flow analysis.

10 Q. And why did you assign the most weight to the DCF  
11 analysis?

12 A. Because in precedent transaction analysis you're trying to  
13 go back into the marketplace and identify transactions,  
14 acquisitions of similar type portfolios in similar financial  
15 condition, done at or around a similar economic time. And we  
16 went back and looked to, no surprise given the financial crisis  
17 that ensued over the last few years, there really haven't been  
18 many transactions and acquisitions of reinsurance companies,  
19 let alone mortgage reinsurance companies in the last few years  
20 because the inherent uncertainty that the market assumes exists  
21 in these portfolios. So to find any type of precedent  
22 transaction that one could look at you had to go back as early  
23 as ten years and certainly the majority of them took place in  
24 the early part of the last decade.

25 So we saw nothing that was recent, let alone anything that

1 was comparable that we felt comfortable relying upon in  
2 utilizing the precedent transaction analysis.

3 Q. Okay. And if you turn to page 23 of your report, does  
4 that show what you considered in the precedent transaction  
5 analysis that you were just describing?

6 A. It does, yes.

7 Q. And can you just briefly describe the approach as outlined  
8 here on the page?

9 A. Yes. Similar to a comparable company analysis you look  
10 for precedents that are somewhat relevant to the company you're  
11 attempting to value. So our targets as we see here were kind  
12 of reinsurance portfolios or businesses and we also tried to  
13 identify transactions that were of comparable size. In order  
14 to get a meaningful level of data we took the size up to 700  
15 million dollars in terms of total size.

16 And if you see the list we broke the precedent  
17 transactions into two components, what we call runoff  
18 precedents which were acquisitions of reinsurance companies  
19 that were in runoff much like reorganized WMI. And then we had  
20 to go as far as back as, you can see the announced statement  
21 completion date to 1998 to 2000 to find any going concern  
22 precedents of similar transactions. So those would be  
23 companies that were actually functioning as a going concern.

24 And we looked at the universe of these transactions and  
25 given, again, as I testified before, when you look at the dates

1 most of these occurred from 2003 to 2008, early 2008 when it  
2 comes to the runoff precedents but certainly they all occurred,  
3 except for the first one on the top, before the financial  
4 crisis.

5 Q. And which of these transactions did you include in your  
6 precedent transaction analysis?

7 A. Again because our conclusion was that reorganized WMI and  
8 it was predominately going to be, its assets were going to be  
9 the runoff reinsurance portfolios we discussed earlier, we  
10 relied predominately on the multiples that we drove out of the  
11 runoff precedents and that range is approximately point seven  
12 to one times. And we applied that point seven to one times  
13 multiple as you see in the left yellow shaded box on the page,  
14 we applied that point seven to one times to the projected book  
15 value of reorganized WMI's book equity to come to a value under  
16 the precedent transaction analysis of 144 to 206 which we've  
17 rounded for simplicity 145 to 205.

18 Q. If I could ask you Mr. Zelin to turn to page 13 of your  
19 report. What does this page show as to your ultimate  
20 conclusion as to the reorganized WMI's estimated enterprise  
21 value range excluding net operating losses?

22 A. And so you'll notice here we've just summarized the two  
23 methodologies we employed, the discounted cash flow methodology  
24 which gave rise to the 110 to 130 million dollar number and the  
25 precedent transaction analysis that we just discussed which

1 gave rise to the 145 to 205 million dollar range. And our  
2 recommended range is 115 million dollars to 140 million dollars  
3 which was that first blue box we saw on page 8 of the report.

4 And as you can see based upon our concluding the 115 to  
5 140 valuation range, we gave substantial weighting to the  
6 discounted cash flow analysis with a little bit of recognition  
7 that while there have been no acquisitions of reinsurance  
8 companies, let alone mortgage reinsurance companies in the last  
9 few years because of the perceived risk in the asset base, we  
10 skewed our discounted cash valuation range slightly towards the  
11 low end of the precedent transaction range.

12 And again because we did not find any precedents that were  
13 of any comparability, and in concluding based upon our review  
14 of those transactions, the DCF really gave us an inherent view  
15 of the intrinsic value of the asset, really the value of the  
16 cash flow generating capability of the asset based upon the  
17 methodology.

18 Q. And if you take a look at page 14 of your report it says  
19 valuation approach?

20 A. Yes.

21 Q. And then the last item on the page under approaches it  
22 lists discounted cash flow, precedent transactions, and  
23 comparable companies, what's the comparable company analysis?

24 A. Not dissimilar in style but different in substance,  
25 comparable company analysis is a way of valuing a company based

1 upon reference to how public companies trade in the marketplace  
2 today. And when we looked at the universe of public companies  
3 that trade in the marketplace today, no surprise, there were no  
4 runoff reinsurance portfolio companies in the marketplace that  
5 were trading publicly.

6 There were some that were of comparable size to Wimrick.  
7 There are some distressed insurers that are trading in the  
8 marketplace today like PMI, Majick (ph), Genworth, which are  
9 themselves in runoff, but they're much larger and have a much  
10 broader portfolio.

11 And then, of course, you have these diversified insurers  
12 like Met Life and Prudential and Torchmark (ph) which don't  
13 feel like they're very comparable to the assets we're valuing  
14 here. So while we did look at a comparable company analysis,  
15 we did not employ that methodology at all just given the size  
16 and nature of what reorganized Wimrick will be -- reorganized  
17 WMI will be.

18 Q. Now let's discuss your valuation of the net operating  
19 losses potentially available to reorganized WMI.

20 A. Okay.

21 Q. If I could direct you to page 26 of your report, please.

22 A. I'm here.

23 Q. I think you said earlier that in the second step of the  
24 valuation you calculated the present value of the NOLs  
25 potentially available to shelter the existing portfolios'

1 projected taxable income.

2 A. Yes.

3 Q. And taking a look at page 26, what net operating losses  
4 did you assume were available to reorganized WMI?

5 A. Excuse me. Based upon the information that was provided  
6 to us, and I believe included in the disclosure statement as  
7 well, we assumed that and I think subject to testimony earlier  
8 this morning, there was an assumption that there would be  
9 approximately five-and-a-half billion dollars of net operating  
10 losses, gross net operating losses available to reorganized  
11 WMI.

12 Q. Okay. And what is your understanding of potential net  
13 operating losses other than those listed in your report?

14 A. Based on our diligence I understand there are, and this  
15 may have been disclosed as well, but there is some potential  
16 for those net operating losses to increase from two primary  
17 facts; one, is that there may be payments to be made pursuant  
18 to the plan that have not factored into the calculation of the  
19 five-and-a-half billion dollars; and there also might be an  
20 increase, if you will, in that operating losses resulting from  
21 the global settlement agreement.

22 The combination of those two buckets may add another four  
23 billion or so of potential net operating loss available to  
24 reorganized WMI.

25 Q. And how would those additional net operating losses effect



1 your valuation?

2 A. Given the methodology we employed, they would not have any  
3 impact on our valuation.

4 Q. Now which tax provisions --

5 A. Not -- sorry. No impact on our valuation.

6 Q. Which tax provisions do you understand would impact the  
7 ability of reorganized WMI to utilize net operating losses?

8 A. There are two basic provisions that we focused on in our  
9 valuation analysis, and again I think the subject of much  
10 testimony this morning; one is Section 382 and the other is  
11 Section 269.

12 Q. Okay. And what is your understanding of why Section 382  
13 could apply to the net operating loss?

14 A. Pursuant to the plan we will have an ownership change and  
15 based upon my understanding of 382 that ownership change will  
16 occur pursuant to a subsection called 382(L)(6). And my  
17 understanding of 382(L)(6) is that that results in essence a  
18 proration of the net operating losses to what I refer to, and I  
19 think others refer to, as a pre-change period and a post-change  
20 period under the assumption that the plan will be effective on  
21 August 31st.

22 The pre-change period will be in essence eight months out  
23 of the year, eight out of twelve months. The post-change  
24 period will be four months. I think it's actually measured in  
25 days, but I'm just using months for simplicity, and as a result

1 approximately two thirds of the five-and-a-half billion dollar  
2 NOL will actually be a pre-change NOL, and approximately one  
3 third of four out of twelve months of the NOL of 1.8 billion  
4 dollars will be a post-change NOL, just based upon a straight  
5 proration. Assuming an August 31st effective date.

6 Q. Okay. Now how did you calculate the present value of the  
7 net operating losses sufficient to shelter the existing  
8 portfolios taxable income?

9 A. And this is something that is not uncommon in most  
10 reorganizations when there will be attributes that will  
11 survive, as I testified I believe there will be some taxable  
12 income generated by reorganized WMI by virtue of the operation  
13 of the runoff. Reorganized WMI will have a sufficient amount  
14 of NOL available to it, and we assume for purposes of valuing  
15 the NOL that all of the taxable income that will be generated  
16 by the portfolio will be sheltered by the net operating losses  
17 available to reorganized WMI such that as a result reorganized  
18 -- it's a tongue twister -- reorganized WMI will not have to  
19 pay taxes and the avoidance of those tax payments will result  
20 in greater cash flows, and those greater cash flows give rise  
21 to greater value.

22 And as I testified earlier the present value of those tax  
23 savings we estimated at ten to twenty million dollars.

24 Q. Okay. And if I could direct you to page 28 of your  
25 report. Does that page show your calculation of the discounted

1 cash flows, including net operating losses?

2 A. Yes. Using the same exact methodology we discussed  
3 earlier, I believe, on page 16, we applied the same thirteen to  
4 fifteen percent discount rates to the projected dividend  
5 streams or distributions under both a financial and the  
6 adjusted financial models, applying the fifteen percent to the  
7 lower level of cash flows and the thirteen percent discount  
8 rate to the higher adjusted level of cash flows.

9 And under the same approach, same methodology, just using  
10 the cash flows that include the benefit of the NOLs, we come to  
11 a valuation range of 120 to 150 on a DCF basis. And given our  
12 valuation excluding the NOLs, as I testified earlier, was 110  
13 to 130 the straight mathematical difference between the two  
14 present value computations, one excluding NOLs and one  
15 including the benefit of the NOLs, gives rise to the ten to  
16 twenty million dollar different.

17 And that is the value we ascribed to the net operating  
18 losses that will be used to shelter to income generated from  
19 the existing portfolio.

20 Q. And if you turn back to page 8 of your report, is that the  
21 range reflected on page 8?

22 A. Yes. We've already covered the 110 to 130 which is the  
23 value of the portfolio -- I'm sorry, 115 to 140 which is the  
24 value of the portfolio excluding NOLs, the next bucket that  
25 I've described earlier, ten to twenty is what we just discussed

1 a few minutes ago.

2 Q. Okay. And if I could now direct you, please, back to page  
3 26 of the report. If you look at the bottom of page 26, what  
4 amounts of the net operating losses is assumed to be used for  
5 the purpose of generating that ten to twenty million dollars of  
6 value that you just discussed?

7 A. It's approximately, this is a midpoint number, but it's a  
8 range with a midpoint being approximately seventy million  
9 dollars. So we would need to employ sixty to eighty -- fifty  
10 to ninety million dollars of net operating losses, midpoint  
11 seventy, in estimating the value of the tax savings through the  
12 application of the NOLs to the existing portfolio.

13 Q. Okay. Now did you determine whether there was any  
14 additional value to the net operating loss beyond the ten to  
15 twenty million dollars you've just testified about?

16 A. Well it wasn't lost on us that if the existing portfolio  
17 only needed midpoint seventy million dollars of net operating  
18 losses to shelter its projected taxable income that that number  
19 was meaningfully less than the five-and-a-half billion dollars  
20 of NOL that before any outside opportunities, as I testified  
21 earlier, that there may be and we should look at whether there  
22 will be incremental value that could be generated by  
23 reorganized WMI's use of the NOLs that based upon the existing  
24 asset base it cannot use.

25 And we did attempt to value those net operating losses.

1 Q. And what did you do to attempt to do that?

2 A. Well we came to the conclusion, and we refer to this as  
3 the corporate opportunity -- we came to the conclusion that the  
4 only way, and I think others have come to similar conclusions,  
5 the only way you can actually create value in the use of the  
6 NOL is to go out and bring additional taxable income into  
7 reorganized WMI beyond, again, the taxable income currently  
8 generated by the existing portfolio.

9 That taxable income doesn't exist today. There are no  
10 other assets that are generating taxable income. So one has to  
11 make the assumption, as a starting point, not as an ending  
12 point, but as a starting point, that reorganized WMI will raise  
13 money and use that money to go acquire additional income  
14 taxable income producing assets. And then employ its net  
15 operating losses to shelter that taxable income for purposes of  
16 valuing the NOL.

17 Q. Okay. And now are you opining that capital will, in fact,  
18 be raised?

19 A. I'm not opining that capital will be raised and we take  
20 that risk into consideration.

21 Q. Now how did you determine what amount of capital could be  
22 raised?

23 A. Well we basically look at, in essence, the risks inherent  
24 in raising that capital. And today, as reorganized WMI itself  
25 is not an ongoing, you know, reinsurance operator that is

1 writing new policies, it would have to go out and make  
2 acquisitions. It would have to, in essence, raise capital. It  
3 doesn't have a management team, no offense to my client, it  
4 doesn't have a management team that can execute on those  
5 transactions, it does not have a business plan, it does not  
6 have the infrastructure in place to employ capital for purposes  
7 of making those kinds of acquisitions.

8 So you would have to, I don't want even say restart since  
9 its historical operation as a captive within -- WMI was as a  
10 captive and it never had the ability to generate reinsurance  
11 policies of its own, you'd have to basically create something  
12 brand new that never before existed on a stand-alone basis.  
13 And all those risks are risks that we considered in estimating  
14 the value of what the NOL is.

15 In addition there is, as I've come to learn, significant  
16 tax risk that one also has to consider in estimating the dollar  
17 amount of NOLs that we could assume would be raised before the  
18 tax risks become so large that it's hard to put a value on the  
19 benefits of raising that much more capital because the risks of  
20 raising more capital far outweigh the theoretical benefits that  
21 come from raising that much capital.

22 And taking into consideration all those risks that was the  
23 two things that we looked at, and those were the things that we  
24 looked at in estimating the value.

25 Q. And is the second piece of the risk you're referring to,

1 is that related to Section 269?

2 A. Yes, that is what we call the 269 issue.

3 Q. And what is your understanding of that issue of what  
4 Section 269 does?

5 A. Because it is a complex, not that tax law isn't complex in  
6 general, because it is a complex issue we went and retained,  
7 early on in the case, the law firm of Willkie Farr, Mr. Rick  
8 Reinhold in particular, who just testified a few minutes ago in  
9 the courtroom. We went out and retained our own counsel who  
10 could advise us on what Section 269 risks are and how we might  
11 want to incorporate those risks into our valuation.

12 In its simplest form what Section 269 does and this is  
13 written into our disclosure statement, I think I've heard it  
14 mentioned in court today, it really is meant to protect against  
15 the trafficking of net operating losses, you know, for purposes  
16 of just utilizing NOLs or transferring NOLs for the benefit of  
17 the acquirer.

18 More technically there are really fundamentally, as we  
19 understand it, two elements of Section 269, this may be a  
20 little repetitive to Mr. Reinhold's testimony, but you first  
21 have to have an acquisition of control.

22 And in our analysis and in our discussions with Willkie  
23 Farr we, in fact, do have an acquisition for control, and that  
24 acquisition for control is the acquisition by the creditors of  
25 the stock in reorganized WMI pursuant to the plan. And that is

1 the acquisition of control we focused ourselves and in our  
2 conversations with Willkie Farr, and that is the acquisition  
3 that in essence triggers or is the first stage of Section 269  
4 risk.

5 The second stage has to be once you've had that  
6 acquisition that the principal purpose of that acquisition, as  
7 it's been explained to me and as I think as Mr. Reinhold has  
8 testified, the principal purpose of that acquisition has to be  
9 for the avoidance of taxes.

10 MR. ARD: I'd like to object to the last answer to the  
11 extent that he's testifying to what 269 means. He's not  
12 qualified as a tax expert. If he's simply testifying to what  
13 he assumed to be true about the tax laws, fine. But he's not  
14 qualified to opine on the meaning of 269. So I'd object to  
15 that extent.

16 MR. MASTANDO: Well I think it's neither, Your Honor.  
17 He's testifying as to the advice he was given by counsel and  
18 the purpose for which they were retained, is my understanding.

19 THE COURT: All right. But we've heard what counsel  
20 told him do we need to have him repeat it?

21 MR. MASTANDO: No, I'm just trying to establish the  
22 background.

23 THE COURT: All right.

24 MR. MASTANDO: Thank you, Your Honor.

25 BY MR. MASTANDO:



1 Q. And so how did your understanding of the Section 269 issue  
2 impact the amount of capital that you determined could be  
3 raised by reorganized WMI?

4 A. Again, it was clear to us that the only way one can  
5 actually get at or attempt to use the excess NOL and put a  
6 value on it is to assume capital is raised, that capital is  
7 used to acquire additional tax income producing assets and then  
8 a shelter that income with the NOLs.

9 Given the descriptions of 269 and as I understand it's a  
10 very fact intensive test based upon the facts and circumstances  
11 -- actually a subjective test for which objective factors are  
12 considered and the facts and circumstances of any individual  
13 situation weigh heavily into how one evaluates 269, based upon  
14 the advice of counsel and the facts and circumstances that we  
15 saw today in our discussions with counsel, is that in order to  
16 insure that it was more likely than not that a subsequent  
17 challenge by the IRS as to that investment that was made and  
18 the acquisition post-emergence of assets for which the existing  
19 NOL would be used, in order to get an opinion -- I'm sorry.  
20 I'll start over.

21 UNIDENTIFIED SPEAKER: Could you slow down a little  
22 bit.

23 THE WITNESS: Sure.

24 A. In order to get an opinion that it was more likely than  
25 not that any subsequent investment of capital, with that

1 capital being used to acquire new income producing assets for  
2 which then the NOL could be used to shelter and avoid cash  
3 taxes or tax payments on account of those assets acquired, in  
4 order to get an opinion that it was more likely than not that  
5 the courts would not find that the principal purpose of the  
6 acquisition for control was the avoidance of taxes, it was best  
7 to limit the assumed amount of new investment to the value of  
8 the non-tax assets that reorganized WMI will emerge with.

9 Q. And what was your understanding of the consequences of the  
10 IRS determining that the principal purpose of the creditors'  
11 acquisition of stock under the plan was to take advantage of  
12 the NOLs? What was the consequence as you understood it  
13 potentially?

14 A. The complete, as I understood it, the complete  
15 disallowance of the ability of reorganized WMI to utilize those  
16 NOLs, and that would not only be the disallowance of their  
17 being utilized to shelter the income that was just acquired  
18 through acquisition, but it could also disallow or might also  
19 disallow the use of the NOLs in sheltering the income generated  
20 by the existing portfolio that existed on the date WMI emerges  
21 from bankruptcy.

22 Q. Okay. And what facts and circumstances did you consider  
23 based on your discussions with counsel as indicia of an intent  
24 to avoid taxation by the creditors acquiring stock pursuant to  
25 the plan?

1 A. We looked at what --

2 MR. ARD: I just want to propose the same objection.

3 THE CLERK: What's your name, sir?

4 MR. ARD: I apologize. Seth Ard, Susman Godfrey, on  
5 behalf of the equity committee.

6 MR. MASTANDO: Your Honor, it's the same point. It's  
7 the discussions he had with counsel that form the basis for  
8 this portion of his report that he's relying on. That's why  
9 Mr. Reinhold testified, and now he's testifying --

10 THE COURT: And why are we hearing it twice, really?

11 MR. MASTANDO: Just so we can put it in the context of  
12 his report. It's just that question on it, Your Honor.

13 THE COURT: All right. You can answer it.

14 MR. MASTANDO: Thank you, Your Honor.

15 THE WITNESS: We looked at what reorganized WMI will  
16 be, which is a reinsurance runoff. It is not by itself a  
17 business that one needs to acquire for purposes of being in the  
18 reinsurance business. It offers no unique reinsurance  
19 technology, no management team, no intellectual property that  
20 makes this a great platform to enter into the reinsurance  
21 business.

22 And when we looked at the value of the underlying  
23 assets relative to the potential benefits that one could derive  
24 from the use of the net operating losses, that relationship was  
25 a factor that we discussed with counsel and considered. We

1 looked at the fact that the share -- the soon to be  
2 shareholders were active participants in the negotiation of the  
3 plan and structured the plan as also another important factor.  
4 And then those were the two primary factors -- three primary  
5 factors that we considered.

6 BY MR. MASTANDO:

7 Q. Now, why did Blackstone assume that reorganized WMI could  
8 potentially raise new equity, as opposed to another form of  
9 capital?

10 A. In an attempt to drive the largest value we could with  
11 respect to the NOLs, if reorganized WMI actually raised debt,  
12 that debt would actually have an interest cost, as an example.  
13 That interest cost in and of itself is a tax yield, and we  
14 didn't think that that would result in the need to use a  
15 significant amount of NOL to shelter the income that would be  
16 generated by the debt-financed acquisition.

17 So by the use of equity, which doesn't have a tax yield  
18 associated with it, we were able to employ and maximize the  
19 amount of NOL that we would need to use for purposes of valuing  
20 the net operating loss.

21 Q. Okay. And if I could direct you to page 37 of your  
22 report, Mr. Zelin.

23 A. Yes.

24 Q. It's entitled future corporate opportunity continued.  
25 Referring to this page, how much new capital did you assume

1 could be raised?

2 A. We assumed a range of -- a midpoint of 127.5 million  
3 dollars.

4 Q. And that's the midpoint of the 115 to 140 million dollar  
5 range?

6 A. The midpoint of our value, excluding any application of  
7 net operating losses, that's correct.

8 Q. Okay. And did you make any assumptions about who would  
9 make an equity investment in reorganized WMI?

10 A. The only assumption we made is that whatever equity  
11 investment got made would not trigger a subsequent change of  
12 control that would then therefore limit what is now anticipated  
13 to be unlimited -- unrestricted net operating losses.

14 Q. Okay. And after determining that reorganized WMI could  
15 potentially raise 127.5 million dollars in new equity capital,  
16 what did you do next to value the corporate opportunity NOL?

17 A. We assumed it generated a range of income streams at eight  
18 to twelve-and-a-half percent. Those income streams, absent the  
19 NOL, would result in tax payments. Those tax payments were,  
20 you know, three million and growing, depending upon whatever  
21 income stream we could generate. And therefore, by employing  
22 the NOL to shelter those tax payments, in essence the value we  
23 ascribed to the NOL as a starting point was, again, the present  
24 value of the tax savings generated by tax payments that were  
25 avoided through the use of the net operating loss.

1 Q. Okay. And then after determining the rate of return what  
2 were the next steps?

3 A. The present -- we had to apply, like we do in a  
4 traditional discounted cash flow factor, once we calculate a  
5 stream of tax savings, we have to present value those tax  
6 savings back. Then we present value those tax savings back at  
7 a twenty-five to thirty-five percent cost of equity discount  
8 rate to drive the present value of the assumed utilization of  
9 the NOLs.

10 Q. And why did you apply a twenty-five percent to thirty-five  
11 percent discount rate to determine the present value of the  
12 assumed tax savings?

13 A. One, in evaluating the value of any tax shield, applying  
14 the cost of equity is traditional from the methodology  
15 standpoint. Two, and more importantly, since the relative  
16 attractiveness of making an investment in reorganized WMI was  
17 not owning -- was not because of the fundamental assets one was  
18 acquiring, but because the attractiveness was the utilization  
19 of NOLs and because this was in essence going to be a startup  
20 of a brand new company, not a restart of an existing company,  
21 we -- based upon our judgments, we thought investors who would  
22 look to make this kind of investment would look to get equity  
23 returns out of the savings -- tax savings of twenty-five to  
24 thirty-five percent.

25 Q. Now, after applying the twenty-five percent to thirty-five

1 percent range of discount rates, what is the present value of  
2 the assumed tax savings?

3 A. As a starting point, the present value, as we summarize in  
4 the bottom right of the page, is a low end of 15 million  
5 dollars and a high end of 45 million dollars.

6 Q. And were any other discounts applied to the present value  
7 of the assumed tax savings?

8 A. Yes. The 15 to 45 assumes as a starting point that that  
9 capital raise will occur as of the effective date. The  
10 investments will get made as of the investment date and begin  
11 to generate income from the effective date going forward.  
12 Because we know that that's likely not going to happen and  
13 because of all the other risks that I've described that we took  
14 into consideration, the lack of a management team, the lack of  
15 any plan, the lack of any evidence, but there will be this  
16 capital raised, we applied an adjustment to reflect the fact  
17 that in essence, this value is nothing more than an option  
18 value that, you know, given all the uncertainty about actually  
19 going out and executing on the capital raise and making use of  
20 the NOLs, and the fact that there is still some task risk  
21 inherent, there's no guarantee that 269, even at this level,  
22 will be challenged by the IRS, we adjusted downward our values  
23 to come to a net range of 10 to 25 million dollars.

24 Q. And if you just flip back to page 35 of your report, can  
25 you just describe -- I know you already have in part -- the

1 risks that you took into account with respect to the corporate  
2 opportunity?

3 A. Again, this is very similar to what I've testified to.  
4 There is no management team and there is no infrastructure in  
5 place to do this. The nature of their historical business was  
6 one that could not generate reinsurance assets on its own, so  
7 in essence this is a startup of a brand new business. We had  
8 no evidence that there, in fact, will be this capital employed,  
9 or that there are, in fact, acquisitions that can be made at  
10 this level that will generate additional income. And then just  
11 the overall risk that, you know, this asset in and of itself is  
12 not such a unique asset that one would want to own it, other  
13 than in the context of making use of or trying to obtain the  
14 benefit of the net operating losses.

15 Q. Now, would your value of the corporate opportunity change  
16 if you assume that reorganized WMI were a public company?

17 A. It would not change materially. The issues of capital  
18 raise would be the same whether it was a public company or a  
19 private company in that the amount of capital raise that we  
20 would assume would not change. It would still be limited to  
21 the value of the principal non-tax assets. And I've seen  
22 public companies that had trouble raising capital. I've seen  
23 private companies that have had, you know, excellent ability to  
24 raise capital. The real issue is how much capital can be  
25 raised, and it's limited for the reasons we discussed.



1 Q. Okay. Now, if I could ask you to flip back to page 8 of  
2 your report, have you now covered the pieces of your  
3 recommended value range for the total enterprise value of  
4 reorganized WMI?

5 A. Yes. The last piece we just covered was the value of the  
6 NOL in this corporate opportunity scenario, and that's the  
7 third component that gives rise to the overall 135 to  
8 185 million dollar valuation.

9 Q. Okay. Now, did Blackstone consider a corporate  
10 opportunity in its November 23rd, 2010 report?

11 A. We did. It wasn't called that, but we did have a similar  
12 value in our prior valuation.

13 Q. If you can take a look at Debtor's Exhibit 151, which I  
14 believe should be in front of you.

15 A. I do have it in front of me.

16 Q. If you take a look at page 76 --

17 A. I'm sorry. The numbers are somewhat cut off on my copy.

18 Q. Yeah. I think it's page 29 of your report. It might be  
19 page 76 of the exhibit.

20 A. I believe I have it, yes.

21 Q. How do you compare the value of the corporate opportunity  
22 in your November report to your June report?

23 A. There's a little bit of uniqueness to this, in that in  
24 December the assumption was that reorganized WMI would emerge  
25 from bankruptcy during the last week to ten days or so of the

1 fiscal year. So from a proration standpoint, the substantial  
2 majority of the net operating losses were actually going to be  
3 pre-change losses, because the proration was for 355 out of 365  
4 days or so. And there would be very, very little unlimited NOL  
5 or post-change NOL available to reorganized WMI.

6 So like the current valuation, we were able to shelter the  
7 taxable income generated by the then-existing portfolio through  
8 the use of this unlimited NOL, and that's the top number of 15  
9 to 25 million dollars. But given the timing of emergence, once  
10 we used the unlimited or unrestricted NOL to shelter income,  
11 the post-change NOL to shelter income from the existing  
12 portfolio, there was not much, if any at all, unrestricted NOL  
13 left and available to reorganized WMI.

14 So all we effectively had in evaluating the corporate  
15 opportunity was the assumption that the max amount of NOL that  
16 could be used on an annual basis would be the pre-change or  
17 NOLs limited pursuant to 382 L6. So the income stream we  
18 assumed was effectively the use of the few million dollars a  
19 year of restricted NOL, and that gave rise to the 5 to 10  
20 million dollar range. So it was in essence the employment of  
21 capital post-emergence, but because the NOLs available were  
22 severely restricted, it gave rise to a lower valuation.

23 Q. Okay. Well, you now calculate approximately two billion  
24 dollars in non-limited NOLs. Why is the value of the corporate  
25 opportunity not substantially greater as compared to your

1 November report?

2 A. The fundamental premise of the corporate opportunity is,  
3 is the execution risk around being able to raise the capital.  
4 We spoke about a number of execution risks, lack of a  
5 management team, nature of the business, the availability of a  
6 portfolio to acquire -- a similar portfolio to acquire, but we  
7 also spoke about this 269 risk.

8 And while there is significant unlimited NOL available in  
9 the current formulation of the plan, it's that relative  
10 analysis of the size of the NOL relative to the value of the  
11 existing business that caused us to consider Section 269 in our  
12 discussions and based upon advice of counsel, to consider 269  
13 to limit the dollar amount or the size of the investment that  
14 we should assume in valuing the corporate opportunity or making  
15 use of this unlimited NOL.

16 So while there are, in fact, large NOLs available that are  
17 unlimited, for purposes of valuing those NOLs, understanding  
18 their existence, for purpose of putting a value on them, given  
19 all the risks that we identified, including 269 and execution,  
20 we limited the assumed investment to the 127. And by  
21 definition, as a result the values didn't -- they moved upward,  
22 but they didn't move up materially based upon the fact that we  
23 do have a significant NOL available here on an unrestricted  
24 basis.

25 Q. Now, Mr. Zelin, can you tell me, have you read the expert

1 reports prepared by Mr. Anderson?

2 A. I do -- I did.

3 Q. And did you read his deposition transcript?

4 A. I did, yes.

5 Q. Do you agree with the assertion in his second supplemental  
6 report that you imposed a per se limitation on account of  
7 Section 269?

8 A. I do not agree that that's what we did.

9 Q. Why not?

10 MR. ARD: Excuse me. Your Honor, Mr. Zelin and  
11 Mr. Maxwell had submitted simultaneous reports. Neither one of  
12 them submitted a supplemental report critiquing each other. I  
13 have no objection to his critiquing or talking about Ander's  
14 (sic) report right now, but I just want to make sure it's a  
15 two-way street.

16 MR. MASTANDO: I asked him about Mr. Anderson's  
17 report.

18 MR. ARD: Oh, I apologize.

19 MR. MASTANDO: Sure.

20 MR. ARD: But the same point.

21 THE COURT: All right.

22 MR. MASTANDO: Well, but Mr. Anderson submitted a  
23 supplemental report criticizing Mr. Zelin. So --

24 MR. ARD: And he didn't --

25 MR. MASTANDO: -- and it's not the same point, and I'm

1 entitled to ask him about it, I believe.

2 MR. ARD: Well, that's fine, but he didn't file a  
3 supplemental report after that.

4 THE COURT: I don't think it matters. He can --

5 MR. ARD: That's fine.

6 THE COURT: -- criticize another expert's report. Go  
7 ahead.

8 MR. MASTANDO: Thank you, Your Honor.

9 BY MR. MASTANDO:

10 Q. So I'm sorry, Mr. Zelin.

11 A. I forgot what --

12 Q. I did too. Do you agree with Mr. Anderson's second  
13 supplemental report in which he asserted that you imposed a per  
14 se limitation on account of Section 269?

15 A. I don't agree with that assertion.

16 Q. Why not?

17 A. In coming in and evaluating the application of 269, we  
18 didn't say the law says or the code says you can only invest  
19 that amount. What we did is we looked all the facts and  
20 circumstances that I've already testified to, and I think  
21 Mr. Reinhold testified to, all the facts and circumstances  
22 surrounding this specific instance, including the risk of the  
23 IRS or a court might find if a subsequent investment into  
24 reorganized WMI were too large, that the court might find that  
25 the acquisition of control pursuant to the plan had as its

1 principal purpose tax avoidance.

2 And the way we attempted to capture that risk and, in  
3 essence, be able to solicit or get a more than likely -- more  
4 than -- more likely than not -- sorry, more likely than not  
5 opinion that the acquisition for control pursuant to the plan  
6 was not tax avoidance was to, in essence, limit the size of the  
7 new investment to the value of the non-tax assets. Because  
8 then when one looks at the total value of reorganized WMI, at  
9 least half of that value will be in the existing assets and not  
10 in the newly acquired assets.

11 Q. Okay. And do you agree with Mr. Anderson's assumption  
12 that you were looking at a subsequent acquisition of control?

13 A. I'm not sure I understand the question.

14 Q. Well, Mr. Anderson assumed that you were looking at a  
15 subsequent acquisition of control, correct?

16 A. No. In our -- yeah, yeah, in our discussions -- I  
17 understand that one. In our discussions with Willkie, the --  
18 whether there was a 269 risk specific solely to that subsequent  
19 acquisition was really not relevant. And I know Mr. Anderson  
20 talks a lot about that. But that was really not relevant to  
21 the analysis.

22 What was relevant to the analysis was whether the facts  
23 and circumstances, including the fact that there was a  
24 subsequent raise of capital, the purpose of which was to  
25 acquire assets such that reorganized WMI, having been acquired

1 in a control transaction, would use the net operating losses to  
2 shelter the income in that subsequent acquisition. That's the  
3 269 risk that from our perspective really mattered. I don't  
4 think the advice received from Willkie as to whether there was  
5 a unique 269 risk in a subsequent acquisition was relevant to  
6 the analysis of the 269 risk that exists pursuant to the  
7 acquisition of control under the plan.

8 Q. Okay. Now, let me just ask you briefly, have you read the  
9 residual Washington Mutual Inc. valuation critique prepared by  
10 Mr. Maxwell of Peter J. Solomon?

11 A. I did, yes.

12 Q. Have you read the deposition transcript of Mr. Maxwell?

13 A. I have, yes.

14 Q. Okay. Have you identified any significant similarities  
15 between your evaluation of reorganized WMI and Mr. Maxwell's  
16 critique?

17 A. Yes. I think there are two fundamental similarities that  
18 we noticed in his valuation critique, excuse me, and our  
19 valuation report. As to the base business itself, which we  
20 valued excluding the corporate opportunity, as to the base  
21 business itself, I think our valuations were actually very  
22 similar. I think his range was 129 to 135 million dollars.  
23 And you can see our range listed on page 8 of my report,  
24 leaving aside the corporate opportunity, was 125 to 160.

25 So he was actually a little bit on what we think is an

1 apples-to-apples basis slightly lower than our valuation. Then  
2 that was the one similarity I noticed. And I think in his  
3 deposition he stated we think Blackstone's valuation is  
4 appropriate.

5 Q. And have you identified any other similarities between  
6 your valuation and your Mr. Maxwell's critique?

7 A. Yes. He also comes to the conclusion, which I think  
8 everyone else has come to, which is that in order to then --  
9 given the existing portfolio cannot generate enough taxable  
10 income to use any meaningful amount of the NOLs that  
11 reorganized WMI will have available to it, he assumes that in  
12 order to generate value in that net operating loss you have to  
13 make significant and sizable investments where you have to  
14 actually invest money to make an acquisition that brings  
15 taxable income into the company so the NOL can be used.

16 Q. And is that the unique opportunity presented by  
17 reorganized WMI?

18 A. I think, frankly, from the standpoint of our view of the  
19 business, the only real unique asset this company has is its  
20 net operating loss, yes.

21 Q. Do you have any critiques of Mr. Maxwell's report?

22 A. I do. I think in coming up with a -- well, I'm not even  
23 too sure, other than the 129 to 135, he's actually valued these  
24 other acquisitions and opportunities. I think he calls them  
25 hypothetical or speculative. So there isn't any conclusion as



1 to value.

2 But he makes the assumption that, one, this company can  
3 just go raise any amount of capital it needed to to make  
4 maximum use of the NOL, and he doesn't take into account, which  
5 he think he acknowledges, he doesn't take into account any of  
6 the risks inherent in raising that capital, including the risks  
7 of just what this asset is on a stand-alone basis, that it  
8 doesn't have a management team, that it would have to incur  
9 overhead and build an infrastructure to turn itself on, if you  
10 will, to make those acquisitions. Nor does he account at all  
11 for any 269 risk that is significant that would arise from a  
12 meaningful investment of equity and/or debt in his sum  
13 analysis.

14 A meaningful investment of equity into this company that  
15 when compared, again, to the relative size of the asset base  
16 that exists today in our judgment creates meaningful risk with  
17 respect to 269 arising from the acquisition of the company  
18 pursuant to the plan. He makes -- takes no account of any  
19 risks associated, he just creates it as a hypothetical, here's  
20 what could happen, but doesn't discount it and therefore  
21 doesn't come to a valuation with respect to that opportunity.

22 Q. Okay.

23 MR. ARD: Your Honor, oh, I apologize. I object to  
24 the last question, to the extent that he's trying to offer an  
25 opinion on what 269 means. It's not his expertise.

1 THE COURT: Overruled.

2 MR. ARD: Okay.

3 MR. MASTANDO: Okay. Thank you, Mr. Zelin. Nothing  
4 further at this time, Your Honor.

5 THE COURT: All right. Cross?

6 MR. ARD: Good afternoon, Your Honor. Seth Ard,  
7 Susman Godfrey on behalf of the equity committee.

8 CROSS-EXAMINATION

9 BY MR. ARD:

10 Q. Good afternoon, Mr. Zelin.

11 A. Hello.

12 Q. Okay. You concluded that the range of enterprise values  
13 for reorganized WMI is 135 to 185 million dollars, correct, on  
14 page 8 of your report?

15 A. Yes. I was checking. That's correct.

16 Q. And as you have just been discussing, one of the  
17 components included in that enterprise value is the value of  
18 the future corporate opportunity, correct?

19 A. Yes, that's correct.

20 Q. And you value that future corporate opportunity at 10 to  
21 25 million dollars, correct?

22 A. Yes.

23 Q. And this is the value of Wimrick's opportunity to shelter  
24 taxable income generated by future investments, correct?

25 A. The acquisition of assets that would generate income, yes.

1 Q. Right. And so the future corporate opportunity value is  
2 the value of Wimrick's opportunity to shelter that income  
3 through the NOL, correct?

4 A. That's correct.

5 Q. And your report assumes there would be a large post-change  
6 NOL available to the company, correct?

7 A. Yes, that's correct.

8 Q. Your report says it's 1.8 billion, I believe?

9 A. I think that's correct. Let me just check the amount.

10 Q. Yeah.

11 A. On page 26, 1.8 billion, what we refer to as the NOL not  
12 subject to limitation.

13 Q. And we heard from Mr. Carreon this morning that it's  
14 actually 2 billion; is that right?

15 A. I think it actually could be a little bit higher, yes.

16 Q. And to utilize the -- this corporate opportunity, the  
17 company would have to go out and raise more capital to bring in  
18 additional income producing assets, correct?

19 A. Yes.

20 Q. And the corporate opportunity value is the value derived  
21 by the excess NOLs that will be -- I mean, the excess income  
22 that will be sheltered through the future investments, correct?

23 A. I'm not sure I understand the term excess income, but it  
24 is truly the taxes that reorganized WMI would not have to pay,  
25 would avoid from paying, would not have to pay, on the income

1 generated by the subsequent acquisition of new assets.

2 Q. Okay. And to get a subsequent acquisition, of course, you  
3 would have to have a future investment, correct?

4 A. There -- and from our analysis there would be no way to  
5 bring that income into the company without making a subsequent  
6 investment for that purpose.

7 Q. Okay. And in assessing the value of the corporate  
8 opportunity, you cap the size of the investment that could be  
9 made, correct?

10 A. Well, we considered all the facts and circumstances around  
11 sourcing that investment and that investment being made and  
12 came to the view that in order to minimize the risks that we  
13 had identified, that limiting the size of that investment to  
14 127 is from a valuation standpoint a prudent way of looking at  
15 the value of that opportunity.

16 Q. Okay. This may just be semantics, but you capped the size  
17 of the investment that could be made in term -- for purposes of  
18 your report, correct?

19 A. It's the use of the word cap that I'm not too sure I like.  
20 We for -- in order to minimize the risk, we assumed that the  
21 dollar amount of investment that can be considered for  
22 valuation purposes should be limited to 127 million dollars,  
23 the size of the non-income producing assets.

24 THE COURT: I'm sorry. The size of the --

25 THE WITNESS: The value of the non-income producing

1 assets -- the non-tax assets, I'm sorry.

2 MR. ARD: Your Honor, may I approach to hand you the  
3 deposition transcript?

4 THE COURT: Yes. Thank you.

5 MR. ARD: Can you please turn on the Elmo?

6 (Pause)

7 BY MR. ARD:

8 Q. I understand you don't like the word cap, but that was the  
9 word you used during the deposition, correct? You just -- if  
10 you look on the -- just below the highlighting, you just cap  
11 the size of that investment for reasons that you're sure  
12 that --

13 A. I guess that is what I testified to. But in essence, it  
14 is a limit taking into consideration cap limit, taking into  
15 consideration the risks that we identified.

16 Q. Okay. And this 127.5 -- oh, sorry, and in particular you  
17 concluded that the size of that investment would be limited to  
18 the value of the existing assets in the estate or 127.5 million  
19 dollars, correct?

20 A. Well, for purposes of valuation we did limit the assumed  
21 size of the new investment to the value of the non-tax assets.

22 Q. Which is 127.5 million?

23 A. As a midpoint, that's correct.

24 Q. Okay. And this 127.5 million cap includes investments  
25 both through debt and equity raises, correct?

1 A. They both should be considered, that's correct.

2 Q. But the 127 million dollar cap includes both equity raises  
3 and debt raises combined, correct?

4 A. Yes. And we assumed equity raises for our valuation  
5 purpose.

6 Q. Okay. So in sum, you assume that the total investment  
7 that could be used by this company to acquire new business  
8 could not exceed 127.5 million dollars without violating  
9 Section 269 of the IRS Code, correct?

10 A. To be a little more precise, we are trying to value this  
11 excess unlimited, unrestricted NOL, and to come up with that  
12 value we had to assume an investment. And based upon advice of  
13 counsel and discussions -- an assessment of the facts and  
14 circumstances, in order to be comfortable from a valuation  
15 standpoint that it was more likely than not that a court would  
16 not find that the acquisition of control pursuant to the plan  
17 was for the principal purpose of avoiding taxes, or tax  
18 avoidance, that the best way to reflect that in the valuation  
19 analysis was to limit the dollar amount of new investment made  
20 to the value of the non-tax assets. And that's just how we  
21 attempted to value those assets and consider all the risks,  
22 including risks inherent in Section 269.

23 Q. Okay. So you assumed that the total investment could not  
24 exceed 127.5 million dollars without violating Section 269 of  
25 the code.

1 A. Again, it's the issue of you saying without violating  
2 Section -- the way I would describe it is that in order to get  
3 an opinion of counsel that it was more likely than not that the  
4 IRS would not find that the acquisition of control pursuant to  
5 the plan, excuse me, was for the principal purpose of tax  
6 avoidance away from a valuation standpoint to avoid the risk  
7 associated with, was to limit the amount of the investment to  
8 127.

9 Q. I believe I neglected to give you a copy of your  
10 deposition.

11 A. That's okay.

12 Q. If you could please turn to page 23.

13 A. Okay.

14 Q. The question was during your deposition:

15 "You assume for your threshold that the total investments  
16 that could be used by this company to acquire new business or  
17 to take on new business could not exceed 127.5 million  
18 dollars."

19 Your answer was, "Without implicating 269, that's  
20 correct."

21 The question was, "Without violation 269?"

22 And you said "Yes."

23 A. Yeah. Well, you're pointing to the last few questions of  
24 what was three or four pages of discussion. I think what I've  
25 just testified here was covered. That may have been a short

1 summation. But we do describe -- I do describe in the  
2 deposition the theory behind why we limited the investment to  
3 127 so we could, again, avoid the risks or avoid this more  
4 likely than not issue that -- with respect to the acquisition  
5 of control. So you have to read --

6 Q. Okay.

7 A. -- I think the few pages before to get the full benefit of  
8 the discussion, not just one question and answer.

9 Q. Okay. Your -- but, okay. But you do agree that you  
10 assumed that the threshold amount you can invest was 127.5  
11 without violating 269. Is that not right?

12 A. Again, you're being a clever lawyer by focusing on one  
13 question and one answer. And I respect you for it, but this  
14 was the sum total of a lot of conversation that happened around  
15 this issue. And as I've described it in my deposition, I  
16 believe as I described it here, we -- the issue was more from a  
17 valuation perspective, how much money could we assume was  
18 invested for purposes of valuing the corporate opportunity and  
19 receive a more than likely than not opinion from counsel that  
20 that acquisition of the company pursuant to -- actually, of  
21 control pursuant to the plan was not for the principal purpose  
22 of avoiding taxes.

23 So again, you point me to one last question and answer,  
24 but I think it's in context, the substance of my deposition is  
25 consistent.



1 Q. Your analysis assumes that there will be no debt raised?

2 A. Yes. We did assume no debt would be raised.

3 Q. And you also assume that the 127.5 million cap applies to  
4 investments made by future owners of the company, correct?

5 A. I'm not sure I understand the question.

6 Q. If future owners of the company made pro rata  
7 contributions, you assume that the 127.5 million dollar cap  
8 would apply to that as well?

9 A. Yeah. We don't distinguish as to whether the money comes  
10 from future owners or new investors. We just focus on the 127.

11 Q. And you understand that at least one of the creditors  
12 here, Owl Creek, was running spreadsheets on the value of  
13 Wimrick assuming very large investments, correct?

14 A. I've read that deposition. I did come to be aware of  
15 that. What hedge funds do hedge funds do. People run  
16 scenarios all the time. I think in substance the depositions  
17 that I've read with respect to those -- that testimony was that  
18 they were hypothetical things that were done, but everyone was  
19 fundamentally aware of the risks of making that size of an  
20 investment. And while they ran spreadsheets, they were nothing  
21 more than an analyst running a hypothetical number, but no real  
22 indication that that's what the intent was to do, especially  
23 given the risks of making that size of an investment.

24 Q. Okay. And to clarify, you do not consider yourself a tax  
25 expert, correct?

1 A. I do not consider myself a tax expert.

2 Q. And --

3 A. That's why I retained Willkie Farr to help us through  
4 this.

5 Q. And you do not consider yourself an expert on Section 269  
6 of the IRS Code, correct?

7 A. That would be within the general broad definition of tax.

8 Q. So no, you do not consider --

9 A. I do not.

10 Q. And for purposes of assigning value to the corporate  
11 opportunity, you didn't make any assumption regarding whether  
12 Wimrick will be run as a runoff company, correct?

13 A. Well, we don't -- we looked at what Wimrick is and what it  
14 will be at the time the company emerges from bankruptcy and we  
15 have the acquisition of control pursuant to the plan. That's  
16 what we have as a fact in our analysis.

17 Q. Right. But you assigned a corporate opportunity value to  
18 this company, correct?

19 A. That is correct.

20 Q. And in making that assignment of value you don't make any  
21 assumption regarding whether Wimrick will be run as a runoff  
22 company, correct?

23 A. We are fundamentally focused on the ability to value the  
24 NOL that is not otherwise used by Wimrick. We call it  
25 corporate opportunity, but we're really trying to get at is the

1 substance of the value of this NOL. And in order to get at  
2 that value independent of what Wimrick will be upon emergence,  
3 you have to assume some investment, independent of what happens  
4 or what will happen to Wimrick upon emergence.

5 Q. Okay. But in particular, you do not make any  
6 determination whether Wimrick will be a runoff or a small  
7 little ongoing company, correct?

8 A. No. We just look at the facts and circumstances that  
9 exist today.

10 Q. Okay. So you're not assuming that Wimrick will be a  
11 runoff company for purposes of this --

12 A. We are assuming no change to Wimrick's business operations  
13 going forward.

14 Q. I didn't hear that.

15 A. We are assuming no change to Wimrick's business operation  
16 with respect to the existing runoff portfolio going forward.  
17 It will continue to runoff.

18 Q. It will continue to runoff, but Wimrick, the entire  
19 company, or reorganized WMI, you do not assume that reorganized  
20 WMI will be run as a runoff company, do you?

21 A. I don't think we make any assumption. One, for purposes  
22 of valuing the net operating loss I don't think we make an  
23 assumption that reorganized WMI will or will not be a runoff  
24 company. We are just looking at investment to be made and the  
25 sheltering of the income generated by that investment for

1 purposes of valuing the net operating loss only.

2 Q. Now, the discounted cash flow analysis that you perform in  
3 your report assumes that the company will operate as a runoff  
4 company, correct?

5 A. That the runoff portfolio will continue to be operated as  
6 is, yes, that's correct.

7 Q. The business plan, as you call it, assumes there will be  
8 no new business; is that right?

9 A. I don't know that I called anything a business plan. What  
10 we have is a financial projection that shows the cash flow  
11 generating capabilities of the existing runoff reinsurance  
12 portfolio. I haven't seen a business plan; I've just seen a  
13 financial model that suggests what will happen over the next 10  
14 years to the existing portfolio.

15 Q. Okay. But there's no business plan that you're aware of  
16 that assumes that there will be any new business at reorganized  
17 WMI, correct?

18 A. I have not seen a business plan that shows that.

19 Q. And Alvarez and Marsal provided the forecasts upon which  
20 you run the runoff portfolio valuation; is that correct?

21 A. I believe they had primary responsibility for its  
22 preparation, so I believe we got it from Alvarez and Marsal,  
23 yes.

24 Q. Okay. And those forecasts assume that all money that's  
25 available to be paid out in dividends will be paid to investors

1 as soon as it's available to be paid, correct?

2 A. That is correct.

3 Q. Okay. So you assume that none of the available cash  
4 generated from the runoff will be used internally for the  
5 company to make new investments?

6 A. That's correct.

7 Q. And you didn't run analysis to see what the company would  
8 be worth if you took the cash flow and used it to acquire new  
9 assets and ran a going concern company, correct?

10 A. Well, I think, one, we did not run those analyses. Those  
11 cash flows come many years out, three, five, six, seven years  
12 out. So they would not be available to make new investments  
13 until that point in time. And two, as I think we talked about  
14 in my report and I believe at my deposition, the fundamental  
15 functioning of discounted cash flow methodology assumes in its  
16 core that whatever discount rate we apply to present value of  
17 those cash flows that the cash itself is assumed to continue to  
18 return that discount rate as far as future income.

19 So it's implicit in a discounted cash flow methodology  
20 that the cash flow is available for distribution,  
21 notwithstanding they are assumed paid out to shareholders, will  
22 continue to generate a thirteen to fifteen percent rate of  
23 return. That's just fundamental to internal rate of return  
24 analysis and discounted cash flow methodology, and I think I  
25 state that in the report as well.

1 Q. Okay. But you're assuming that for purposes of the report  
2 that the cash flow itself will not be used to reinvest anything  
3 in the company, correct?

4 A. No, but it's assumed to generate a nice thirteen to  
5 fifteen percent rate of return, which in today's market I think  
6 is --

7 Q. Okay.

8 A. -- is a good -- is a very, you know, nice assumption.

9 Q. And you don't know what the intentions of the future  
10 owners of the company are, correct?

11 A. I do not know.

12 Q. Okay. Page 13 of your report --

13 A. I'm sorry. You said page 13?

14 Q. 13 of your report, yeah.

15 A. Okay.

16 Q. Indicates that the precedent transaction value of Wimrick  
17 is 145 to 205 million, correct?

18 A. That the value applying -- using market-observed multiples  
19 from precedent transactions applied to Wimrick would give you a  
20 mathematical value of 145 to 205.

21 Q. Okay. But you gave substantially all the weight to the  
22 DCF analysis, correct?

23 A. That is correct.

24 Q. Between the time of your last report and this report there  
25 was a new precedent transaction, correct?

1 A. I believe that is correct. I'm just -- give me a moment  
2 to turn to the page. Yes, I believe the Enstar Group  
3 transaction, which is the first in our list of runoff  
4 precedents, came to -- arose or was announced just at or before  
5 we issued the prior report -- just after we issued the prior  
6 report.

7 Q. Okay. But you determine notwithstanding this recent  
8 precedent transaction to still give substantially no weight to  
9 the precedent transaction analysis?

10 A. I did. And again, precedent transaction requires looking  
11 at the market activity, the nature of the underlying assets  
12 that are being acquired to see if there's some similarity to  
13 the asset that you're trying to value. And while there was one  
14 transaction at .8 times cash -- .8 times book value it was,  
15 again, for a property and casualty company, which is a very --  
16 portfolio I should say, which is a very different portfolio  
17 from a mortgage reinsurance portfolio. That notwithstanding,  
18 the incorporation of that multiple in our range of multiples  
19 didn't affect materially the 145 to 205, but our conclusion of  
20 value was still more heavily -- significantly more heavily  
21 weighted to discounted cash flow.

22 Q. Okay. You didn't approach Enstar about its interest in  
23 purchasing Wimrick or reorganized WMI, did you?

24 A. I did not.

25 Q. You didn't approach Citadel Risk Management, I think is

1 the second company listed here on page 23, as a company that  
2 engaged in a similar precedent transaction?

3 A. The asset that was acquired was a property and casualty  
4 and health and welfare portfolio, very different from a  
5 mortgage reinsurance portfolio. But I did not approach Citadel  
6 Risk Management, who last made an acquisition that we could  
7 tell back in February of 2008.

8 Q. And you didn't approach any of these companies here about  
9 potentially buying reorganized WMI, did you?

10 A. No, I did not approach those companies.

11 Q. But Blackstone was asked by WMI to represent it in the  
12 potential sale of Wimrick; is that right?

13 A. We were asked during the course of our mandate that if a  
14 decision were to be made for which Blackstone has no influence  
15 in that decision, but for if a decision were to be made would  
16 be willing -- would we be willing to take on the marketing of  
17 the asset. And we agreed to be the M&A adviser if and when  
18 that transaction was pursued. But that -- we have not been  
19 retained, nor have we approached the market to do that. I'm  
20 sorry. We have not been asked to commence a marketing process,  
21 I should say.

22 Q. Just to be clear, this is page 4 of your report, indicates  
23 that Blackstone was asked by the company to represent it in the  
24 potential sale of Wimrick; is that right?

25 A. Yeah. And it says if a sale process commences this would



1 be our compensation, but no such process has commenced because  
2 we've not been asked to commence one.

3 Q. Okay. You indicate that WACC is -- well, WACC is  
4 shorthand for weighted average cost of capital, right?

5 A. Yes, that's correct.

6 Q. And in a company with no debt leverage, WACC is the cost  
7 of the company raising equity, correct?

8 A. No. In the application of weighted average cost of  
9 capital, one looks at the market and derives the weighted  
10 average cost of capital from an analysis of similar WACCs that  
11 you can observe in the marketplace or in transactions,  
12 acquisition transactions. And you apply kind of a market WACC  
13 to the subject target portfolio independent of what the capital  
14 structure will be of the company coming out of bankruptcy.

15 Q. Okay. And on page 17 of your report you give some  
16 historical figures about what the market is doing in this  
17 respect, right?

18 A. Yes. That's correct.

19 Q. So if you look at page 17 and you look at those two boxes  
20 on the bottom right-hand corner of the page --

21 A. Yes.

22 Q. -- the box on the left represents the two-year average  
23 WACC historical figures in the market, right?

24 A. Yes, that's correct.

25 Q. And the right box is a five-year historical average?

1 A. Yes, that's correct.

2 Q. And the top columns is the -- is for the total universe of  
3 companies?

4 A. Yes, that's correct.

5 Q. And the bottom column that you set out separately is for  
6 distressed insurers?

7 A. That's correct.

8 Q. Okay. As a general matter, the lower the WACC the higher  
9 the DCF value of the company will be, right?

10 A. The lower the WACC the higher the DCF will be, all else  
11 being equal.

12 Q. Yes.

13 A. Yes.

14 Q. So if you look at the upper left-hand corner of the box on  
15 the left, do you see 10.9 percent there?

16 A. I do see that, yes.

17 Q. And that represents the observed return for equity in the  
18 marketplace today in a company with no debt?

19 A. Over a two-year period, that's correct.

20 Q. And you look to the two-year average and the five-year  
21 average in order to average through a period of time to come up  
22 with historical averages, right?

23 A. That's correct.

24 Q. Okay. And your -- sorry, your recommended WACC range for  
25 this company is thirteen to fifteen percent?

1 A. Yes, that is correct.

2 Q. And you didn't just choose the thirteen percent from the  
3 upper left-hand corner of the box on the right, did you?

4 A. No, I did not.

5 Q. Rather, you looked at the data on the page and chose  
6 thirteen percent based upon the entirety of the facts you saw,  
7 right?

8 A. Yes. I looked at the data on the page and in coming to  
9 our judgment, as I testified, valuation is an art not a  
10 science. In coming to a judgment as to the range that we  
11 should apply from a discount standpoint we focus more on the  
12 numbers in the top right of the four quadrants in the bottom of  
13 the chart, representing in essence the implied observed  
14 weighted average cost of capitals for the total universe of  
15 comparable companies we looked at over a five-year period. And  
16 we focused on the five-year averages for a number of reasons.

17 Q. Okay. But you just explained that you didn't choose the  
18 thirteen percent from the upper left-hand corner. Rather you  
19 looked at the data on the page and chose thirteen percent based  
20 upon the entirety of the facts you saw, right?

21 A. Yes, with a focus on the ranges more implicit or  
22 consistent with the top right quadrant. But I did look at all  
23 the facts on the page, that's correct.

24 Q. Okay. And more broadly, in calculating the WACC you'll  
25 look at all the circumstances, including any change from a

1 precedent standpoint, any change in the market and anything  
2 unique to Wimrick, right?

3 A. Can you repeat the question again?

4 Q. More broadly, in calculating the WACC you'll look at all  
5 the circumstances, including any change from a precedent  
6 standpoint, any change in the market and anything unique to  
7 Wimrick, right?

8 A. Well, we would do that in coming up with a valuation. In  
9 this instance, our use of the five-year average was meant to  
10 eliminate the ups and downs experienced in the marketplace for  
11 many of these insurers because of the crisis that occurred in  
12 the last few years.

13 So by using the five-year average we attempted to look  
14 through and take away any unique fluctuations in WACC arising  
15 from the volatility in the markets in the last few years.

16 Q. But you didn't just calculate the five-year average part;  
17 you calculated both the two-year average and the five-year  
18 average, correct?

19 A. Yes. And what we're presenting here is all of the facts  
20 and all of the analysis that we did, but the judgment we came  
21 to with respect to selecting the discount rate was focused on  
22 the top right quadrant, or the five-year average.

23 Q. I think you know the question that's coming up, since it  
24 came up in the deposition but --

25 A. I'll let you ask it, though.

1 Q. Sure. Thank you. You recommend and use the same WACC for  
2 this report as you did for the prior report, right?

3 A. Yes, that's correct.

4 Q. Thirteen percent to fifteen percent.

5 A. Yes, that's correct.

6 Q. But the WACC for the two-year and five-year average has  
7 gone down considerably for distressed insurers, right?

8 A. Which made me extremely comfortable with the decision I  
9 made back in December and the decision I made today.

10 Q. Was that a yes?

11 A. It was a yes with an exclamation point.

12 Q. Okay. And since your last report it's gone down 8 to 10  
13 percentage points for the two-year WACC?

14 A. For the two-year WACC.

15 Q. Yes.

16 A. That's correct, not for the five-year WACC, but for the  
17 two-year WACC.

18 Q. For the five-year WACC it's gone down about six percentage  
19 points?

20 A. Let me -- I have the -- if I can just check, that's in my  
21 prior report. I'm sorry. Give me one moment to find it if you  
22 don't mind. No. For the five-year WACCs that we relied upon,  
23 there really wasn't significant movement at all between our  
24 December report or November report and the June report at all.

25 Q. I apologize. I was asking about for distressed insurers.

1 A. Yes. Again, if you look at the three quadrants, the two  
2 on the left and the one on the bottom right, they did move  
3 meaningfully. But when you look at the quadrant on the top  
4 right, they didn't move much at all. Which got us comfortable  
5 that in selecting a five-year average for the universe of  
6 insurers back in November with the expressed intent of trying  
7 to eliminate the volatility in the marketplace that we knew the  
8 market was experiencing in this industry and the fact that  
9 those same five-year averages did not move in the last six  
10 months meaningfully but the two-year averages moved and the  
11 five-year averages moved meaningfully for the distressed  
12 insurers, it gave us a significant amount of comfort that by  
13 focusing on the long-term five-year averages for the universe,  
14 exigencies in the marketplace over the last six months should  
15 not result in any meaningful swings in the value of the  
16 enterprise.

17 Q. The top document, which is from Equity Committee Exhibit  
18 153, is your prior -- is the same chart in your prior report,  
19 correct?

20 A. Yes, that's correct.

21 Q. Okay. So just to -- again, just to go through it real  
22 quickly, in the upper left-hand corner you see considerable  
23 movement down, right, about five percentage points?

24 A. In the two-year total universe WACCs, which we did not  
25 rely upon for our WACC range, they did move meaningfully, yes.

1 Q. Okay. And the bottom left-hand corner, which is the two-  
2 year WACC for distressed insureds, it moved meaningfully about  
3 8 to 9 percentage points?

4 A. That's correct, which meaning if I had applied the 21  
5 percent numbers to our prior valuation I would have had a  
6 dramatically lower valuation. But I ignored the bottom left  
7 quadrant in December, as I ignored it today, for purposes of  
8 selecting a discount rate. But they did move meaningfully,  
9 that's correct.

10 Q. Okay. And the bottom right-hand corner, they move  
11 meaningfully by about, what, six percent?

12 A. Yes. And again, those -- the bottom right was ignored and  
13 disregarded for the selection of the WACC range in our  
14 valuation. And the ones that did not move meaningfully --  
15 well, they did move -- were the ones in the top right quadrant,  
16 which, again, as I said before, gave us meaningful comfort that  
17 the reason for selecting the top right quadrant back in  
18 November, i.e. to ignore all the volatility in the marketplace,  
19 was the right decision because, in fact, those five-year  
20 averages didn't move much in the last six months,  
21 notwithstanding the significant movement in the other averages.

22 Q. So you were trying to ignore the volatility in the  
23 marketplace?

24 A. What I was trying to do was look at the fundamental  
25 intrinsic value of the asset. And if I had applied a two-year

1 WACC average in December and November 2010, my value would have  
2 been dramatically lower. But by virtue of the -- of looking  
3 through the risk or the movements in the markets in the last  
4 few years, the intrinsic value of this portfolio in applying  
5 the same thirteen to fifteen percent discount rate hasn't  
6 really fundamentally changed by virtue of the market. And that  
7 I think is the right result.

8 Q. Okay. So your WACC shouldn't have changed then, you know,  
9 in 2010 either. You were trying to account for lack of  
10 volatility in the market, correct?

11 A. I was trying to -- given the unique volatility of the last  
12 few years in the market we came to the valuation judgment that  
13 it's best to look over a longer period of time than just look  
14 at the last two months, two years in driving what we think the  
15 right discount rate is for purposes of evaluating the intrinsic  
16 value in the asset.

17 Q. So if you don't know what --

18 THE COURT: Excuse me. Let's take a five-minute  
19 break. Okay.

20 MR. ARD: Sure.

21 THE COURT: I think we're going to go to 6:30, is all.  
22 I hope you can conclude by then.

23 MR. ARD: I will finish by then. Yeah.

24 THE COURT: All right.

25 MR. ARD: Thank you, Your Honor.



1 (Recessed at 5:54 p.m.; reconvened at 5:59 p.m.)

2 THE CLERK: You may be seated.

3 THE COURT: You're still under oath, and you may  
4 proceed with cross.

5 MR. ARD: Thank you, Your Honor.

6 BY MR. ARD:

7 Q. The major volatility in the market happened in what, 2008,  
8 2009?

9 A. Well, there was a major swing down as a result of the  
10 crisis and then a major turn back up. Post-crisis the market  
11 recovered.

12 Q. And so why don't you assume that the last two years is a  
13 return to normalcy?

14 A. Because they -- the markets' growth in the last couple of  
15 years was quite aggressive. These insurers experienced all  
16 kinds of stress during the last few years. So by going back  
17 five years we can get through normalcy, downs and ups and look  
18 at a long-term average and get the noise out of the market.

19 Q. Yeah. But so you're just trying to intentionally going  
20 back into the volatile period, whereas if you just used a two-  
21 year WACC you would be looking only at the period of normalcy?

22 A. If I had used the two-year WACC back in December I would  
23 have dramatically undervalued the assets. And while the two-  
24 year WACC has moved meaningfully, the fact that I used the  
25 five-year average was fundamental to our initial decision was

1 that the movements in the datas and the volatility of the  
2 stocks in this portfolio were such over the last two years that  
3 we were best to go back a longer period of time and smooth out  
4 the ups and the downs.

5 Q. And I assume --

6 A. And I think that was my methodology back in December, and  
7 that continues to be my methodology today.

8 Q. Okay. And I assume that this isn't arbitrary. If you had  
9 done it nine months prior to that, you'd want to use the same  
10 WACC, right, because you want the same WACC over time?

11 A. Nine months prior to when?

12 Q. To your last report in November.

13 A. I would have evaluated these very same numbers, and I  
14 don't know whether I would have come to a similar conclusion  
15 nine months prior. But in my evaluation of the analysis in  
16 December and my evaluation today, given that the attempt was to  
17 in a DCF look at the intrinsic value of the asset, the  
18 selection of the thirteen to fifteen percent discount rate was  
19 meant to discover that intrinsic value without regard to unique  
20 volatility in the marketplace.

21 Q. Right. So if you're looking at periods of five-year  
22 periods you should have constancy over the last year or the  
23 last seven months is your point?

24 A. Well, I don't know if you have constancy over the last  
25 seven months or year. You would have an ability to eliminate

1 the impacts of unusual swings in the marketplace over the last  
2 few years.

3 Q. Are you aware that in analysis you performed in March of  
4 last year you used a twelve percent WACC?

5 A. I thought I had used a thirteen to fifteen percent WACC.

6 Q. March of last year.

7 A. Oh, in March of last year. I don't think I -- I think I  
8 was just retained in March of last year. Are we talking about  
9 the same case?

10 Q. Maybe not. Let's see. Can you pull EC-283 please? It's  
11 in your -- it's in Volume 4 --

12 A. Okay.

13 Q. -- right there. I apologize.

14 THE COURT: EC-20 --

15 MR. ARD: 283.

16 THE COURT: 283.

17 THE WITNESS: It's Volume 4 of this. I see EC-283.

18 Q. Okay. Do you see the e-mail from Alvarez & Marsal?

19 A. I do see an e-mail from Alvarez & Marsal.

20 Q. Reporting on a DCF valuation of Wimrick?

21 A. I do see that, yes.

22 Q. And you see that it says that they're using a discount  
23 rate of twelve percent?

24 A. I believe that whatever model was sent from Brad Sheller  
25 to Chris Wells did include a twelve percent discount rate, yes.

1 Q. It's from Chris Wells to Brad Sheller, correct?

2 A. I'm sorry, from -- I apologize, from Chris Wells to Brad  
3 Sheller, yes.

4 Q. Was Alvarez and Marsal doing an independent DCF analysis  
5 that you weren't performing?

6 A. I do not understand at all the context of why this model  
7 was prepared and sent. I just know that we were retained  
8 sometime in late March in April of 2010. So our involvement,  
9 at least any valuations of conclusions we, Blackstone,  
10 independently came to was post this analysis -- was post this  
11 e-mail.

12 Q. Unless I'm mistaken, wasn't it 2009 you were retained?

13 A. Then the company owes me a lot more money for fees.

14 Q. Oh, okay. It's 2010. Okay.

15 A. And that would bring the value down as well.

16 Q. So you -- that's a pretty expensive bill you're acquiring  
17 here. Okay.

18 A. Quality comes -- does not come cheap.

19 Q. All right. Let's move on.

20 A. That's a good idea. I can put this binder back or do we  
21 need to --

22 Q. You can put that back. Thank you. On page 34 of your  
23 current report --

24 A. Page 34?

25 Q. Yeah.

1 A. Okay. I have it, yes.

2 Q. You note that there is a compounded annual rate of return  
3 on investment of approximately eight to 12.5 percent based on  
4 historical returns generated by similar portfolios, right?

5 A. That's correct.

6 Q. And here we're in the corporate opportunity section of  
7 your report, right?

8 A. Yeah, attempting to value the NOL not otherwise used by  
9 Wimrick.

10 Q. Okay. So the eight to 12.5 percent range that you're  
11 using here is consistent with your view of what expected  
12 returns on assets would be for similar portfolios in the  
13 industry, correct?

14 A. It was an estimate of that, yes.

15 Q. Okay. But that -- estimate of expected returns on  
16 assets --

17 A. Yes.

18 Q. -- would be for similar portfolios in the industry?

19 A. Yes.

20 Q. Yet you assume that the cost of equity for the company is  
21 -- the cost of capital is thirteen to fifteen percent, right?

22 A. No, I don't.

23 Q. No, earlier in the report for the WACC.

24 A. The WACC was thirteen to fifteen percent.

25 Q. Okay. So you assume that investors in this type of

1 company will require thirteen to fifteen percent returns?

2 A. For purposes of valuing the runoff portfolio, which was an  
3 existing asset base, which was generating cash flow and income,  
4 we used a weighted average cost of capital, which includes both  
5 the cost of debt and the cost of equity, of thirteen to fifteen  
6 percent. That's for valuing the existing portfolio that is  
7 being managed and runoff today.

8 Q. So you're assuming that investors are going to require  
9 thirteen to fifteen percent returns, right?

10 A. That would be the required -- that's the weighted average  
11 cost of capital for the reorganized company for anyone wanting  
12 to make an investment in the existing portfolio.

13 Q. Okay. But --

14 A. Not in WMI but in -- for the existing portfolio.

15 Q. Okay. But you say here that the returns on assets for  
16 similar portfolios in the industry are about eight to 12.5  
17 percent, right?

18 A. That's correct.

19 Q. Okay. So people are going to expect thirteen to fifteen  
20 percent, even though the returns on assets in this industry are  
21 only eight to 12.5 percent?

22 A. And that's the benefit of leverage, yes.

23 Q. Leverage?

24 A. Leverage. You -- this is an asset return. The weighted  
25 average cost of capital is the return on the debt plus the

1 return on the equity.

2 Q. Right. But here you said before you're assuming there is  
3 going to be no debt raising here.

4 A. It's a little nuance of weighted average cost of capital  
5 methodology, is that you apply -- you look through the capital  
6 structure of the current company and you look at the market  
7 weighted average costs of capital for coming up and then  
8 forming a discount rate, notwithstanding what the leverage will  
9 be or the capital structure will be of the existing company.

10 Q. But you are assuming that there will be no debt in this  
11 company, right?

12 A. As far as I know there will not be any debt raised, but  
13 that's independent of a weighted average cost of capital  
14 analysis.

15 Q. Well, I hate to turn back to it, but very quickly on page  
16 17 on your little charts there, in the upper left-hand corner  
17 is -- where it says zero percent --

18 A. That's correct.

19 Q. -- right, that's the cost of capital for companies where  
20 there will be no debt, right?

21 A. That would be in essence the implied equity cost of  
22 capital being run through these charts. That's correct.

23 Q. Okay. So it's different. Depending on whether there  
24 would be debt or not the cost of capital can vary, right --

25 A. Sure.

1 Q. -- of the company? Sure.

2 A. Sure.

3 Q. Okay. In this company, there is going to be no debt,  
4 right?

5 A. In the existing portfolio there will be no debt.

6 Q. And in the future portfolio you're assuming there's not  
7 going to be any debt.

8 A. When you say I'm assuming, I don't know what's going to  
9 happen in the future. But for purposes of valuing the company  
10 today we generate a weighted average cost of capital based upon  
11 market analysis. I don't know what will happen to the company  
12 tomorrow or upon emergence from bankruptcy.

13 Q. Okay. But you said twenty, thirty minutes ago that you're  
14 assuming for purposes of this corporate opportunity valuation  
15 that there will be no debt.

16 A. For the corporate opportunity or the value of the NOL --

17 Q. Yeah.

18 A. -- which is an independent valuation from the value of the  
19 runoff portfolio, we assume that we raise 127 million dollars  
20 of equity. That's independent of the methodology we used to  
21 value the runoff portfolio, two different valuations.

22 Q. I got you. And in neither one is there any debt.

23 A. For purposes of estimating the value of the net operating  
24 losses we did not assume any debt. And what you typically do,  
25 I think as I testified before, in valuing tax attributes, it is



1 common methodology to value the present value of that tax  
2 attribute using a cost of equity, since in valuation technology  
3 NOLs are typically attributable to the equity. So therefore,  
4 you use cost of equity to value net operating losses.

5 Q. Okay. And I think we've now come full circle.

6 A. Okay.

7 Q. You are assuming that equity investors are going to  
8 require thirteen to fifteen percent returns in an industry that  
9 has an average of eight to twelve percent return rates.

10 A. From an asset standpoint?

11 Q. Yes.

12 A. That's -- as of right now that's correct.

13 Q. And the only way that that return rate would increase is  
14 through leverage.

15 A. That's one way it could increase, but it could also  
16 increase through growth, through the continued acquisition,  
17 through the future addition or expansion of businesses. People  
18 -- the return on equity has as its core a number of components.  
19 One is the existence of an asset base today and the potential  
20 for that business to grow its equity value over a period of  
21 time.

22 Q. Okay. But your report here doesn't attempt to evaluate  
23 any of those growth opportunities the company can have such as  
24 through debt or anything else?

25 A. Yeah, because those are not unique opportunities that this

1 company has. If any of them wanted to grow a reinsurance  
2 portfolio it could take a brand new shell corporation, go out  
3 into the marketplace and acquire reinsurance assets. The value  
4 that's intrinsic in this business is the existing runoff. It  
5 has no management team. It has no sales force, no ability  
6 today, nor has it -- did it have one while it was a captive  
7 pre-bankruptcy to go generate its own asset value, I'm sorry,  
8 to go generate new reinsurance contracts. And that's how we  
9 are valuing this asset today.

10 Q. Okay. But you're telling me that people are going to  
11 return -- are going to expect -- investors are going to expect  
12 higher rates of return than are average in this industry. And  
13 the reason that makes sense, according to you, is because  
14 there's other growth opportunities, but you don't attempt to  
15 evaluate any of those growth opportunities regardless of  
16 whether they exist in other companies or not, correct?

17 A. Trying to create -- you're trying to create a little  
18 confusion. I'm probably not doing a very good job of  
19 explaining it. When investors look at making investments in  
20 these types of assets, we have come to the conclusion that they  
21 would look for a weighted return of thirteen to fifteen  
22 percent. And that is the discount rate we apply to the runoff  
23 portfolio. That return, even though the underlying assets, the  
24 income on those assets, the cash that's being invested today,  
25 might not be generating that kind of return, an investor would

1 look to be able to manage the asset such that they can gain a  
2 thirteen to fifteen percent return once they own the asset.

3 Q. But you don't attempt in this report to figure out how  
4 they would get that up to thirteen to fifteen percent. You  
5 just run it as a runoff.

6 A. Again, when you say -- this is a runoff portfolio, and  
7 acquirers of these types of portfolios might think they can  
8 manage the asset better. Acquirers of these types of  
9 portfolios might think there may be a little bit of upside in  
10 the underlying reinsurance contracts. The issue is at what  
11 price would somebody be willing to look at making an investment  
12 here. At what price would investors look -- I'm sorry, at what  
13 returns would investors acquire, given the asset base that  
14 exists today. And the weighted average cost of capital is the  
15 application of the market-observed returns that investors would  
16 require, and that drives value.

17 Q. Okay.

18 A. That's what drives the value.

19 Q. And if you look at public disclosures of major insurance  
20 companies, the range of asset returns they are currently  
21 getting is six to nine percent, correct?

22 A. I think we've seen one pension fund that was getting a  
23 thirteen percent rate of return, which I think was CalPERS.  
24 But I think the majority of pension funds and portfolios when  
25 you look at the asset returns that they are realizing in their

1 investments are in the six to nine, six to ten. I think that's  
2 probably right.

3 Q. Okay. To be clear, your assumed rate of return is pretax;  
4 is that right?

5 A. That is correct.

6 Q. Okay. You further assume for the purpose of corporate  
7 opportunity that an investor would expect a rate of return of  
8 twenty-five to thirty-five percent; is that right?

9 A. Absolutely. For purposes of valuing the NOL --

10 Q. Okay.

11 A. -- and making use of the NOL.

12 Q. And you testified earlier that this rather high discount  
13 rate reflects the fact, among other things, that this is a  
14 startup, right?

15 A. I don't know that I testified at all that this was a  
16 rather high discount rate. Please don't put words in my mouth.  
17 I think I testified that our judgment as to what investors  
18 would want if they're looking for fifteen plus or minus percent  
19 of equity return for an existing runoff where you can touch and  
20 feel and smell the portfolio and understand it. If you're  
21 trying to build something new, something out of nothing, then  
22 to make that investment you would likely require not a high but  
23 a higher rate of return than what you would otherwise require  
24 from acquiring an existing set of assets.

25 So the twenty-five to thirty-five is by definition higher

1 than what we used in the existing portfolio, but it reflects  
2 all the risks that an investor who's attempting to realize  
3 value out of this NOL and all the steps that would have to be  
4 taken to make use of that NOL in our judgment would likely look  
5 to from a returns standpoint.

6 Q. Okay. So that twenty-five to thirty-five percent takes  
7 into account all those risks.

8 A. And is used just for the specific purpose of valuing the  
9 net operating loss.

10 Q. Okay. You also make a thirty-three percent or more  
11 downward adjustment to the corporate opportunity value to  
12 reflect -- on page -- let me see.

13 A. Page 37?

14 Q. Yeah. On the bottom right-hand corner there, that little  
15 adjustment, you -- when you did your calculations it got you to  
16 15 to 45 million. You do your adjustment and it goes down to  
17 10 to 25 million.

18 A. That's correct.

19 Q. Adjustment is at least thirty-three percent there. Now,  
20 you testified earlier today that that adjustment is -- it was  
21 supposed to reflect all of the risks of investing in this  
22 company, right?

23 A. That's correct.

24 Q. So aren't you just double counting this risk? The twenty-  
25 five to thirty-five percent discount rate reflects the risk and

1 then you have another thirty-three percent discount on top of  
2 it to account for the risk?

3 A. I'll try to give you a relaxed answer to that question.  
4 The 15 to 45 assumes a present value of the tax savings  
5 assuming the acquisition and investment occurs day one. We had  
6 not factored into that valuation -- it's the pure present value  
7 of the tax savings -- a number of things. One is how long it  
8 will take to execute that transaction.

9 So this is a value as of the effective date. It may take  
10 as much as a year or year and a half to put an infrastructure  
11 in place, to incur costs of building a business and building a  
12 management team here before any acquisition gets made. It  
13 takes into consideration, you know, whether, in fact, you can  
14 find. But the time and the cost between today and when you can  
15 actually effectuate that acquisition is reflected in this  
16 incremental adjustment.

17 And the way I like to think about it is that we view in  
18 essence, given all the risks that exist, all the execution  
19 risks that exist and tax risks that exist, that the NOL  
20 opportunity here from our instinctive standpoint, while on  
21 paper feels like a lot because of the gross amount of NOLs  
22 available to reorganized WMI, is reality nothing more than an  
23 option this company has that may or may not work. And it's  
24 hard for us with all the inherent risks -- while we can look at  
25 the components, I look at the bottom line -- it's hard for us

1 with all the inherent risks to value this thing other than as  
2 in essence an option.

3 Q. Okay. You met with Appaloosa and Centerbridge four to six  
4 weeks after you were retained; is that right?

5 A. I think that's right. I might have misremembered the  
6 specifics, but it was in the first two months certainly of when  
7 we were retained.

8 Q. And Owl Creek and Aurelius may have also been there but  
9 you don't -- you're not sure?

10 A. Yeah. I don't think -- I don't know that all four of the  
11 what we call settlement note holders there, but I certainly  
12 remember at least two of them being there.

13 Q. And you wanted to ask them questions because they were  
14 likely to be large stakeholders in the reorganized WMI and you  
15 wanted to understand their perspectives on what intentions they  
16 had on the asset; is that right?

17 A. That was part of my diligence, yes.

18 Q. And WAMU, either Alvarez or Weil, told you that they would  
19 be the right holders to speak to, right?

20 A. They were certainly the larger holders in the case who, I  
21 guess, had been spending a significant amount of time in  
22 negotiating and prosecuting the ultimate restructuring.

23 Q. WAMU told you they would be the right holders to speak to?

24 A. The Alvarez and Marsal folks and Weil folks did, yes.

25 Q. And the -- some of the note holders who were attending the

1 meeting were working off the same set of projections for  
2 Wimrick that you were working off of, correct?

3 A. They obviously were involved in the case well before I was  
4 involved in the case, so they would have received whatever they  
5 were provided prior to that meeting. It may have been the same  
6 or different from what I was provided because projections tend  
7 to get updated, but I believe they had access to some financial  
8 information before that meeting.

9 Q. And your diligence --

10 A. I didn't ask them what they were looking at, though.

11 Q. Your diligence was focused on what their views of the NOL  
12 opportunity was and whether they were committing capital; is  
13 that right?

14 A. That was -- of the many purposes of the meeting, that was  
15 certainly one of them.

16 Q. Thank you.

17 MR. ARD: No further questions.

18 THE COURT: Mr. Steinberg, how long do you think  
19 you're going to be?

20 MR. STEINBERG: Ten -- five, ten minutes.

21 THE COURT: All right. I'll let you go ahead.

22 MR. STEINBERG: Maybe seven minutes. I'll try to move  
23 it fast.

24 THE COURT: Thank you.

25 MR. STEINBERG: I'll only do it if Mr. Zelin gets to



1 go home.

2 THE COURT: Well, I don't mean to cut you off because  
3 he's coming back tomorrow anyway.

4 MR. STEINBERG: Oh, is he? Okay.

5 THE WITNESS: I am?

6 THE COURT: Does the debtor have no redirect?

7 MR. MASTANDO: I don't believe at the current time,  
8 Your Honor.

9 MR. STEINBERG: All right. So then I'll try to  
10 finish, because I like Mr. Zelin.

11 THE COURT: All right.

12 THE WITNESS: I appreciate that, Mr. Steinberg.

13 CROSS-EXAMINATION

14 BY MR. STEINBERG:

15 Q. All right. Mr. Zelin, I think you testified that  
16 Blackstone has not been retained to market Wimrick at this  
17 point in time; is that correct?

18 A. That is correct. Well, we've agreed to market it so we're  
19 effectively retained to do it, but we haven't commenced any  
20 marketing process.

21 Q. Have you spoken to any potential bidders for Wimrick to  
22 try to assess what the value would be?

23 A. I have not spoken to any potential bidders.

24 Q. Okay. In the debtor's liquidation analysis in trying to  
25 assess Wimrick in the liquidation scenario, it says the

1 debtor's belief of what it would be worth on a liquidation is  
2 based on consultation with various investment banks and  
3 potential bidders of Wimrick. Are you saying that they didn't  
4 consult with you to try to figure out what this would be worth  
5 on a liquidation basis?

6 A. I did not have any conversations with Alvarez as to the  
7 liquidation analysis.

8 Q. And you didn't have any conversations with any potential  
9 bidders in order to try to assess the precedent value of how to  
10 value Wimrick, right?

11 A. No. I was aware that there were indications expressed,  
12 but I did not have any conversations.

13 Q. Okay. Now, I know you've done a lot of valuation. Have  
14 you valued before NOLs?

15 A. I have, yes.

16 Q. Okay. Which companies?

17 A. Most recently I valued them in Abitibi Bowater in front of  
18 Judge Carey. I would be dishonest if I didn't admit that the  
19 majority of companies I deal with end up in bankruptcy for  
20 reasons that they not only have losses, but they can't repay  
21 all of their indebtedness. So the majority of tax analysis  
22 that we've done has been focused on whether there's enough  
23 attributes in NOLs to offset cancellation of indebtedness  
24 income. But most recently we valued the NOLs in Abitibi  
25 Bowater.

1 Q. And how much was the NOL in Abitibi Bowater?

2 A. I don't know that that value is public, but the overall  
3 valuation analysis in Abitibi Bowater -- this happened about  
4 six months ago -- I think was between two -- maybe three to  
5 three-and-a-half billion dollars, and I think the NOL component  
6 of that valuation was materially less than 500 million dollars.

7 Q. Okay. And when you did your valuation did you discount  
8 for the Section 269 concern?

9 A. Well, we did talk about Section 269, albeit briefly, but  
10 the conclusion there was that 269 would likely not be an issue,  
11 because the size of the business and the nature of Abitibi  
12 Bowater's assets, which were the largest newsprint manufacturer  
13 in the world, and the inherent value in that business relative  
14 to the attributes that were surviving was -- and actually, the  
15 complete different relationship to what we have here. So while  
16 there was a 269 discussion, it was all -- it was very, very  
17 brief.

18 Q. Now, I think you said that the -- that you took out a  
19 discount because of the risk of raising capital when you were  
20 analyzing the corporate opportunity factor; is that correct?

21 A. I'm not sure that's -- I think I said we took a discount  
22 to reflect all the risks, of which raising capital was one of  
23 them.

24 Q. Right. And what percentage discount did you give for  
25 raising capital?

1 A. I did not give any unique percentage to any one factor. I  
2 just looked at all the facts and came to a judgment.

3 Q. Was there any consideration that you -- either you gave or  
4 the company gave to actually try to get the financing component  
5 in place so that you could minimize that risk and perhaps give  
6 people a better insight if they were going to make the  
7 shareholder election under the plan?

8 A. Can you repeat that question again?

9 Q. Was there insight -- was there any discussion that either  
10 you had or with the company to try to get that financing risk  
11 ameliorated so that you would reduce the risk for the valuation  
12 purposes and also give people who were making a shareholder  
13 election greater insight as to how the reorganized entity --

14 A. If you mean did I go out and try to source the capital  
15 ahead of the plan, I did not.

16 Q. Right. Do you know whether anybody tried?

17 A. in the prior plan there was a rights offering that was  
18 embedded in it, and that was I think the only attempt I'm aware  
19 of to raise capital. That was -- albeit that's six or seven  
20 months ago. I'm not aware of any attempts ahead of the current  
21 plan.

22 Q. And once the rights offering was withdrawn you're not  
23 aware of whether anybody tried to do something to substitute  
24 that to try to put that piece of the puzzle in place and to  
25 minimize the risk that you're otherwise taking on the corporate

1 opportunity?

2 A. I am not aware of any attempt to raise capital.

3 Q. All right. Are you aware of any, you know, favorable  
4 stories of how debtors in Chapter 11 emerged where their  
5 primary asset or one of their major assets were an NOL and then  
6 post-bankruptcy they grew that entity to create value for the  
7 shareholders that existed as of the time of the confirmation of  
8 the plan?

9 A. Am I aware? I think I'm aware of at least one bankruptcy  
10 that's ongoing now where there's an NOL dispute -- an NOL  
11 discussion. I'm aware that there was certainly a bankruptcy  
12 that was just consummated a few -- not consummated, close to  
13 consummation where the ultimate parent would have access to  
14 cash NOL. But I'm not aware of any resolutions with respect to  
15 NOLs in those deals.

16 Q. But I'm not talking about a present dispute. I'm talking  
17 about something which actually has a history where the entity  
18 emerged from bankruptcy with a large NOL and grew itself,  
19 utilizing its NOL to create value for its shareholders. Are  
20 you aware of any precedent-setting situations, like  
21 International Harvester, that was one, but that may be --

22 A. I don't know if I was born when that was going on.

23 Q. Well, yeah.

24 A. At that point, I don't know if I was at work when that one  
25 was happening.

1 Q. You're not that young.

2 A. The majority of the valuations that I've done where there  
3 were sizable NOLs, the values -- leaving WAMU aside for the  
4 moment -- were valuations in where the utilization of NOL was  
5 -- or the reorganized company, like Abitibi Bowater, was able  
6 to use its attributes based upon the projected taxable income.  
7 I've not done any valuations that I'm personally aware of, nor  
8 am I aware if there are such valuations in the marketplace,  
9 where the assumption was significant acquisitions of assets or  
10 significant growth in assets. If the underlying business would  
11 grow into or grow income that -- and there was NOL, a valuation  
12 expert like myself would incorporate those NOLs into the  
13 existing business. But I'm not aware of where there was an  
14 assumption of a major infusion of capital for the purpose of  
15 going and making an acquisition, such that those NOLs would be  
16 used. I've never done a valuation like that, that I can  
17 recall.

18 Q. Okay. Were you at all aware of what happened in the U.S.  
19 Lines bankruptcy case in the late 1980s?

20 A. I am not.

21 Q. Okay. All right. You're aware in this case that  
22 shareholders who were otherwise entitled to cash took an  
23 election to take stock of the reorganized entity?

24 A. I know that that election was available. I did not know  
25 the results of that election.

1 Q. Okay. And you don't know who the entities are who made  
2 that election?

3 A. I do not, no.

4 Q. Okay. Now, I think you testified that there was -- that  
5 embedded into your assumption as to what the corporate  
6 opportunity was worth was an equity financing raise of what you  
7 estimated to be the present value of Wimrick of around 127  
8 million dollars; is that correct?

9 A. To adjust it slightly, we assumed for purposes of valuing  
10 the NOL that in order to obtain this more likely than not  
11 opinion that we were discussing earlier that the value of the  
12 investment we would assume for purposes of valuing the NOL that  
13 the size that would be limited to the value of the non-tax  
14 assets.

15 Q. And the NOL is good for twenty years, right?

16 A. And we've assumed a twenty-year run out of the NOL, yes.

17 Q. So what would happen if you did a transaction for 127  
18 million dollars of equity financing and then three years later  
19 you did another transaction for the larger entity, would that  
20 create 269 concerns for you?

21 A. I -- my understanding of 269 is that the facts and  
22 circumstances that exist will be evaluated, and they come back  
23 to the date today, which is what was the principal purpose of  
24 the acquisition for control pursuant to the plan. If and when  
25 there is a challenge to a subsequent larger investment, that

1 will be one of the factors that whomever makes that challenge,  
2 the IRS presumably, will take into consideration.

3 But as I understand, and I've been -- I've learned about  
4 269, those subsequent acquisitions, the facts and circumstances  
5 will be -- one of the facts and circumstances including the  
6 time between the plan and that acquisition could be one of the  
7 things that would inform a court's decision as to whether the  
8 principal purpose of the bankruptcy acquisition was for the  
9 avoidance of tax.

10 Q. But you -- okay. So if my first transaction was not a  
11 pure equity transaction, but was a leveraged transaction to try  
12 to make it as big as possible, and now I have this big combined  
13 entity with Wimrick. And then five years later I've decided to  
14 do another transaction to better utilize the NOL based off my  
15 larger size. Do you think that creates 269 if I stage my  
16 transactions that way?

17 A. A 269 risk exists as of the date the company emerges from  
18 bankruptcy.

19 Q. Right.

20 A. Okay. Subsequent transactions, in whatever form they  
21 take, will always be measured against the principal purpose of  
22 the acquisition for control as of the date of emergence. If it  
23 happens through debt in a year and equity four years from now,  
24 could the IRS choose to challenge that? I can't sit here and  
25 say I'm an IRS agent, but as I understand it those transactions



1 will always be subject to a look back to the principal purpose,  
2 if someone attempts to try to challenge it, i.e. if meaning the  
3 IRS.

4 So the risk exists upon emergence. Whether in fact  
5 subsequent transactions inform or, you know, result in that  
6 risk being, you know, materializing, that would be a facts and  
7 circumstances analysis. But again, the look back is to the  
8 acquisition of control today.

9 Q. But to be fair, that 269 analysis is something that you  
10 looked to Willkie to provide for you, right?

11 A. They were the independent tax adviser that we retained to  
12 help us think through these issues.

13 Q. Did you --

14 A. That's correct.

15 Q. Did you discuss with them this kind of like staging  
16 acquisitions, or the fact that you could have acquisitions that  
17 took place during the course of the twenty years that would  
18 take better utilization of the NOL and could potentially drive  
19 up the value of the corporate opportunity?

20 A. We did have those kinds of discussions, yes.

21 Q. You did have those discussions?

22 A. Yes.

23 Q. And how did that factor into your analysis?

24 A. Again, the very simple fact is, is that the acquisition of  
25 control we're talking about is the one pursuant to the plan,

1 and whether the principal purpose of that acquisition was the  
2 avoidance of taxes. What happens post-emergence could or could  
3 not step into the risk of 269, such that the NOLs themselves  
4 would become challenged.

5 And, you know, we did talk about whether acquisitions can  
6 happen a year, two, four, ten, twelve, and certainly the time  
7 between the acquisition and the emergence from bankruptcy would  
8 be one of the factors. But I don't know that 269 risk goes  
9 away.

10 Q. Did you factor into your analysis for purpose of valuing  
11 the corporate opportunity that you could potentially do staged  
12 transactions and the entity would gradually grow larger and you  
13 would have better utilization of the NOL than what you actually  
14 projected out?

15 A. Two things I'll react to from that standpoint. The longer  
16 you wait, the value of the NOL diminishes just from a time  
17 value standpoint. So if you want five or ten years to do  
18 something, regardless of what that means from 269, if you  
19 present valued that today you would get a very, very small  
20 number. But yes, we did talk about whether you can stage  
21 acquisitions and whether, in fact, that could create 269 risks,  
22 but the answer is always the same.

23 Since the acquisition for control is the emergency from  
24 bankruptcy and the principal avoidance -- the principal purpose  
25 tests are measured as of the date of the bankruptcy, any

1 subsequent transaction could trigger a review and risk of 269,  
2 which is why our view of the value of the NOL was that it was  
3 really akin to an option this company would have to make those  
4 acquisitions. But if there was significant tax risk, to put a  
5 lot of value on that option was something that we just didn't  
6 think was justified.

7 Q. All right. So when you analyzed the corporate  
8 opportunity, you limited the amount of the equity financing in  
9 conjunction with the advice given to you by the Willkie partner  
10 in order to feel -- so that he could feel more comfortable that  
11 you wouldn't have a 269 concern, correct?

12 A. I don't think the concern ever goes away. I think what we  
13 -- he -- what Mr. Reinhold testified to and what I have  
14 testified to is that the 127 number was consistent with the  
15 ability to suggest that it was more likely than not -- not  
16 zero, but more likely than not that any subsequent challenge by  
17 a court of the principal purpose of the acquisition pursuant to  
18 the plan would not be for tax avoidance.

19 Q. Okay. So --

20 A. So it's not that it goes away; it was just to be in the  
21 comfort zone that one could obtain a more likely than not  
22 opinion.

23 Q. So even though the basis of your structure was to fit  
24 within the Willkie comfort zone, you still took a discount on  
25 the corporate opportunity factor for the 269 risk?

1 A. I think the discount, if you're referring to the 5 to 20  
2 million dollar number, that was to account for the fact that  
3 there is still some residual 269 risk. But in fact, more  
4 importantly, it will take time to execute on that transaction.  
5 So the five to twenty considers a present value computation.  
6 If it takes a year or a year and a half to do something, the  
7 value of my NOL would come down to reflect the year.

8 It reflects the costs that reorganized WMI will have to  
9 incur between now and executing that acquisition that are not  
10 in any of the projections that we put together for purposes of  
11 valuing the NOL.

12 Q. And in the corporate opportunity discount, how much of  
13 that discount is reflected for the 269 risk where you  
14 structured the transaction to make it more comfortable for the  
15 Willkie partner to find a more likely than not scenario?

16 A. I don't know that I enjoy your characterization that more  
17 comfortable for the Willkie partner. I think Mr. Reinhold has  
18 many, many years of tax experience and, you know, he issues  
19 opinions as a firm.

20 THE COURT: Just answer. Just answer. Just --

21 Q. What percentage?

22 A. We didn't apply any specific percentage to any one factor  
23 in coming up with that discount.

24 Q. It was just the gestalt that you felt as to the aggregate  
25 number based on all the risks that --

1 A. I haven't spoke Yiddish in a while, but if one just looks  
2 at a two-year implementation, for example --

3 Q. It's not Yiddish.

4 A. Then if one just looks at a two-year implementation, the  
5 present value of the fifteen million dollars probably gets  
6 below ten. If one looks at having to hire a CEO and a  
7 corporate staff to make that acquisition, I would argue that  
8 the costs of the corporate staff that would be hired might be  
9 close to or in excess of that five million dollars. So the  
10 five million to twenty million is not a gestalt. It was, I  
11 looked at the present value as of today and said there's time  
12 to implement it, there's costs that will be incurred, and  
13 there's still risk. And I concluded --

14 Q. But you didn't --

15 A. And I concluded that the value here is really akin to an  
16 option value for the enterprise.

17 Q. But you didn't break it down to the individual risk that  
18 you saw. You took an aggregate risk based on all the things  
19 that you saw.

20 THE COURT: I think he said that.

21 MR. STEINBERG: Okay. I just wanted -- which is to me  
22 a gestalt, but I have no more questions.

23 THE COURT: All right.

24 MR. BERG: Your Honor, I'm sorry to extend this  
25 briefly, just two minutes if you could, please.

1 THE COURT: All right. Identify yourself for the  
2 record.

3 MR. BERG: Yes. Thank you, Your Honor. James Berg,  
4 equity security holder.

5 CROSS-EXAMINATION

6 BY MR. BERG:

7 Q. Mr. Zelin, you state that one element of execution risk is  
8 the ability to raise capital, correct?

9 A. Yes, that's correct.

10 Q. To minimize that execution risk under Section 269 with  
11 respect to a capital raise, you believe it is best to raise no  
12 more than 127.5 million dollars, due to the increased IRS  
13 scrutiny above that number, correct?

14 A. Based upon advice of counsel, that -- for purposes of  
15 valuing the net operating loss, that would be the number we  
16 were most comfortable using.

17 Q. Thank you. Is it your understanding that at present WMI  
18 bondholders under this plan are to be paid out billions of  
19 dollars, largely in cash?

20 A. I know the total payouts are probably in -- at least in  
21 excess of six billion dollars, yes.

22 Q. Thank you. If instead of paying off the existing WMI  
23 bondholders they were instead given new bonds in WMI rather  
24 than paying them out instead of raising new capital, would this  
25 reduce this execution risk, this capital-raising execution

1 risk?

2 A. The hypothetical is the company retains all its cash and  
3 issues 6 billion dollars of bonds?

4 Q. It wouldn't necessarily have to be six billion. That  
5 would be a theoretical maximum, yes.

6 A. Would there still be a change of ownership pursuant to the  
7 plan in that circumstance?

8 Q. I'm not certain. I thought there --

9 A. Because if it is an acquisition for control or a change in  
10 ownership there could be implications to the ability to use  
11 that cash for purposes of investing further. So I think the  
12 hypothetical requires a bit more detail than what you're  
13 suggesting --

14 Q. Okay. Perhaps --

15 A. -- what you're describing.

16 Q. All right. Perhaps then I should abandon this line  
17 without further understanding. Thank you.

18 A. You're welcome.

19 THE COURT: Thank you.

20 Q. It was my -- it had been my intention to suggest that this  
21 would reduce that weighted cost -- average cost of capital that  
22 Mr. Ard was speaking of.

23 A. Well, it also depends on the terms of the securities you  
24 would have to force creditors to take.

25 Q. Right. But if they were, I mean, paid back interest and

1 just given new bonds on the existing terms, would that reduce  
2 that execution risk?

3 A. Again, it goes to what terms they would get, whether they  
4 would take the bonds on the terms or whether the interest costs  
5 would be significantly higher, whether there's a willingness to  
6 do it or whether you can force it, whether you would have a  
7 change of ownership, an acquisition of -- there's lots of  
8 factors that would drive that analysis that I just can't  
9 analyze it on the hypothetical you've outlined.

10 Q. Okay. I just wanted to raise the point because it seems  
11 illogical to pay out seven billion dollars--

12 THE COURT: Well --

13 Q. -- nearly --

14 THE COURT: Don't make argument.

15 MR. BERG: I'm sorry. Okay. Thank you. All right.

16 I'll abandon that line of questioning. And thank you,

17 Mr. Zelin.

18 THE WITNESS: Thank you.

19 MR. SIEGEL: Martin Siegel from Brown Rudnick on  
20 behalf of the TPS consortium. As I understand it, the witness  
21 will not be back tomorrow if there are no further questions, so  
22 I have a quick procedural issue.

23 THE COURT: Well, I'm ready to quit now.

24 MR. SIEGEL: Well, I'm hoping --

25 THE COURT: If there are a lot of questions I'm going



1 to make him come back.

2 MR. SIEGEL: I do not have a lot of questions. I  
3 really have just two procedural matters to make sure that the  
4 way the TPS consortium is approaching the witness is acceptable  
5 to the Court. And that is, we're relying on and have  
6 designated certain testimony from his prior testimony at the  
7 prior hearing. We had some conversations with the debtor, and  
8 they appear to agree that we will be able to use testimony from  
9 the prior hearing in connection with this hearing. But nobody  
10 has discussed that with the Court. So we didn't want to let  
11 the witness go and then find that the Court --

12 THE COURT: Good point.

13 MR. SIEGEL: -- had some problem with that procedure.

14 THE COURT: Good point. Are all the parties agreeable  
15 that -- and what portion of the prior confirmation hearing are  
16 we incorporating, all of it?

17 MR. SIEGEL: No. We've designated Mr. Zelin's trial  
18 testimony pages 18 to 22 is all we've -- and we've set -- you  
19 know, we've served that on all the parties what that  
20 designation was. We've done that for some other witnesses too,  
21 but I wanted to make sure that Mister -- you know, that we  
22 didn't let Mr. Zelin go and find that there was an issue with  
23 that.

24 MR. MASTANDO: Your Honor, as to hearing testimony  
25 we're okay with that, but not prior deposition testimony from

1 before the prior confirmation hearing.

2 MR. SIEGEL: What we have designated for Mr. Zelin is  
3 his testimony for this -- his deposition, certain portions of  
4 his deposition for this hearing, which we intend to rely on.  
5 And if we can do that then we also don't have to cross-examine  
6 him. And we think under 803(d)(2)(D) I think it is, as a agent  
7 of a party, we're allowed to rely on the party's admission upon  
8 that testimony at least for hearsay purposes. We haven't  
9 received any objections to our designations. They certainly  
10 have the relevancy or anything else as, you know, as to that if  
11 they make such an objection. But we wanted to make sure that  
12 we are not faced with a hearsay objection by --

13 THE COURT: I hear what your argument is. Is the  
14 debtor agreeable that deposition testimony of depositions taken  
15 in connection with the present confirmation hearing may be --

16 MR. MASTANDO: No, I --

17 THE COURT: -- introduced into evidence?

18 MR. MASTANDO: The present -- the deposition testimony  
19 in connection with today's hearing I believe can be designated,  
20 but not the testimony prior to that.

21 MR. SIEGEL: And what we've designated is deposition  
22 testimony taken in connection with this hearing, recent  
23 testimony. And in that case then, Your Honor, we will have no  
24 questions for Mr. Zelin today.

25 THE COURT: Okay. And no redirect?

1 MR. MASTANDO: Nothing further, Your Honor.

2 THE COURT: All right. We can release the witness?

3 THE WITNESS: Thank you.

4 THE COURT: All right. You're released.

5 And we'll -- when are we coming back here tomorrow?

6 (Pause)

7 THE COURT: On the record.

8 MR. MASTANDO: Yes. It's the portions that he -- that  
9 they designated in connection with this hearing, not all the  
10 testimony. I believe certain portions were designated.

11 MR. SIEGEL: We're only seeking to introduce the stuff  
12 that we have designated.

13 MR. MASTANDO: Okay.

14 THE COURT: Well, I'm not making a ruling that nobody  
15 else can introduce deposition --

16 MR. MASTANDO: That's fine.

17 THE COURT: -- testimony. You're -- I'm simply  
18 getting your agreement to his designation.

19 MR. MASTANDO: Right. His designation, that's all I  
20 wanted to clarify.

21 THE COURT: All right.

22 MR. MASTANDO: It's not the entire deposition.

23 (Pause)

24 MR. ROSEN: Your Honor, counsel has a concern based  
25 upon the scheduling for tomorrow. We understand that we're

1 going to be starting at one o'clock. We know that we have Mr.  
2 Goulding on, we have Mr. Maxwell on, subject to cross-  
3 examination for both of those people. Counsel is concerned  
4 about whether or not his client needs to come for tomorrow  
5 versus Friday morning.

6 MR. TRACHTMAN: It just -- it sounded like we were  
7 probably going to be very close to the end of the day tomorrow,  
8 and it might make sense for -- to start first thing Friday  
9 morning with module three. But if -- since we did finish Mr.  
10 Zelin this evening, we may actually be able to move faster  
11 tomorrow. So I mean, we don't want to hold things up.

12 MR. ROSEN: So then have your client here.

13 MR. TRACHTMAN: So --

14 THE COURT: Well, how long is the debtor going to take  
15 for module two?

16 MR. ROSEN: Your Honor, we only have as our witness in  
17 that second piece, I'll call it a tranche, a mod, Mr. Goulding.  
18 As I said before, it'll be approximately thirty-five or forty-  
19 five minutes of direct. I have no idea the length of cross-  
20 examination. The equity committee is going to put on Mr.  
21 Maxwell. We do have a considerable amount of cross-examination  
22 of Mr. Maxwell. So all in, Your Honor, I would say that it  
23 would take two to three to three-and-a-half hours perhaps for  
24 those two witnesses.

25 THE COURT: All right. I think we'll be done tomorrow

1 after then, because given the estimates -- everybody's  
2 estimate. I'm sure we'll go beyond 5:00 so I'd rather not.  
3 You can bring your witness on Friday morning then --

4 MR. TRACHTMAN: Okay. Thank you, Your Honor.

5 THE COURT: -- at 9:30. We'll recess now and be back  
6 here at 1:00.

7 You can leave your documents. I do have a hearing  
8 here at 11:30 that will be very short, but I will --

9 MR. MASTANDO: Your Honor --

10 THE COURT: -- trust counsel not to interfere with  
11 your documents.

12 MR. MASTANDO: I apologize. May Mr. Zelin be released  
13 from trial?

14 THE COURT: He is released.

15 MR. MASTANDO: Thank you, Your Honor.

16 MR. STRATTON: Your Honor, we just said we would start  
17 at 9:30 on Friday?

18 THE COURT: Nine -- isn't that when we're starting?  
19 That's what I have, 9:30 on Friday.

20 MR. STRATTON: Thank you very much, Your Honor.

21 THE COURT: All right. We'll stand in recess.

22 (Whereupon these proceedings were concluded at 6:44 p.m.)  
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C E R T I F I C a T I O N

I, Clara Rubin, certify that the foregoing transcript is a true and accurate record of the proceedings.

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CLARA RUBIN

AAERT Electronic Certified Transcriber cet\*\*d-491

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Date: July 15, 2011