

SETTLEMENT AGREEMENT

THIS **SETTLEMENT AGREEMENT** (the “Agreement”) is made as of August 31, 2011 by and between the CITY OF NEW YORK DEPARTMENT OF FINANCE (the “City”) and AMBAC FINANCIAL GROUP, INC. (“AFG”) on behalf of itself and all of its affiliates that are or were members of the combined tax group for purposes of filing general corporation tax returns with the City for one or more tax years during the period from January 1, 2000 through and including December 31, 2010 (collectively, the “Combined Group”). The City and AFG are also referred to herein each as a “Party” and collectively as the “Parties.”

RECITALS

- A. For each of the tax years 2000 through and including 2009, AFG and certain members of the Combined Group filed a combined general corporation tax return with the City.
- B. As of November 8, 2010, the liability of AFG and the members of the Combined Group for taxes owed to the City for tax years 2000 through 2009 had been the subject of a pending dispute.
- C. On November 8, 2010 (the “Commencement Date”), AFG commenced a voluntary case (the “Chapter 11 Case”) under chapter 11 of title 11 of the United States Code (the “Bankruptcy Code”). AFG continues to operate its business and manage its assets as debtor in possession as authorized by sections 1107(a) and 1108 of the Bankruptcy Code.
- D. On December 14, 2010, the City filed proof of claim number 4 in the Chapter 11 Case, asserting that AFG owes it \$116,817,949.00, comprised of \$77,940,995.00 in principal and \$38,876,954.00 in interest thereon for the tax years commencing on January 1, 2000 and ending December 31, 2010 (the “Tax Claim”). Similarly, the City contends that each of the members of the Combined Group is severally liable to the City in the same amount for the same tax period.
- E. On May 23, 2011, AFG filed its *Objection and Request to Disallow the Claim Submitted by the City of New York Department of Finance* [Docket No. 278] objecting to the Tax Claim.
- F. On July 6, 2011, the City filed its *Response in Opposition to Ambac Financial Group, Inc.’s Objection and Request to Disallow the Proof of Claim Filed by the City of New York Department of Finance* [Docket No. 346] (the “Response”).
- G. The Parties desire to resolve their differences without further resort to litigation and, as a result of the Parties’ good faith and arm’s length negotiations, have agreed to the settlement set forth herein.

AGREEMENT

In consideration of the foregoing and such other good and valuable consideration discussed below, the Parties agree as follows:

1. Tax Periods Affected This Agreement will resolve any and all remaining tax liability of AFG and the Combined Group to the City for the period from January 1, 2000 through and including December 31, 2010 (the “Relevant Tax Period”).

2. Disposition of the Tax Claim The Tax Claim shall be allowed as an unsecured priority claim under 11 U.S.C. § 507(a)(8) in the total amount of \$3,233,611.00. The balance of the Tax Claim shall be disallowed with prejudice. The Tax Claim shall be deemed to be satisfied in full by the Settlement Consideration discussed below.

3. Settlement Consideration **In full and final satisfaction of the Tax Claim and all tax liability owed by AFG and the Combined Group to the City for the Relevant Tax Period, the City shall:** (i) receive a cash payment of two million dollars (\$2,000,000.00) from AFG (the “Cash Consideration”) and (ii) apply in settlement of the Tax Claim, rather than refund or apply to any other tax claim or tax period, the \$1,233,611.00 in funds currently on deposit with the City as a result of payments previously made by AFG to the City prior to the Commencement Date (the “Credit Consideration” and collectively with the Cash Consideration, the “Settlement Consideration”).

4. Transfer of Settlement Consideration Upon entry of a final non-appealable order: (i) AFG will remit the Cash Consideration to the City and (ii) AFG and the Combined Group shall be deemed to have surrendered all right, title and interest in and to the Credit Consideration. For purposes of this Agreement, a final non-appealable order shall mean an order entered by the Bankruptcy Court authorizing AFG to consummate this Agreement, unless any objection to such order shall have been properly made and overruled, in which case the time for filing a notice of appeal from such order shall have lapsed without any stay in effect or notice of appeal having been filed, or if any notice of appeal has been filed and a stay obtained, such appeal has been finally adjudicated.

5. Release of AFG and the Combined Group Effective upon the transfer of the Settlement Consideration, the City shall be deemed to have released AFG and each member of the Combined Group from any and all claims relating to the Tax Claim and any other general corporation tax claim that the City may have for the tax period from January 1, 2000 through and including December 31, 2010 (collectively, with the Tax Claim, the “Tax Claims”) and including, without limitation, as defined in section 101(5) of the Bankruptcy Code, defaults, obligations, rights, damages, causes of action, demands, suits, judgments, remedies, setoffs, recoupments, defenses, debts, and liabilities of any kind or nature whatsoever, under any legal

theory, including under contract, tort, or otherwise, whether at law, in equity, or otherwise, whether known or unknown, matured or unmatured, fixed or contingent, liquidated or unliquidated, disputed or undisputed, asserted or unasserted, suspected or unsuspected, foreseen or unforeseen, direct or indirect, choate or inchoate, now existing or hereafter arising that the City may now have, has ever had or may in the future have, against AFG or a member of the Combined Group, which relate to the Tax Claims and occurring from the beginning of time through and including the date of this Agreement.

6. **Counterparts** This Agreement may be executed in several counterparts (including by facsimile transmission or electronic transmission of a portable document format file), each of which shall be an original and all which together shall constitute a single agreement.

7. **Amendments** No amendment, modification or waiver in respect of this Agreement will be effective unless in writing (including writing evidenced by facsimile transmission or electronic transmission of a portable document format file) and executed by each of the Parties.

8. **Severability** If any term or other provision of this Agreement is invalid, illegal or incapable of being enforced under any law or public policy, all other terms and provisions of this Agreement shall nevertheless remain in full force and effect for so long as the economic or legal substance of the settlement is not affected in any manner materially adverse to either Party hereto. Upon such determination that any term or other provision is invalid, illegal or incapable of being enforced, the Parties shall negotiate in good faith to modify this Agreement so as to effect the original intent of the parties as closely as possible in an acceptable manner so that the settlement is consummated as originally contemplated to the greatest extent possible.

9. **Entire Agreement** This Agreement sets forth the entire understanding and agreement between the Parties as to the matters covered herein and supersedes and replaces any prior understanding, agreement or statement of intent, in each case, written or oral.

10. **Binding Nature** The terms and provisions of this Agreement shall be binding in all respects on, and shall inure to the benefit of, the Parties, their estates and their respective successors and assigns, including any trustee, receiver, conservator, rehabilitator, liquidator, or superintendent relating to the reorganization, rehabilitation, liquidation, conservation or dissolution of any of the Parties. The members of the Combined Group are third-party beneficiaries of this Agreement and the terms and provisions of this Agreement benefiting the members of the Combined Group shall be binding and inure to their benefit and to the benefit of their respective successors and assigns.

11. Joint Drafting This Agreement is the product of negotiations between the Parties and any rule of construction that ambiguities are to be resolved against the drafting Party shall not apply in the interpretation of this Agreement.

12. AFG's Representation AFG acknowledges and agrees that in entering into this Agreement the City has relied on AFG's statements relating to its financial condition as set forth in the Disclosure Statement of Ambac Financial Group, Inc., dated July 8, 2011, and the Plan of Reorganization annexed thereto [Docket No. 387], which have been filed in the Chapter 11 Case, and AFG represents that such statements were true and correct when made.


13. No Admissions This Agreement reflects a compromise of a disputed claim and shall not be construed as an admission against any Party's interest and shall not be used as or deemed to be evidence of any liability by any Party in any proceeding before the Bankruptcy Court or any other court, except in a proceeding to enforce the terms of this Agreement.

14. Choice of Law and Forum This Agreement shall be governed by and construed in accordance with the laws of the State of New York without regard to the conflict of law principles thereof. All disputes arising out of or related to the Agreement shall be subject to the exclusive jurisdiction of the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court"). To the extent the Bankruptcy Court does not exercise its jurisdiction over any dispute arising out of or relating to this Agreement, such dispute(s) shall be subject to the exclusive jurisdiction of the courts located within the State of New York.

15. Condition to Effectiveness This Agreement shall not be effective and shall have no force and effect unless and until this Agreement shall have been approved by an order of the Bankruptcy Court.

IN WITNESS WHEREOF, AFG, on behalf of itself and each member of the Combined Group, and the City each caused this Agreement to be executed by its duly authorized representative, as of the date first above written.

MICHAEL A. CARDOZO
Corporation Counsel of the City of New York
Attorney for the City of New York Department of Finance

By: 

Andrew G. Lipkin
Senior Counsel

AMBAC FINANCIAL GROUP, INC.
On behalf of itself and each member of the Combined Group

By: _____
Name:
Title:

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MICHAEL A. CARDOZO
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Attorney for the City of New York Department of Finance

By: _____
Andrew G. Lipkin
Senior Counsel

AMBAC FINANCIAL GROUP, INC.
On behalf of itself and each member of the Combined Group

By:  _____
Name:
Title: **David Trick**
Senior Managing Director,
CFO and Treasurer