EXHIBIT 3

Brief

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

In re	:	Chapter 9
CITY OF DETROIT, MICHIGAN,	:	Case No. 13-53846
Debtor.	:	Hon. Steven W. Rhodes
AMBAC ASSURANCE CORPORATION,	:	Chapter 9
Plaintiff,	:	Adv. Pro. No. 13-05310
v.	:	Hon. Steven W. Rhodes
THE CITY OF DETROIT, MICHIGAN, KEVYN D. ORR, individually and in his official capacity as the EMERGENCY MANAGER, JOHN NAGLICK, individually and in his official capacity as FINANCE DIRECTOR, MICHAEL JAMISON individually and in his official capacity as DEPUTY FINANCE DIRECTOR, and CHERYL JOHNSON, individually and in her official capacity as TREASURER,	:	
Defendants.	:	

MEMORANDUM IN SUPPORT OF THE INDIVIDUAL DEFENDANTS' MOTION TO DISMISS THE COMPLAINT

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Defendants Kevyn D. Orr, John Naglick, Michael Jamison, and Cheryl Johnson (collectively, the "individual defendants") file this memorandum in support of their motion, pursuant to Fed. R. Civ. P. 12(b)(6), made applicable to this proceeding by Fed. R. Bankr. P. 7012(b), to dismiss the complaint of Ambac Assurance Corporation ("Ambac" or the "monoline").

I. BACKGROUND

Ambac filed this action seeking a declaration that the City of Detroit and the individual defendants are required to deposit the City's *ad valorem* tax revenues into specific Debt Retirement Funds (Compl. ¶¶ 57-59), and to segregate and not to commingle the *ad valorem* tax revenues with the City's other funds (*id.* ¶¶ 60-62); are prohibited from using the City's *ad valorem* tax revenues for any purpose other than repaying bondholders (*id.* ¶¶ 63-65); and are barred from granting super-priority status or any other interest to any other creditor or person that would impair Ambac's alleged interests (*id.* ¶¶ 66-68). Finally, Ambac requests injunctive relief enjoining defendants to comply with any declaratory relief that Ambac is granted (*id.* ¶¶ 69-70).

The factual background of the case and this motion is set forth in the memorandum filed by the City this day in support of its companion motion to dismiss Ambac's complaint, and for the convenience of the Court the individual defendants incorporate that material by reference. *See* Memorandum Of The City

Of Detroit In Support Of Motion To Dismiss, pp. 1-6. However, at bottom, the monoline has sued for declaratory and injunctive relief to require the City and the individual defendants to adhere to the monoline's reading of Section 701 of the Revised Municipal Finance Act, Act 34 of 2001, MCL § 141.2701 ("RMFA").

Ambac evidently joined the individual defendants as parties – in both their individual and official capacities – in an effort to intimidate them or to exert additional leverage over the City. In support, the monoline cites a subsection of § 701 that makes "[a]n officer who willfully fails to perform duties required by" § 701 "*personally liable* to the municipality or to a holder of a municipal security for loss or damage arising from his or her failure." Compl. ¶ 47 (emphasis supplied by Ambac, and not in original statutory text). However, when challenged by the Court, counsel retreated, denying that the monoline was seeking to impose personal liability on the individual defendants. *See* Transcript of December 3, 2013 Hearing on Motion For Expedited Adjudication Of Complaint, pp. 23:18-24:4, attached to the Motion to Dismiss as Exhibit 6.

II. ARGUMENT

A. The Claims Against The Individual Defendants Should Be Dismissed For The Same Reasons Demonstrated In The City Of Detroit's Motion To Dismiss

In addition to the arguments set forth below, the individual defendants hereby adopt, and incorporate by reference, all of the arguments made by

codefendant the City of Detroit in its motion to dismiss Ambac's complaint. *See* Memorandum Of The City Of Detroit In Support Of Motion To Dismiss, filed December 9, 2013.

B. The Complaint's Conclusory Assertions Fail To State A Claim Upon Which Relief Can Be Granted

It is well established that "[t]hreadbare recitals of the elements of a cause action, supported by mere conclusory statements" are insufficient to survive a motion to dismiss. *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). Yet, with respect to the claims against the individual defendants, Ambac has tendered only "'naked assertions' devoid of 'further factual enhancement.'" *Id.* (quoting *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 557 (2007)). Accordingly, as explained in detail below, Ambac's claims should be dismissed.

Fed. R. Civ. P. 8(a)(2), made applicable to this proceeding by Fed. R. Bankr. P. 7008(a), "requires that a pleading contain 'a short and plain statement of the claim showing that the pleader is entitled to relief.'" *Kapla v. Fannie Mae (In re Kapla)*, 485 B.R. 136, 140 (Bankr. E.D. Mich. 2012). "The purpose of this pleading standard is 'to give the defendant fair notice of what the . . . claim is and the grounds upon which it rests.'" *Id.* (quoting *Twombly*, 550 U.S. at 555).

As the Supreme Court has explained, "[t]o survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Iqbal*, 556 U.S. at 678 (quoting *Twombly*,

550 U.S. at 570). Two key principles underlie this requirement. "First, the tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions." *Id.* In other words, a court is "not bound to accept as true a legal conclusion couched as a factual allegation." *Id.* at 678 (quoting *Twombly*, 550 U.S. at 555). Second, "[a] claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Id.*

Here, Ambac's claims against the individual defendants are based on RMFA § 701(7), which provides that "[a]n officer who *willfully* fails to perform *duties required by this section* is personally liable to the municipality or to a holder of a municipal security for *loss or damage arising from his or her failure*." MCL § 141.2701(7) (emphases added); s*ee* Compl. ¶¶ 6, 47. But Ambac has failed to make competent factual allegations regarding *any* element of its claims against the individual defendants. Instead, the complaint merely lists the names, titles, and some of the hiring dates for the individual defendants (Compl. ¶¶ 15-18), quotes a statutory provision (*id.* ¶ 6), and then paraphrases the same statutory provision (*id.* ¶ 47).[1] The complaint does not contain any factual allegations concerning the

[1] "Based on the City's representations, and the duties and responsibilities of the Emergency Manager, the CFO, the Finance Director, the Deputy Finance Director, and the Treasurer, the Individual Defendants have willfully failed to

purported "duties" of Kevyn Orr, John Naglick, Michael Jamison, or Cheryl Johnson under § 701 of the RMFA. Nor does it contain factual allegations relating to the specific acts or omissions that purportedly constituted a "fail[ure] to such "duties," § 701(7). In short, the complaint lacks any factual allegations that are relevant to the elements of Ambac's claims against the individual defendants.

Ambac's pleading is defective in other respects as well. Section 701(7) is limited to circumstances in which the relevant official "willfully" failed to perform his or her responsibilities under the section. Under Michigan law, willfulness is limited to an act or omission "that was intended to harm the plaintiff." *Odom v. Wayne County*, 760 N.W.2d 217, 225 (Mich. 2008) ("our standard civil jury instructions define 'willful misconduct' as 'conduct or a failure to act that was intended to harm the plaintiff'"). But the complaint in the present case contains

(continued…)

perform their duties under Act 34 and therefore are personally liable to Ambac for loss or damage arising from those failures."

The complaint also asserts that "the City's then finance director" – who, at the relevant times, was not John Naglick or any other party here – issued certain sale orders years ago, *see* Compl. ¶¶ 26-28, but this is merely a background assertion that has nothing to do with Ambac's claims against the individual defendants. The complaint's only other references to the individual defendants appear in the description of relief sought, *see, e.g.*, *id.* ¶¶ 59, 62, and in a one-sentence legal conclusion about the purported inapplicability of 11 U.S.C. § 904, *see* Compl. ¶ 12.

absolutely no allegation that the individual defendants "intended to harm" Ambac or, for that matter, what specific acts the individual defendants took at all.

Additionally, Ambac's legal theory requires it to establish that any "loss or damage" it suffered "aris[es] from" the individual defendants' "failure" to perform duties under § 701 of the RMFA. "To establish the requisite proximate cause between the alleged wrongful act and resulting damages, as required when liability is at issue in any action," Ambac at a minimum would have to prove that the individual defendants' "conduct was both a cause in fact and a legal, or proximate, cause of [its] damages." *Lamp v. Reynolds*, 645 N.W.2d 311, 316 (Mich. Ct. App. 2002). Yet the complaint is devoid of any allegation regarding the causal connection between the monoline's purported "loss" and the individual defendants' alleged failure to perform duties under § 701.[2]

In sum, the complaint's "labels," "conclusions," and "formulaic recitation of the elements of the cause of action" are plainly insufficient. *See Twombly*, 550

[2] The complaint also lacks allegations about the powers and authorities that each of the individual defendants may or may not have to carry out the actions that are the subject of Ambac's requested injunctive order. Indeed, the complaint completely fails to address – or event recite – the elements of the standard for an injunction. *See Lucky's Detroit, LLC v. Double L, Inc.*, 2013 U.S. App. LEXIS 16589 (6th Cir. 2013) (citation omitted) ("A court may issue a permanent injunction when the party requesting the injunction demonstrates that: (1) it will suffer an irreparable injury absent an injunction; (2) legal remedies, such as money damages, provide inadequate compensation; (3) the balance of hardships warrants an injunction; and (4) the public interest would not be disserved by an injunction.").

at 555. As a result, the claims against the individual defendants should be dismissed for failure to state a claim. *See, e.g.*, *Kapla*, 485 B.R. at 138, 140, 152-153 (granting a motion to dismiss in an adversary proceeding pursuant to Fed. R. Bankr. P. 7012 and Fed. R. Civ. P. 12(b)(6)); *In re Bajas*, 443 B.R. 768, 770-772, 774-776 (Bankr. E.D. Mich. 2011) (same).

C. Ambac's Claims Should Be Dismissed Because They Fall Outside The Narrow Scope Of RMFA § 701(7)

As the City pointed out in its accompanying motion to dismiss, there is no private right of action under the Revised Municipal Finance Act. *See* Memorandum Of The City Of Detroit In Support Of Motion To Dismiss, pp. 7-10. Here, even if there were a private right of action under the statute, Ambac has not made out a viable claim against the individual defendants.

The provision of the RMFA that imposes personal liability is § 701(7), which provides that "[a]n officer who willfully fails to perform duties required by this section is personally liable to the municipality or to a holder of a municipal security for loss or damage arising from his or her failure." This provision's "willful[ness]" requirement strongly suggests that a claim brought under the provision sounds in tort. *See generally Odom*, 760 N.W.2d at 225 (discussing, in the context of tort liability, the meaning of willfulness).

Claims sounding in tort that are asserted against governmental officers implicate the principle of "governmental immunity." Governmental immunity is

"the public policy, derived from the traditional doctrine of sovereign immunity, that limits imposition of tort liability on a governmental agency." *Nawrocki v. Macomb County Road Comm'n*, 615 N.W.2d 702, 709-10 (Mich. 2000). Michigan law provides immunity to governmental officers in a variety of circumstances. *e.g.*, MCL §§ 691.1407(2), (3), (5). Governmental immunity can only be waived "'by an express statutory enactment or by necessary inference from a statute.'" *Ballard v. Ypsilanti Township*, 577 N.W.2d 890, 895 (Mich. 1998) (citation omitted).

To the extent that § 701(7) can be viewed as a waiver of – or departure from –governmental immunity, it must be narrowly construed. Indeed, the Supreme Court of Michigan has expressly reaffirmed the "basic principle" that "the immunity conferred upon governmental agencies is *broad*, and the statutory exceptions thereto are to be *narrowly* construed." *Nawrocki*, 615 N.W.2d at 711. And where there "is a narrowly drawn exception to a broad grant of immunity, there must be strict compliance with the conditions and restrictions of the statute." *Id.* Consequently, the court must "strictly abide by" § 701's "statutory conditions in deciding the instant case." *Id.*

One critical statutory condition found in § 701(7) is that any liability arising under that provision must be based on a willful "fail[ure] to perform duties required by *this section*." *Id.* (emphasis added). A close examination of "this

section" – namely, § 701 – reveals that its primary purpose is to require municipal finance officers to levy the necessary tax. *See, e.g.*, § 701(1) (requiring the officer or official body to "include all of the following in the amount of taxes levied each year"); § 701(3) ("the municipality shall levy the full amount of taxes required by this section for the payment of the municipal securities without limitation as to rate or amount").

Here, Ambac does not allege that the individual defendants failed to levy the relevant tax. On the contrary, the gravamen of the complaint is instead that defendants are "unlawfully diverting" *ad valorem* taxes "that the City must levy and collect for the sole purpose of paying principal and interest" on the relevant bonds. Compl. ¶ 1; *see also id.* ¶ 10 (referring to the "City's refusal to segregate the Restricted Funds," and its "improper use of the Restricted Funds"); *id.* ¶ 9 ("The City has stated publicly that it intends to continue to levy and collect the Restricted Funds . . . ."); *id.* ¶ 10 (referring to the "City's refusal to segregate the Restricted Funds," and its "improper use of the Restricted Funds"); *id.* ¶ 48 ("prior to its Chapter 9 filing, the City collected and set aside the portion of the *ad valorem* taxes specified for repayment of the Unlimited Tax Bonds, as required by Michigan law"); *id.* ¶ 51 ("the City indicated that it would continue to collect the Restricted Funds"); *id.* ¶ 56 (referring to "the funds specifically collected for the purpose of paying the Bondholders"). But these allegations – if assumed to be true

– at most would establish a violation of RMFA § 705, not § 701. In relevant part, § 705 provides:

> Debt retirement funds . . . shall be accounted for separately and . . . *shall be used only to retire the municipal securities of the municipality for which the debt retirement fund was created*.

(Emphasis added).[3] Section 705, unlike § 701, does not permit the imposition of personal liability for violation of its provisions.

Thus, the claims against the individual defendants do not fall within § 701(7) because they do not rest on an alleged failure to perform duties required by *that section* and, likewise, any "loss or damage" allegedly suffered by Ambac does not "aris[e] from" a "failure" to perform duties set forth in § 701. To the extent that Ambac has pled a violation of § 705, that section does not permit the imposition of personal liability against individual defendants.

In any event, even if § 701(7) were to apply based on the allegations in the complaint (which it does not), it does not apply to Kevyn Orr. Under Michigan law, "the elective or *highest appointive executive official of all levels of government* are immune from tort liability for injuries to persons or damages to property if he or she is acting within the scope of his or her judicial, legislative, or

[3] That same section also states that "[d]ebt retirement funds created for the following categories of debt evidenced by a municipal security may be pooled or combined for deposit or investment purposes only with other debt retirement funds created for the same category of debt evidenced by a municipal security: (a) Voted debt. . . ." § 705.

executive authority." MCL § 691.1407(5) (emphasis added). Kevyn Orr falls within this statutory "grant of absolute immunity to high-ranking officials," *Odom*, 760 N.W.2d at 223, as the "highest appointive executive official" of a level of government. *See, e.g.*, *Payton v. City of Detroit*, 536 N.W.2d 233, 242 (Mich. Ct. App. 1995) (concluding that Detroit's police chief was covered by this provision); *Nalepa v. Plymouth-Canton Cmty. Sch. Dist.*, 525 N.W.2d 897, 901-02 (Mich. Ct. App. 1994) (holding that the superintendent of a school district was covered); *Bischoff v. Calhoun Co. Prosecutor*, 434 N.W.2d 249, 251 (Mich. Ct. App. 1988) (*per curiam*) (concluding that a county prosecutor was covered); *see also Grahovac v. Munising Township*, 689 N.W.2d 498, 504 (Mich. Ct. App. 2004) (Griffin, J., dissenting) (collecting cases).

In sum, the claims against the individual defendants have no basis in the RMFA and must be dismissed.

D. The Bond Resolutions Did Not Confer Any Rights Against The Individual Defendants And, In Any Event, Plaintiff Released Any Claims It May Have

Ambac's complaint is predicated upon the theory that defendants were required to strictly segregate *ad valorem* taxes the City collected and to apply those funds solely for the purpose of paying principal of and interest on the unlimited and limited tax general obligation bonds issued by the City ("UTGOs" and "LTGOs," respectively). In practice, this requirement flows from the relevant

bond resolutions. *See* Mich. Dep't of Treasury, Accounting Procedures Manual for Local Units of Government in Michigan, Chapter 3, p. 13 (July 2007) ("Separate investment and/or bank savings accounts may be required for each bond issue, debt fund and capital projects fund *as specified within the specific bond ordinance or resolution* . . . .") (emphasis added).

Each of the relevant bond resolutions expressly states that "[t]he provisions of this Resolution . . . shall constitute a contract between the City, the Paying Agent, the Bond Insurer, if any, and the Bondowners."[4] The bond resolutions further contain a release of all claims against individual municipal officers relating to the payment of principal or interest on the bonds:

> No Recourse Under Resolution. All covenants, agreements and obligations of the City contained in this Resolution shall be deemed to be the covenants, agreements and obligations of the City and not of any councilperson, member, officer or employee of the City in his or her individual capacity*, and no recourse shall be had for the payment of the principal of or interest on the Bonds or for any claim based thereon* or on this Resolution against any councilperson, member, officer or employee of the City or any person executing the Bonds in his or her official individual capacity.

Ex. D to Compl. (ECF No. 6, at 32, 64, 79) (emphasis added).

This broad language clearly releases any claims that the bondholders – and the monoline who now stands in the shoes of the bondholders – may have against the individual defendants for payment of principal and interest on the bonds.

[4] Ex. D to Compl. (ECF No. 6, at 33, 64, 79).

Under Michigan law, "[t]he validity of a contract of release turns on the intent of the parties," and "a release must be fairly and knowingly made." *Skotak v. Vic Tanny Int'l*, *Inc.*, 513 N.W.2d 428, 429-30 (Mich. Ct. App. 1994); *see also Batshon v. Mar-Que Gen. Contractors*, 624 N.W.2d 903, 906 n.4 (Mich. 2001).[5] Here, the release was given by sophisticated parties, advised by experienced counsel. And there is no doubt about the meaning of the release, which unambiguously states that "no recourse shall be had . . . for *any* claim based . . . on this Resolution against *any* . . . officer of employee of defendants or *any* person executing the Bonds in his or her official individual capacity." (Emphases added.) The unambiguous releases should, therefore, be enforced according to their terms. Since any claims against the individual defendants were previously released, Ambac cannot now bring such claims.

III. CONCLUSION

For the foregoing reasons, the individual defendants submit that the Complaint should be dismissed as to them with prejudice.

[5] To the extent that Michigan law excepts willful conduct from contractual releases, *see, e.g.*, *Lamp v. Reynolds*, 645 N.W.2d at 314, such an exception should not be applied in this case because there is no factual allegation here of any specific willful conduct by the individual defendants, and such an exception should not be applied in cases involving defendants who are governmental officers.

Dated: December 9, 2013 Respectfully submitted,

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[6] National Public Finance Guarantee Corporation ("National") recently indicated to Jones Day its concern that Jones Day may have a conflict of interest in representing the City against National in Adversary Proceeding 13-05309, a companion to this adversary proceeding, which National brought against the City on November 8 and in which Jones Day has already appeared. (National is a Jones Day client in unrelated matters. National has consented to Jones Day's taking adverse positions in certain circumstances.) In the time available, Jones Day has not been able to complete its investigation into National's concerns. In an abundance of caution, Jones Day is not appearing as counsel of record in Adversary Proceeding 13-05309 until this issue is resolved. Jones Day has no conflict it is aware of in this adversary proceeding, and will continue to appear as counsel of record in this case.

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