BRACEWELL
&GIULIANI

New York
Connecticut
Texas
Washington, DC
Kazakhstan
London
Dubai

Evan D. Flaschen
Partner

860.256.8537 Office
860.760.6310 Fax
860.518.6799 Mobile

evan.flaschen@bgllp.com

Bracewell & Giuliani LLP
Goodwin Square
225 Asylum Street, Suite 2600
Hartford, CT 06103

MEMORANDUM

TO:	The Federal Deposit Insurance Corporation, as Receiver of Washington Mutual Bank
FROM:	Bracewell & Giuliani LLP
DATE:	November 25, 2008
RE:	Anticipated Tax Refund

I. Background

Washington Mutual Bank ("WMB"), a federal savings and loan association and direct, wholly-owned subsidiary of Washington Mutual, Inc. ("WMI"), was placed into receivership ("Receivership") by the Office of Thrift Supervision (the "OTS") on September 25, 2008. On the same date, after the Receivership was effective, the Federal Deposit Insurance Corporation, in its capacity as statutory receiver for WMB (the "FDIC" or "Receiver"), entered into a Purchase and Assumption Agreement (the "Purchase Agreement") with JPMorgan Chase Bank, National Association ("JPM"), whereby JPM acquired substantially all of the assets of WMB, including the stock of its subsidiary, Washington Mutual Bank fsb ("WMBfsb"), in exchange for $1.9 billion and the assumption of certain liabilities of WMB. Under the terms of the Purchase Agreement, JPM did not assume the approximately $6.1 billion of senior notes or $7.6 billion of subordinated notes issued by WMB.

The purpose of this memorandum is to explain why the anticipated tax refund resulting from the carryback of WMB's 2008 losses to 2006 and 2007 income taxes paid was not sold to JPMorgan Chase pursuant to the Purchase Agreement.[1] The short answer is that the Purchase Agreement excludes claims that WMB has against WMI, and the anticipated tax refund is, from WMB's perspective, a claim by WMB against WMI under their tax sharing agreement.

II. The Purchase Agreement

The Purchase Agreement states that JPM shall acquire all of the assets of WMB from the Receiver, subject to certain exclusions. Specifically, the Purchase Agreement, in Section 3.1, provides:

> [T]he Receiver hereby sells, assigns, transfers, conveys, and delivers to [JPM], all right, title and interest of the Receiver in and to all of the assets (real, personal and mixed, wherever located and however acquired) including all subsidiaries, joint ventures, partnerships, and any and all other business combinations or arrangements, whether active, inactive, dissolved or terminated, of [WMB] whether or not reflected on the books of [WMB] as of [the close of business on the date the OTS closed WMB (the "WMB Closing")].

The Purchase Agreement further provides, in Section 3.5, that:

> JPM does not purchase, acquire or assume, or (except as otherwise expressly provided in this Agreement) obtain an option to purchase, acquire or assume under this Agreement the assets or Assets listed on the attached Schedule 3.5.

[1] This memorandum focuses on federal income tax law but there may also be relevant anticipated state tax refunds, recognizing that many states (unlike federal) do not permit the carryback of losses.

Schedule 3.5 to the Purchase Agreement specifically provides that assets so excluded from the sale to JPM include:

> [A]ny interest, right, action, claim, or judgment against...any shareholder or holding company of [WMB]...<u>provided</u>, <u>that</u> for the purposes hereof, the acts, omissions, or other events giving rise to such claim shall have occurred on or before [the WMB Closing], regardless of when any such claim is discovered....

The Purchase Agreement does not specifically identify any tax-related items of WMB as being included in or excluded from the assets sold to JPM.

For the years ended December 31, 2006 and 2007, WMB reported, in the aggregate, profits of approximately $4 billion and over $2 billion in income tax expense.[2] In 2008, however, WMB incurred losses in excess of $3 billion in the first six-months of 2008.[3] Although there is no publicly-available information regarding U.S. federal taxable income of, or taxes paid by or on behalf of, WMB for these years, it is reasonable to conclude that WMB had significant taxable income in 2006 and 2007 and incurred substantial tax losses in 2008 prior to the Receivership (the "WMB Pre-Closing Losses"). It is also believed that WMB incurred losses as a result of the Receiver's sale of WMB's assets to JPM (the "Sale Losses")

[2] Washington Mutual Inc., Annual Report (Form 10-K) (Year Ended Dec. 31, 2006); Washington Mutual Inc., Annual Report (Form 10-K) (Year Ended Dec. 31, 2007).

[3] Washington Mutual Inc., Quarterly Report (Form 10-Q) (Period Ended June 30, 2008).

and has and will continue to generate tax losses from the disposition of its retained assets until the Receivership terminates (the "WMB Post-Sale Losses").

For U.S. federal income tax purposes, WMI and WMB are members of a consolidated group that files a single U.S. federal income tax return (the "WMI Group"). WMI has been the common parent of such group for at least the past three years, and WMB was a wholly-owned direct subsidiary of WMI during such time. WMI files tax returns, and pays the taxes owing, on behalf of the WMI Group.

WMI and WMB are parties to a Tax Sharing Agreement dated August 31, 1999 by and between WMI and its subsidiaries (the "Tax Sharing Agreement"). The Tax Sharing Agreement generally provides that each subsidiary that is a party to the agreement shall pay to WMI its share of the taxes, and WMI will pay to each such subsidiary its share of the refunds, of the WMI Group. A subsidiary's share of the group's tax liability or tax refunds is determined as the tax liability it would have incurred or the refund it would have earned had such subsidiary filed tax returns separately and not as a member of the consolidated group. Specifically, the Tax Sharing Agreement provides, in relevant part, that:

> WMI shall pay to [its subsidiaries] amounts that may be due them on account of (i) any overpayment of their said tax liability for a taxable year or (ii) any credit that may result from the utilization of their net operating loss for a taxable year, such credit being determined in accordance with the provisions of item 1 above,[4] within 30

[4] Item 1 of the Tax Sharing Agreement provides, in relevant part, that "[f]or all taxable years during which [any of its subsidiaries] is a member of an 'affiliated group' of WMI as defined in Section 1504 of the Internal Revenue Code and is required to join in the

> days after the consolidated return is filed for that taxable year or, to the extent any such amount due must be recovered from the IRS, within 30 days after payment is received from the IRS.[[5]]

III. Summary of U.S. Federal Income Tax Law With Respect to Net Operating Losses

The Internal Revenue Code of 1986, as amended (the "Code") allows a deduction for certain net operating loss ("NOL") carrybacks and carryforwards by corporate taxpayers.[6] An NOL, generally the excess of allowable deductions over gross income of a corporation,[7] is computed for each taxable year of a corporate taxpayer.[8] An NOL may be carried back two taxable years and forward twenty taxable years to offset taxable income of the corporation in such years.[9] Absent an affirmative election, an NOL must first be carried back to the second prior year, then the first prior year to obtain refunds for taxes paid in those years, with any remaining NOL carried forward to the next following taxable year or years to

---

filing of a consolidated federal income tax return of WMI and its consolidated subsidiaries, the federal income tax liability of such consolidated group shall be allocated and shared among [the subsidiaries] as if such entities filed a separate or consolidated return, as the case may be."

[5] Tax Sharing Agreement, at Section 2(b).

[6] Code Section 172.

[7] Code Section 172(c).

[8] Treasury Regulation Section 1.172-2(a).

[9] Code Section 172(b)(1).

offset taxable income.[10] A corporation's "taxable year" generally is the calendar year or fiscal year ending during such calendar year, for which the taxpayer computes taxable income and files a tax return. Such period generally is the twelve month period properly adopted by the corporation for tax reporting purposes, but can be less than twelve months as corporate reorganizations and liquidations can cause an early termination of a tax year.[11] The taxable year of a subsidiary of a consolidated group does not end solely because it is placed into bankruptcy or receivership or upon a sale of substantially all of its assets, and its tax year continues until the tax year of its consolidated group ends.[12]

The NOL for a corporate consolidated group generally is the excess, if any, of the aggregate allowable deductions over aggregate gross income of all members of a group for the taxable year.[13] The consolidated NOL can be carried back and carried forward by the taxpayer to other consolidated return years under the principles of Code Section 172. If a consolidated group has an NOL in a taxable year, then the common parent corporation, or its designated agent, may file for a tentative carryback adjustment to apply such NOL against

---

[10] Code Section 172(b)(2).

[11] Id.

[12] Treasury Regulation Section 1.1502-75 and Rev. Rul. 63-104, 1963-1 CB 172. See also IRS PLR 200643001 (July 26, 2006).

[13] Treasury Regulation Section 1.1502-11(a).

prior year consolidated taxable income to obtain a refund.[14] A tentative application for an NOL carryback to adjust the taxes paid by a taxpayer during prior taxable years may be filed with Internal Revenue Service (the "IRS") only on or after the due date for filing such taxpayer's tax return for the year in which the NOL is generated.[15] Any refund due is then paid to the common parent of the consolidated group, or its designated agent.[16]

Notwithstanding the general rule that tax refunds attributable to a consolidated group are applied for by, and payable to, the common parent of such group, when a subsidiary of the consolidated group is an insolvent financial institution for which the FDIC is authorized to act as receiver, the FDIC may also file a carryback claim and receive the refund directly as an agent of the consolidated group.[17] While the FDIC, as receiver for a subsidiary of a consolidated group, may file for the direct receipt of a refund with respect to the consolidated

[14] Treasury Regulation Section 1.1502-78(a).

[15] Code Section 6411. Because claims for refunds often trigger a complete audit of the return(s) for the relevant tax years prior to payment of the refund, a taxpayer may be required to wait a substantial amount of time to obtain a refund. To expedite the process, Code Section 6411 enables a taxpayer to apply for a tentative carryback adjustment where the cash payment may be made prior to a full audit. The amount received by the taxpayer, however, is only a tentative allowance of any overpayment. Any overpayment made by the IRS pursuant to a tentative carryback adjustment can later be pursued by the IRS through a deficiency claim, whereas an overpayment of a refund can only obtained if the IRS commence an action to recover the refund from the taxpayer. For purposes of this letter both tentative carryback adjustments and refund claims will be referred to as refund claims.

[16] Treasury Regulation Section 1.1502-78(b).

[17] Treasury Regulation Section 301.6402-7.

group, the IRS is not obligated to pay the FDIC all or any portion of such refund and may use its sole discretion to determine the amount, if any, paid to the FDIC with respect to such claim.[18]

If a corporation is acquired through an acquisition of its stock, such corporation retains its NOLs (generally subject to limitation on future utilization).[19] In contrast, if the assets of a corporation are purchased, the purchaser cannot acquire such corporation's NOLs.[20] A corporation can, however, sell its right to receive a tax refund in connection with the asset sale.[21]

Accordingly, the WMB Pre-Closing Losses can be carried back to the two prior tax years of the WMI Group to obtain a refund of prior years' taxes paid by the WMI Group with any remaining amount of such losses being carried forward up to twenty years to offset future taxable income of the WMI Group. Any refund received by WMI and attributable to the WMB Pre-Closing Losses is payable to WMB as determined under the terms of the Tax Sharing Agreement (the "WMB Tax Payment").

---

[18] Treasury Regulation Section 301.6402-7(g).

[19] Code Sections 381, 382.

[20] Mergers, Acquisitions, and Buyouts, Martin D. Ginsburg and Jack S. Levin, Vol. 3 at 1205 (January 2008).

[21] See infra footnote 27.

IV. Treatment of Consolidated Group Tax Refunds under the Bankruptcy Law

A. A Debtor's Accrued Losses Create an Inchoate Right to a Tax Refund which is Property of the Debtor's Bankruptcy Estate.

Although under the tax law a corporate taxpayer cannot obtain a refund in connection with the carryback of NOLs until after the tax year of such losses closes, the U.S. Supreme Court has interpreted the bankruptcy law to include as property in a debtor's bankruptcy estate a debtor's inchoate right to receive a loss carryback refund.[22] In Segal the debtors had incurred net tax losses for the taxable year through the date of the bankruptcy petition, which did not coincide with the end of the debtors' taxable year. The Court acknowledged that the tax law provides for calculation of tax refunds only on a full year's experience after the tax year has closed and, as of the date of bankruptcy, the amount of any tax claim with respect to losses of the debtors for such year could not be ascertained nor could any claim for payment from the IRS be made. Nevertheless, the Court held that the combination of the losses

---

[22] Segal v. Rochelle, 382 U.S. 375, 379-381 (1966). Bankruptcy law is relevant with respect to an FDIC receivership. The FDIC has stated that "[i]n many ways the powers of the FDIC as receiver of a failed institution are similar to those of a bankruptcy trustee." The FDIC's Role as Receiver, in The FDIC Resolution Handbook at 67-68 (Apr. 2, 2003), available at, <http://www.fdic.gov/bank/historical/reshandbook/>. See also Hightstown Rug Co. v. Nat'l Sav. & Trust Co., 186 F.2d 10, 12 (D.C. App. 1947) (stating that because similar considerations apply to the administration of both bankruptcy and receivership estates, "the legal principles applying to them naturally should follow a similar pattern"); In re Mercury Engineering Co., 60 F. Supp. 786, 788 (S.D. Cal. 1945) (noting that the same principles apply to bankruptcy and receivership cases); In re Riggs, 51 F. Supp. 961, 962 (E.D. Pa. 1943) (same); and Beck v. Fort James Corp. (In re Crown Vantage, Inc.), 421 F.3d 963, 971 (9th Cir. 2005) (finding that a receiver stands in the same capacity as a trustee in bankruptcy).

incurred by the debtors as of the date of bankruptcy and the payment of taxes in years to which such losses could be carried back for a refund was sufficient to find that there was an inchoate claim for refund that was transferable property of the bankruptcy estate. Although no refund with respect to such losses could be collected from the IRS until the following year, the "postponed enjoyment does not disqualify an interest as property."[23] The Court found a property interest in the inchoate right to a refund despite acknowledging that post-petition earnings of the debtors in the same tax year could offset the losses previously incurred, eliminating the opportunity for a refund. Further, the Court noted that had the debtors incurred additional losses in the same tax year after the date of bankruptcy, the proration of such refund would be made between the pre and post-petition periods.[24]

The Ninth Circuit has stated its acceptance of the holding in Segal. In In re Wade Cook Financial Corp.,[25] a petition for bankruptcy was filed before the end of the debtor's tax year and the debtor had incurred a tax loss for such tax year as of the date of the petition. After the debtor's tax year ended, a claim for a carryback of such losses was filed to obtain a

[23] Id.

[24] The practice of prorating tax refunds based upon the amount of losses incurred before and after a petition for bankruptcy filed before the end of the debtor's tax year has been followed in numerous cases. See, e.g. Kokoszka v. Belford, 417 U.S. 642 (1974); In re Barowsky, 946 F.2d at 1518 (cites nine cases and notes that "[e]very court that has considered [the] issue has held that the portion of an income tax refund that is based upon the pre-petition portion of a taxable year constitutes property of the bankruptcy estate.") (citations omitted).

[25] 375 B.R. 580 (9th Cir. 2007).

tax refund. The court determined that the claim for the tax refund with respect to losses incurred prior to the petition was a prepetition claim and not a postpetition claim even though the claim may have been contingent, unliquidated or unmatured when the petition was filed. To resolve any doubt about the applicability of Segal, the court noted "[t]hough Segal was decided under the prior Bankruptcy Act, it remains good law under the Bankruptcy Code applicable to the instant case."[26]

An inchoate right to a future tax refund is assignable by a debtor. In Danning v. Mintz,[27] the court held that a taxpayer's right to its tax refund is generally assignable. As long as the assignment of a tax refund is made pursuant to a valid, enforceable, contract between the parties, the assignee obtains all of the assignor's rights to receive the refund.

B. A Subsidiary Debtor's Right to its Share of a Consolidated Group Tax Refund is a Claim against its Parent in Bankruptcy.

The courts have considered the nature of an inchoate right to a refund of a subsidiary in a consolidated group when refunds payable with respect to taxes of a consolidated group generally are payable by the IRS to the common parent of such group. The courts have evaluated the subsidiary debtor's claim for tax refunds received by its parent with and

[26] Id. at 597-598. See also U.S. v. Sims (In re Feiler), 218 F.3d 948, 955 (9th Cir. 2000); Chappel v. Proctor (In re Chapel), 189 B.R. 489, 493 (9th Cir. 1995).

[27] 367 F.2d 304 (9th Cir. 1966). See also In re Lagerstrom, 300 F. Supp. 538 (S.D. Illinois 1969) and Puget Sound Nat. Bank v. State, 123 Wash. 2d 284, 292 (1994) (holding that a sales tax refund is generally assignable, because to hold would be contrary to the general principles of assignment).

without a tax sharing agreement. In the absence of tax sharing agreement between the parties, the courts generally find that if a subsidiary would have been entitled to a refund in connection with a carryback of NOLs had it always filed as a separate company, the refund received by the parent inures to the benefit of the subsidiary that incurred the loss and the parent holds such refund as an agent of such subsidiary. To permit the parent to retain such refund would result in its unjust enrichment.[28]

When a subsidiary and the parent of a consolidated group are parties to a tax sharing agreement that addresses the treatment of tax refunds, absent a clear agreement that the parent holds refunds attributable to losses generated by a subsidiary in trust for, or as an agent of, such subsidiary, the courts find the parties to have a debtor-creditor relationship with respect to refunds.[29] A tax sharing agreement generally will be found to create a trustee

---

[28] Western Dealer Mgmt. Inc. v. England (In re Bob Richards Chrysler-Plymouth Corp.), 473 F.2d 262, 265 (9th Cir. 1973). See also, Jump v. Manchester Life & Cas. Mgmt. Corp., 438 F. Supp. 185, 189 (E.D. Mo. 1977) ("subsidiary has a right to recover an income tax refund channeled through a parent company filing a consolidated return, and... this right is limited to the recovery which the subsidiary would have had if it had filed individual returns throughout"); U.S. v. Revco D.S., Inc. (In re Revco), 111 B.R. 631, 639 (Bankr. N.D. Oh. 1990) (held that subsidiary was entitled to loss-carryback refund based on In re Bob Richards holding, noting that where the parties made no agreement, the parent corporation acted as an agent for the consolidated group); FDIC v. Brandt (In re Florida Park Banks), 110 B.R. 986, 989 (Bankr. M.D. Fla. 1990) (held that FDIC, as receiver of subsidiary bank, was entitled to the tax refund received by debtor parent that was generated through the subsidiaries' operating losses).

[29] Franklin Savings Corp. v. Franklin Savings Ass'n (In re Franklin Savings Corp.), 182 B.R. 859, 862-863 (D. Kan. 1993), aff'd 31 F.3d 1020 (10th Cir. 2004) (holding that a debtor-creditor relationship existed where "[u]nder the terms of the agreement, the taxes were not held in trust for the benefit of the subsidiary to be automatically turned over to it").

or agency relationship between a parent corporation in possession of a tax refund and its subsidiary if it (i) requires the parent to segregate the tax refund from its other funds; or (ii) restricts the parent's use of the cash tax refund.[30] If the tax sharing agreement does not explicitly or implicitly create a trust or agency relationship between the parent and subsidiary, the court will not deem such relationship to exist.

In In re MCorp Financial, Inc.,[31] the court specifically addressed the rights of a bank subsidiary in receivership to collect its share of a tax refund received by its parent, a debtor in bankruptcy, pursuant to the terms of a tax sharing agreement. The bank subsidiary and its parent were parties to a tax sharing agreement that did not characterize the parent as receiving any refunds attributable to the subsidiary's losses as an agent or nominee for the subsidiary. Thus, the obligation of the parent to remit any portion of a tax refund it received to its subsidiary created a debtor-creditor relationship between the parties. Accordingly, the

---

Similarly, in U.S. v. MCorp Financial, Inc. (In re MCorp Financial, Inc.), 170 B.R. 899, 903 (S.D. Tex. 1994), the court held that where the tax allocation agreement did not contain language creating a trustee relationship or provide that the parent held a "mere nominal claim to the refund," the agreement created a debtor-creditor relationship between the parent and subsidiary.

[30] Superintendent of Ins. v. First Central Financial Corp. (In re First Central Financial Corp.), 269 B.R. 481, 496 (Bankr. E.D.N.Y. 2001), aff'd 377 F.3d 209 (2d Cir. 2004).

[31] 170 B.R. 899, 903 (S.D. Tex. 1994).

court held that if the subsidiary bank, or the purchaser of its assets in receivership, wanted to enforce its right to such refund against the parent it must file a claim in bankruptcy.[32]

The agreement for the sale of the bank subsidiary's assets between the FDIC and the purchaser provided that the FDIC retained all claims against the parent corporation. Thus, the court found that the bank's claim against its parent for the tax refund pursuant to the tax sharing agreement was a claim retained by the FDIC. Further, the purchaser of the bank's assets could not claim any portion of the refund received by the parent on the equities of unjust enrichment because such right does not exist between a post-bankruptcy purchaser out of a receivership and a creditor of the estate.

The courts' interpretation of subsidiaries' rights to refunds received by their parent in bankruptcy is consistent with the FDIC's policy statement regarding tax allocations in a holding company structure (the "Interagency Tax Policy").[33] The Interagency Tax Policy provides that a parent company that receives a tax refund obtains such funds as agent for the consolidated group on behalf of the group members.[34] If a refund is not paid by a parent

---

[32] Id.

[33] Interagency Policy Statement On Income Tax Allocation In A Holding Company Structure, 64758 Interagency Policy Stmt., Federal Register/Vol. 63, No. 225 (Nov. 23, 1998).

[34] Citing Treasury Regulation Section 1.1502-77(a) that states, except as otherwise provided, the common parent for a consolidated return year is the sole agent (agent for the group) that is authorized to act in its own name with respect to all matters relating to the tax liability for that consolidated return year, for each member in the group ...[t]he common parent files claims for refund, and any refund is made directly to and in the name of the

company within a reasonable time period, the receivable should be treated as either an extension of credit or a dividend from the subsidiary to the parent. The Interagency Tax Policy also encourages holding companies and subsidiary financial institutions to enter into written, comprehensive tax allocation agreements and recommends parameters for such agreements including allocating each member's liabilities and benefits as if it had always filed on a separate entity basis.[35] The Interagency Tax Policy further provides that an institution incurring a loss for tax purposes should receive a refund from its parent in an amount that is no less than the amount the institution would have been entitled to receive as a separate entity. The Interagency Tax Policy is thus consistent with the bankruptcy law that a tax refund paid to a parent corporation inures to the benefit of the subsidiary that incurred the loss resulting in such refund; however, if a fair and reasonable tax sharing agreement exists among the parties, it should be followed to determine the rights of the parties with respect to tax refunds.

---

common parent and discharges any liability of the Government to any member with respect to such refund.

[35] Interagency Tax Policy, at 64758. Moreover, one of the primary purposes of a written tax sharing agreement in banking organizations is to govern the rights and responsibilities of the consolidated group's members in order to comport with banking laws and regulations regarding transactions between an insured depository institution and its affiliates. In the absence of a written agreement among the parties of a consolidated group, intercompany tax payments may not be properly recorded and are subject to potential abuse. For example, under Section 11(a) of the Home Owners' Loan Act (12 U.S.C. § 1468(a)), transactions between WMI and WMB, as affiliates, are subject to the requirements of the provisions of Sections 23A and 23B of the Federal Reserve Act (12 U.S.C. § 371c and 12 U.S.C. § 371c-1) and the related regulations of the OTS.

V. JPM's Entitlement to the WMB Tax Payment under the Purchase Agreement

A. The Plain Language of the Purchase Agreement.

Under the Purchase Agreement, JPM acquired from the Receiver all right, title and interest of the Receiver in and to all of the assets of WMB as of the WMB Closing. Specifically excluded from that transfer, however, was any interest, right, action, claim, or judgment against any shareholder or holding company of WMB; provided, that, the acts, omissions, or other events giving rise to such claim occurred on or before the WMB Closing. The critical questions then are: what is the nature of WMB's rights to the tax refund attributable to the WMB Pre-Closing Losses and did JPM acquire such rights?

Prior to undertaking the substantive analysis, the procedural rules for applying the Purchase Agreement must be considered. The Purchase Agreement provides that its interpretation will be governed by federal law and, in the absence of controlling federal law, the law of the state in which the main office of WMB is located.[36] WMB is a Washington corporation and its main office is in Seattle, Washington. Under Washington law, whenever possible, the plain language of a contract should be considered first[37] and words should be given their ordinary, usual, and popular meaning unless the agreement, as a whole, clearly demonstrates a contrary intent.[38] Intent should be determined by objective manifestations

[36] Purchase Agreement, at Section 13.4.

[37] Flores v. American Seafood Co., 335 F.3d 904, 910 (9th Cir. 2003).

[38] Id. (internal citations omitted).

rather than the parties' unexpressed subjective intent.[39] Accordingly, to the extent the plain language of the Purchase Agreement provides a clear expression of intent, such expression should be followed without consideration of other potentially conflicting expressions of the parties' intentions not memorialized in the agreement.

B. WMB's Right to a Tax Refund Attributable to the Carryback of WMB Pre-Closing Losses is in the Form of an Accrued Claim Against WMI under the Tax Sharing Agreement.

As discussed in Section IV of this memorandum, NOLs are computed only with respect to completed taxable years and no refunds can be claimed in connection with an NOL carryback until after the taxable year of such losses has ended. WMB's tax year did not end as a result of the WMB Closing. Accordingly, none of WMI, the Receiver or WMB had the absolute right to receive a cash refund directly or indirectly from the IRS with respect to WMB Pre-Closing Losses as of the WMB Closing. Thus, no tax receivable existed with respect to such losses as of the WMB Closing to be conveyed to JPM.

The accrual of losses together with the payment of taxes in the years to which such losses would be carried back, however, results in an inchoate right to a refund which is transferable property of a bankruptcy estate. The WMB Pre-Closing Losses were all incurred prior to the WMB Closing, and WMB paid taxes in the two carryback years (pursuant to the

---

[39] Paradiso v. Drake, 135 Wash. App. 329, 336 (2006) (internal citations omitted).

terms of the Tax Sharing Agreement). Accordingly, the Receiver should include the inchoate right to a tax refund relating to the WMB Pre-Closing Losses as property of the Receivership.

As previously described, a subsidiary in a consolidated group generally is not entitled to receive any refund directly from the IRS with respect to the carryback of its NOLs by the group. Instead, such refund is payable to the parent, and the subsidiary is entitled to seek recovery of its share in equity or, if a tax sharing agreement exists, as a creditor of the parent, unless the agreement otherwise provides. Because WMI and WMB are parties to the Tax Sharing Agreement as of the WMB Closing, such agreement should govern the rights of the parties with respect to any tax refund paid to WMI. The Tax Sharing Agreement does not indicate that refunds with respect to the group paid to WMI are held by WMI as an agent or nominee of its subsidiaries. Therefore, WMB's entitlement to collect any portion of a refund from WMI under the Tax Sharing Agreement constitutes a creditor claim against WMI.

As noted above, under the Treasury Regulations, the FDIC, as Receiver for WMB, has the right to request that the IRS pay WMB's share of any refund with respect to the carryback of WMB Pre-Closing Losses directly to it as Receiver. However, such right did not vest in the FDIC until it became the Receiver of WMB. The Purchase Agreement is clear that the rights and claims conveyed to JPM are determined as of the WMB Closing, which occurred when WMB was closed by the OTS. The FDIC did not become the Receiver until after such time. Thus, as of the WMB Closing, the FDIC had no right to seek a direct refund

of taxes from the IRS, thus it could not convey such right to JPM nor could it have agreed to remit to JPM any proceeds it received as a result of the exercise of such right.

Accordingly, as of the WMB Closing, the inchoate right to a tax refund with respect to the WMB Pre-Closing Losses accrued to WMB and WMB's ability to collect such refund was limited to establishing a claim as a creditor of WMI. Thus, the WMB Tax Payment is properly characterized as a fully accrued claim against WMI as of the WMB Closing which is expressly excluded from the assets conveyed to JPM under the plain language of the Purchase Agreement and the Purchase Agreement must be interpreted to provide that the WMB Tax Payment is retained by the Receiver.

Further, JPM has no right to any refund arising with respect to the Sale Losses or the WMB Post-Sale Losses since they were not accrued as of the WMB Closing. Accordingly, the right to such refunds is also retained by the FDIC for the benefit of the WMB creditors.

VI. The FDIC Can Collect the Tax Refund in One of Two Ways

As noted, the FDIC is entitled to request that the IRS pay the tax refund directly to the FDIC. However, as also noted, it is within the IRS's sole discretion to determine the amount, if any, that it will pay directly to the FDIC.

The creditors of WMB urge the FDIC, in its capacity as Receiver with the statutory obligation generally to maximize the return on the sale or disposition of the receivership

estate's assets,[40] to expediently seek direct payment from the IRS of the refunds attributable to the WMB Pre-Closing Losses, the Sale Loss and the WMB Post-Sale Losses from the IRS. In making such request, we urge the FDIC to emphasize to the IRS the importance of the refund to the Receivership and the highly inequitable results that would occur were the IRS to make the payment to WMI instead and then for WMI to successfully persuade the bankruptcy court that the Receivership should be accorded only an unsecured claim under the Tax Sharing Agreement. As a creditor of WMI, WMB would likely have a far lesser recovery of such refund for the benefit of WMB's creditors than it would have if the FDIC had successfully applied to receive such amounts directly.

Even if the IRS unjustly refuses to honor the FDIC's request, we would urge the FDIC to enforce an alternative payment mechanism that would ensure that the Receivership receives its full share of the refund, rather than merely an unsecured dividend. The FDIC is well aware of WMI's assertion that it had bank "deposits" with WMB and WMBfsb of not less than $4.4 billion. The FDIC is also aware that we have questioned whether the accounts should properly be characterized as WMI deposits. However, if the accounts are so characterized and if the IRS does not honor the FDIC's direct payment request, we urge the FDIC to invoke its duties as Receiver to exercise its legal rights to offset the tax refund

[40] FDIC Resolution Handbook, Introduction at 2, available at <http://www.fdic.gov/bank/historical/reshandbook/index.html>. See generally Golden Pac. Bancorp. v. FDIC, 375 F.3d 196, 201 (2d Cir. 2004); Phelan v. Middle States Oil Corp., 154 F.2d 978, 991 (2d Cir. 1946).

against the accounts, which will ensure payment in full to the Receivership that is rightly entitled to the refunds for the pre-Receivership taxes paid by WMB.

* * * * *

We are grateful for your consideration of these issues and are willing, at your convenience, to meet with you to discuss these matters or provide any other assistance needed in interpreting the rights and obligations of the parties with respect to the tax refunds at issue. Please do not hesitate to contact us with any questions or comments you may have.