

Bond Case Briefs

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BONDS - ALABAMA

Water Works Bd. of City of Birmingham v. AMBAC Financial Group, Inc.

United States Court of Appeals, Eleventh Circuit - August 5, 2013 - Fed.Appx. - 2013 WL 3970904

The Board created the Reserve Fund by purchasing a surety bond from Ambac, which had a AAA rating at the time. In June 2008 Ambac's rating was downgraded to AA. As a result, the Board had to put cash in the Reserve Fund. When that happened, the Board sued Ambac for breach of contract, fraud, suppression of truth, and negligence.

The Water Works Board of the City of Birmingham appealed the district court's dismissal of its claim against Ambac Financial Group, Inc. for failure to state a claim upon which relief can be granted.

In March 2007 the Board issued water and sewer revenue bonds. To do that, it was required to establish a Reserve Fund. One of the ways the Board could satisfy the requirements for the Reserve Fund was by purchasing a surety bond from an issuer that had a credit rating of AAA. If the issuer's rating fell below AAA while the bonds were still outstanding, the Board was required to deposit into the Reserve Fund the amount of all outstanding securities or replace the original surety bond with another bond from an issuer that had a AAA rating.

The Board created the Reserve Fund by purchasing a surety bond from Ambac, which had a AAA rating at the time. In June 2008 Ambac's rating was downgraded to AA. As a result, the Board had to put cash in the Reserve Fund. When that happened, the Board sued Ambac for breach of contract, fraud, suppression of truth, and negligence.

The district court dismissed the Board's breach of contract claim, reasoning that the contract between Ambac and the Board did not require that Ambac keep its AAA rating. The Board argued that the Trust Indenture, which provided the terms for the Board's issuance of the water and sewer bonds, imposed a contractual obligation on Ambac to maintain a AAA credit rating. The court found that, even if it was assumed that Ambac was bound by the Trust Indenture, the Board had not stated a viable claim for breach of contract. The Indenture did not require the bond issuer to keep a AAA rating. On the contrary, it explicitly acknowledged the possibility of the issuer's rating being downgraded and explained what the Board was required to do in that situation.

The Board alleged that Ambac's statements that it made careful investment choices were misrepresentations because they were made at a time when Ambac was lowering its underwriting standards. The appeals court agreed with the district court that Ambac's statements were merely "puffing statements" designed to make Ambac look appealing.

The Board based its claim of suppression of truth on the fact that Ambac made statements about how selective and cautious it was in investing without disclosing that it had lowered its underwriting standards and without explaining its surveillance policy. Ambac's general statements that it was "selective" or that it was engaging in "active surveillance," however, did not give rise to a duty to

disclose its underwriting standards or surveillance policies

Finally, the Board argued that the court erred when it dismissed its negligence claim, arguing that even if there was no express or implied agreement that Ambac would maintain its AAA rating, Ambac had a duty not to negligently lose its AAA rating. Here, the Board argued that Ambac's negligence caused it to lose its AAA rating. As Alabama law does not impose a duty on Ambac to retain that rating, the only possible source for that duty would be in the contract between the Board and Ambac, making the Board's claim one sounding in contract law.