SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

In the Matter of the Application of

WELLS FARGO BANK, NATIONAL ASSOCIATION, U.S. BANK NATIONAL ASSOCIATION, THE BANK OF NEW YORK MELLON, THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., WILMINGTON TRUST, NATIONAL ASSOCIATION, HSBC BANK USA, N.A., and DEUTSCHE BANK NATIONAL TRUST COMPANY (as Trustees, Indenture Trustees, Securities Administrators, Paying Agents, and/or Calculation Agents of Certain Residential Mortgage-Backed Securitization Trusts),

Petitioner,

For Judicial Instructions under CPLR Article 77 on the Distribution of a Settlement Payment.

Index No. 657387/2017

IAS Part 60

Hon. Marcy S. Friedman

RESPONSE BRIEF OF TILDEN PARK

Jonathan L. Hochman
Anna Vinogradov
Schindler Cohen & Hochman LLP
100 Wall Street
15th Floor
New York, N.Y. 10005
T: (212) 277 6330
F: (212) 277 6333
jhochman@schlaw.com
avinogradov@schlaw.com

Philip Bentley
Andrew Pollack
Kramer Levin Naftalis & Frankel LLP
1177 Avenue of the Americas
New York, N.Y. 10036
T: (212) 715 9100
F: (212) 715 8000
pbentley@kramerlevin.com
apollack@kramerlevin.com

Attorneys for Tilden Park Investment Master Fund LP, Tilden Park Management I LLC and Tilden Park Capital Management LP, on behalf of themselves and their advisory clients (collectively, "Tilden Park")

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Other Authorities

INTRODUCTION[1]

No party disputes that the Settlement Agreement is *res judicata*, having been approved in the first Article 77 proceeding. The Settlement Agreement therefore must be enforced as written. Its unambiguous terms may not be varied to conform to the current wishes of respondents, whether they be Settlement Agreement signatories proclaiming their supposed (but unwritten) intent, or previously silent respondents now challenging the agreement's commercial reasonableness. All certificateholders – including the sophisticated parties that negotiated and drafted this detailed agreement – are bound by its terms. *See* Tilden Br. 5-7; *see also In re Bank of N.Y. Mellon*, 56 Misc. 3d 210, 217, 221-25, 41 N.Y.S. 3d 356 (Sup. Ct. N.Y. Cty. 2017) (enforcing plain meaning of Countrywide settlement agreement and governing agreements; rejecting AIG's and Institutional Investors' attempts to vary agreements' terms to conform to parties' alleged intent or to avoid purportedly absurd results).

Accordingly, the Court's first task is to construe the Settlement Agreement. And on the key threshold issue – whether to apply the Settlement Agreement's distribution and write-up rules in the face of arguably conflicting rules in some trusts' PSAs – the Settlement Agreement's terms are clear: it adopts a hybrid approach. For a number of issues, it establishes uniform rules that unambiguously apply to all Settlement Trusts, regardless of whether any trust's PSA contains conflicting provisions. For other issues, it takes a trust-by-trust approach, harnessing

[1] Three other respondents have adopted and incorporated by reference arguments made in this brief: DW Partners LP and Ellington Management Group, LLC have adopted Point I, and Strategos Capital Management, LLC has adopted Points I and III.B.

The opening briefs filed by respondents are referred to herein as follows: Dkt. No. 515 ("Tilden Br."), Dkt. No. 516 ("DE Shaw Joinder"), Dkt. No. 517 ("Strategos Joinder"), Dkt. No. 528 ("Ambac Br."), Dkt. No. 545 ("Olifant Br."), Dkt. No. 563 ("HBK/P&P Br."), Dkt. No. 568 ("P&P Br."), Dkt. No. 573 ("HBK Br."), Dkt. No. 576 ("II/AIG Br."), Dkt. No. 599 ("GMO Br."). Dkt. No. 600 ("Nover Br."), and Dkt. No. 609 ("DW/Ellington Br.").

the terms of each trust's Governing Agreement. Each of these Settlement Agreement provisions is unambiguous and must be enforced in accordance with its plain terms. *See* Tilden Br. 3-4, 7-8.

As demonstrated in our opening brief and below, this approach dictates the following substantive outcomes: (1) the Settlement Agreement leaves the order of operations to the Governing Agreements; (2) some trusts' Governing Agreements require Write-Up First, while others require Pay First; (3) the overcollateralization release provisions of the Pay First trusts must be enforced as written; and (4) the Settlement Agreement requires the Trustees to follow its uniform write-up methodology, including writing up senior certificates and zero-balance certificates.

ARGUMENT

I. The Settlement Agreement Must Be Enforced as Written

A number of parties ask the Court to read the substantive rules created by the Settlement Agreement as if they applied to only *some* Settlement Trusts (those whose PSAs do not conflict), even though on their face these rules apply to *all* trusts, regardless of any potentially conflicting PSA provisions.

These parties argue, with little explanation, that these uniform rules are overridden by Section 7.05, which provides that the Settlement Agreement "reflects a compromise of disputed claims and is not intended to, and shall not be argued or deemed to constitute, an amendment of any term of any Governing Agreement." But no party grapples with the obvious difficulties presented by this interpretation:

- No-one explains why, had the parties meant Section 7.05 to nullify the Settlement Agreement's substantive rules to the extent they conflict with any PSA provisions, they didn't just say so – *e.g.*, by stating that, notwithstanding the Settlement

Agreement's multiple specific rules for treatment of the Settlement Payment, those rules shall have no force and effect to the extent they conflict with any PSA.[2]

- Nor does any party explain why the Court should not adopt the most harmonious reading of Section 7.05: that it was intended to protect, rather than eviscerate, the Settlement Agreement's substantive rules by confirming that the Settlement Agreement is not an impermissible "amendment" to the PSAs. Instead, it serves as a one-time protocol, specifying the treatment of a recovery that the PSAs did not anticipate or address: a mass settlement (or "compromise of disputed claims," to quote Section 7.05) covering unliquidated, as well as liquidated, loans. *See* Tilden Br. 8-9.[3]

- Finally, no party explains how their expansive reading of this section comports with established contract-interpretation canons, which provide that (i) contract provisions should be harmonized whenever possible, and (ii) "in general, '[a] specific provision will not be set aside in favor of a catch-all clause.'" *See id*. 9-10 (quoting *Ambac Assurance Corp. v. Countrywide Home Loans, Inc*., 2018 WL 3129387, at *6 (N.Y. June 27, 2018)).

The GMO Funds ("GMO") contend that an expansive reading of Section 7.05 could comport with a portion of Section 3.06(b) if the latter provision were read to apply only when a PSA is silent as to write-up method. GMO Br. 3-4. But even if that were true, it is beside the point. This expansive reading of Section 7.05 cannot be applied selectively – and as GMO

[2] The Settlement Agreement's drafters knew perfectly well how to provide that one thing should prevail over another in the case of inconsistency. *See, e.g.,* Settlement Agmt. §6.01 ("In the event of any inconsistency, the implementation date in the Subservicing Protocol shall control.").

[3] The PSAs' failure to address this type of recovery is precisely why the Settlement Agreement directs that each trust's Allocable Share be treated "*as though* such Allocable Share was a 'subsequent recovery' . . ." Settlement Agmt. §3.06(a) (emphasis added). Had the PSAs' definition of "subsequent recovery" covered a mass settlement payment of this sort, this provision would not have been needed. It was needed because the PSAs' definition of "Subsequent Recovery" covers only amounts "specifically related to a Liquidated Mortgage Loan" – a definition too narrow to cover a mass settlement payment on account of a pool of unliquidated, as well as liquidated, loans. *See* DW/Ellington Br. at 3-4. Indeed, Justice Scarpulla so ruled in the second Countrywide Article 77 proceeding, stating that "the Allocable Share does not fit within the definition of 'Subsequent Recovery,' as it is not a recovery on a liquidated mortgage loan . . . ." *Bank of N.Y. Mellon*, 56 Misc. 3d at 217 n.5.

Although the PSAs did not anticipate or address the JPM mass settlement, they did give the Trustees the power to settle the trusts' claims against JPM, as this Court ruled in the initial Article 77 proceeding. *See In re U.S. Bank Nat'l Ass'n, No*. 652382/2014, 2016 WL 9110399, at *9 (Sup. Ct. N.Y. Cty. Aug. 12, 2016). That power included the right to negotiate the settlement's terms, including mechanisms for the distribution and write-up of the Settlement Payment. *Cf. Mitchell v. New York Hospital*, 61 N.Y.2d 208, 214 (1984) ("[U]nless public policy is affronted, parties to a civil dispute . . . 'may fashion the basis upon which a particular controversy will be resolved,' [including] 'stipulat[ing] away statutory, and even constitutional, rights.'") (*quoting Cullen v. Naples*, 31 N.Y.2d 818, 820 (Ct. App. 1972)).

acknowledges, *other* Settlement Agreement provisions *cannot* be harmonized with its reading of Section 7.05: "Other sections of the Settlement Agreement provide clear indication that they intend to supersede conflicting provisions of Governing Agreements . . . ." *Id*. at 4 n.7. For example, the Settlement Agreement unambiguously states that REMIC residual interests shall in no event receive either a distribution or a write-up on account of the Settlement Payment. *See* Settlement Agreement §§ 3.06(a), (b); *see also* Tilden Br. 4 (quoting Settlement Agreement §§ 3.03, 3.07). These provisions can only be read one way: to establish uniform rules that override any conflicting PSA provisions. Each of these specific and important Settlement Agreement provisions would be nullified – an impermissible result – by GMO's interpretation of Section 7.05 as prohibiting any variance from the PSAs.

Nover appears to contend that another Settlement Agreement provision, Section 7.13, supports an expansive reading of Section 7.05. In fact, the opposite is true. Section 7.13 provides in pertinent part: "Subject to Section 7.05, all prior agreements and understandings between the Parties concerning the subject matter hereof are superseded by the terms of this Settlement Agreement." Settlement Agmt. §7.13. The most logical reading of Section 7.13 is that it provides that ***the PSAs are superseded to the extent they address the treatment of the Settlement Payment.*** The PSAs are "prior agreements" between parties to the Settlement Agreement – namely, the Trustees and JPM.[4] The PSAs are therefore "superseded by the terms of this Settlement Agreement" to the extent they "concern[ ] the subject matter hereof" – that is, the treatment of the Settlement Payment. Section 7.13's prefatory phrase ("Subject to Section 7.05") confirms this reading: As Section 7.05 states, the Settlement Agreement does not "amend" the PSAs; rather, it addresses the treatment of the one-time global payment arising out

[4] *See* Settlement Agmt. at 1 ("JPMorgan entities were the Seller, Sponsor, Depositor, and/or Servicer" for the Settlement Trusts). As such, they were parties to the PSAs.

of this "compromise of disputed claims," while leaving the PSAs unchanged for purposes of the trusts' ordinary-course operations.

Thus, Section 7.05 clearly distinguishes the Settlement from an amendment,[5] and Section 7.13 confirms that the Settlement Agreement supersedes, rather than yields to, conflicting PSA provisions with respect to the one-time Settlement Payment.

II. The Governing Agreements Control the Order of Operations

A. The Settlement Agreement Requires a Trust-by-Trust Approach

Two respondents (Nover and Ambac) contend that the Settlement Agreement dictates use of the Write-Up First Method by all Settlement Trusts, while others (the Institutional Investors, AIG and GMO) contend that the Settlement Agreement requires all trusts to use the Pay First Method. Both contentions are wrong.

Both arguments rest on a flawed reading of the opening phrase of Section 3.06(b), which requires each Trustee to write up bonds "[a]fter the distribution of the Allocable Share *to a Settlement Trust* pursuant to Subsection 3.06(a)." (emphasis added). Nover and Ambac ask the Court to infer from this that the write-up must occur *before* the trust's subsequent distribution of these monies to investors, while the Institutional Investors, AIG and GMO ask the Court to infer that it must occur *after* that distribution. But nothing in the quoted language supports either inference; it is simply silent as to whether the write-up should occur before or after a trust distributes its Allocable Share to investors.

The advocates of a Pay First approach also point to the last sentence of Section 3.06(b), which states:

---

[5] Judge Glenn relied on the same distinction – between a settlement and an amendment – in *ResCap*, when he approved a global RMBS settlement over the objection of investors that the settlement improperly amended the trusts' PSAs. *See In re Residential Capital LLC*, 497 B.R. 720, 731, 748 (Bankr. S.D.N.Y. 2013) (agreement was a settlement, not an amendment of the governing agreements).

> For the avoidance of doubt, this Subsection 3.06(b) is intended only to increase the balances of the related classes of securities, as provided for herein, and shall not affect the distribution of the Settlement Payment provided for in Subsection 3.06(a).

But it is a stretch at best to read this sentence to require the Trustees to make all distributions on a Pay First basis, regardless of conflicting PSA provisions. Had the agreement's drafters intended such a drastic result, they would have said so directly. Moreover, they would not have begun the sentence with the words "For the avoidance of doubt": That phrase would make sense only if this sentence confirmed or reinforced another provision in the agreement requiring the use of Pay First – but there is no other such provision. Consequently, the only plausible reading of this sentence is that it serves a modest function: to clarify, "[f]or the avoidance of doubt," that Subsection 3.06(b)'s write-up waterfall is not meant to displace or modify the PSAs' distribution waterfalls (*i.e.*, distribution of the Settlement Payment is not limited, as write-ups are, to classes that have experienced losses). *See* Tilden Br. 13-14.[6]

Even more clearly, the Pay First advocates' expansive reading of this sentence cannot be harmonized with the one Settlement Agreement provision that directly addresses the order of

---

[6] Indeed, the Pay First advocates' reading of this sentence proves too much. Even if all trusts were to use the Pay First Method, the write-up could still "affect the distribution of the Settlement Payment provided for in Subsection 3.06(a)" to some trusts. As explained in DW/Ellington's Response, Pay First scenarios are possible in which a portion of the Settlement Payment may remain undistributed after the initial distribution, in which case Section 3.06(a) requires these remaining funds to "be maintained in the collection or distribution account for distribution on the next distribution date according to the provisions of this Subsection 3.06(a)." This later distribution of these monies would be affected by the write-up. *See* DW/Ellington Response at Point III.A.4.

Still further confirmation that the last sentence does not mandate Pay First for all trusts is provided by the Lehman RMBS settlement agreement, which the Institutional Investors and the Trustees executed last year. As discussed in Point II.B below, that agreement contains a substantially identical sentence, followed by an explicit statement that, in the event the settlement agreement conflicts with any PSA as to any distribution issue, the PSA controls. The Institutional Investors and the Trustees could not have meant their "for the avoidance of doubt" sentence to mandate Pay First for all Lehman trusts, given the next section's explicit rejection of any such across-the-board approach.

operations: the opening sentence of Section 3.06(a), which mandates a trust-by-trust approach. That sentence provides in pertinent part:

> (a) Each Trust's Allocable Share shall be deposited into the related Trust's collection or distribution account . . ., for further distribution to Investors ***in accordance with the distribution provisions of the Governing Agreements*** . . . as though such Allocable Share was a 'subsequent recovery' . . . . (Emphasis added.)

As explained in our opening brief, this mandate to make a distribution "in accordance with the [Governing Agreements'] distribution provisions" requires adherence to the order of operations embedded in each PSA's definition of Certificate Principal Balance. Specifically, any distribution requires calculation of each class's Certificate Principal Balance, and each PSA's definition of that term specifies whether it includes subsequent recoveries received by the trust in the calendar month ending just before that distribution date (Write-Up First) or does not include such recoveries (Pay First). *See* Tilden Br. 10-11, 14-18.

As discussed in our opening brief and in Point II.C below – and as most parties to this proceeding agree – the PSAs for many trusts clearly fall into the first of these two categories, requiring Write-Up First. *See* Tilden Br. 14-16; *see also* Point II.C below. Just as clearly, the PSAs for other trusts fall into the latter category, requiring Pay First. *See* Tilden Br. 16-18. Section 3.06(a) requires that these PSAs' directives be honored.[7]

[7] Given that the PSAs dictate the order of operations, a reading of the Settlement Agreement to require either a Pay First or a Write-Up First approach for all trusts would conflict with the clear terms of many PSAs. Consequently, if the Court were to follow the view of the Institutional Investors and others that the Settlement Agreement cannot modify the PSAs, a trust-by-trust approach to the order of operations issue (as well as every other issue) would be required *even if the Court adopted the Institutional Investors' argument that Section 3.06 directs all trusts to use the Pay First Method*.

B. The Other Settlement Agreements Cited by the Institutional Investors Provide Further Support for a Trust-By-Trust Rather Than Pay First Reading of the JPM Agreement

The Institutional Investors contend that the Settlement Agreement's distribution provisions are "virtually identical" to those of other global RMBS settlements, which they say mandate Pay First. II/AIG Br. 9-14. This is untrue. The operative language of these agreements differs in crucial respects. Moreover, far from showing the parties' consistent agreement to use the Pay First Method, these agreements show that the parties' practice has evolved: After requiring Pay First in the first global RMBS settlement (Countrywide), the Institutional Investors and Trustees subsequently abandoned that approach in favor of a trust-by-trust approach.

The Countrywide settlement required all trusts to use the Pay First Method. However, the provisions of the Countrywide agreement that made this clear were anything but "virtually identical to those in the JPMorgan settlement." II/AIG Br. 12-13. To the contrary, they contained key language that is conspicuously absent from the JPM Settlement Agreement, requiring Trustees to write up bonds "[a]fter the distribution of the Allocable Share ***to Investors***" – *i.e.*, to pay investors first and write up the bonds second. *See* II/AIG Br. 10 (quoting Countrywide settlement agreement Section 3(d)(ii)) (emphasis added). In the face of this unambiguous language, almost all parties to the second Countrywide Article 77 proceeding correctly agreed that Pay First was required, and the Court eventually so ruled. *See* II/AIG Br. 12-13 & nn. 25, 27.

The first sentence of Section 3.06(b) of the JPM Agreement is strikingly different. It instructs each Trustee to write up bonds "[a]fter the distribution of the Allocable Share ***to a Settlement Trust***" – a phrase that some parties construe to require Write-Up First and others (including the Institutional Investors) construe to support Pay First, since it does not specify whether the write-up should occur before or after the distribution *to investors*. *See* pp. 5-6 above.

Notably, the JPM Settlement Agreement was drafted and executed after the Countrywide settlement agreement. The JPM Agreement's drafters clearly used the Countrywide agreement as a model; much of the JPM Agreement's language is identical, word for word, to that of the prior agreement. Yet the parties to the JPM Agreement chose to delete the two critical words ("to Investors") that, in the Countrywide agreement, made the intent to require Pay First plain. The deletion of these two words can mean only one thing: The parties decided to abandon Countrywide's Pay First mandate, choosing instead to leave the order of operations to be determined on a trust-by-trust basis – that is, to leave this issue "unaddressed" (as the Trustees later stated in the Petition, at paragraph 21).

The most recent global RMBS settlement agreement – Lehman – continues this evolution, making even clearer that the parties' current practice is to leave the order of operations to be determined by each trust's PSA. Oddly, the Institutional Investors cite Lehman as a settlement agreement that supposedly mandates Pay First and has language "virtually identical" to that in the JPM Settlement Agreement. II/AIG Br. 9-13. They fail to mention that the section immediately following the two they quote expressly states that *all* distribution and write-up issues must be handled in a manner consistent with each trust's PSA:

> (c) Should the party responsible for calculating distributions and/or making distributions to Investors under the terms of the Governing Agreements of a given Trust or a court determine that the payment procedure described *in Sections 3.06(a) and 3.06(b)* may not conform to the terms of the Governing Agreement for a particular Accepting Trust, *the distribution described above shall be modified to distribute that Trust's Plan Payments* as a payment of principal under the Governing Agreement for that Trust, or in such other manner as the party responsible for calculating distributions under the terms of the Governing Agreements of a

> given Trust or a court should determine is *in conformance with the terms of the Governing Agreement* for a particular Trust.

Lehman Settlement Agreement § 3.06(c) (Ex. 8 to Sept. 14, 2018 Affidavit of David Sheeren ("Sheeren Aff.") at 17) (emphasis added).

Thus, to the extent there is a historical pattern to the global RMBS settlements' treatment of the order of operations issue, it is not their consistent use of the Pay First Method, but rather the rejection of that approach by the more recent settlements – JPM and Lehman – in favor of a trust-by-trust approach.[8]

The Lehman settlement agreement is probative in a second respect as well. It confirms that the last sentence of Section 3.06(b) of the JPM Agreement – the clarifying sentence that the Institutional Investors say mandates the use of Pay First for all trusts – in fact means nothing of the sort. A substantially identical sentence appears at the end of the Lehman agreement's certificate write-up section. *See* II/AIG Br. 12-13; *see also* Sheeren Aff., Ex. 8. at §3.06(b). At the same time, as just noted, the next section of the Lehman agreement (3.06(c)) expressly requires a trust-by-trust approach. The Institutional Investors and Trustees could not possibly have meant the last sentence of Section 3.06(b) to prohibit the trust-by-trust approach that Section 3.06(c) mandates – nor should their use of the same sentence in the JPM Agreement be given such an expansive meaning.[9]

---

[8] The Institutional Investors assert, without evidence or elaboration, that the Trustees have distributed settlement proceeds to over 1,000 RMBS trusts on a Pay First basis. II/AIG Br. 9. These distributions are not relevant to the Court's construction of the JPM Settlement Agreement. Many, if not most, of these distributions were made pursuant to a consensual Countrywide distribution, which covered 512 trusts. Other distributions presumably were also consensual, based on agreements among parties who did not object to Pay First under the particular economic circumstances of those settlements. In contrast, most respondents in the present Article 77 proceeding have objected to Pay First and asked the Court to use Write-Up First instead.

[9] The Institutional Investors quote two comments made by Bankruptcy Judge Chapman, during the recent hearing on their motion to enjoin the Lehman Article 77 proceeding, indicating her initial receptivity to their argument that the last sentence of Section 3.06(b) requires use of the Pay First Method. II/AIG Br.

C. Each of the Governing Agreements Dictates Either Write-Up First or Pay First

Most parties agree that the order of operations is embedded in each PSA's definition of Certificate Principal Balance, which the Trustees are bound to follow. *See* Nover Br. Point III.A; Olifant Br. Point II.A; P&P Br. 3-4; DW/Ellington Br. Point III; DE Shaw Joinder at 2. Moreover, no-one has seriously contested this conclusion. While the Institutional Investors and AIG state that "[t]he Governing Agreements are silent as to the order of operations," they provide no support for this assertion, and they simply ignore the clear PSA language on this point set forth in the Answers of Tilden Park and others. II/AIG Br. 5.

As for the particular outcomes mandated by the various PSAs, the parties appear to be largely in agreement. Most parties focus on PSAs (the "Write-Up First PSAs") that follow the prevailing order of operations approach, which defines Certificate Principal Balance on any distribution date to *include* subsequent recoveries received by the trust in the most recent calendar month. With the sole exception of HBK, acting through U.S. Bank ("HBK"), these parties correctly conclude that these PSAs require Write-Up First. *See* Nover Br. Point III.A; Olifant Br. Point II.A; P&P Br. 3-4; DW/Ellington Br. Point III; DE Shaw Joinder at 2. No party has taken issue with Tilden Park's showing that *other* PSAs, whose Certificate Principal Balance definitions *exclude* subsequent recoveries received by the distribution date, require Pay First. *See* Tilden Br. 16-18.

HBK alone contends that PSAs that follow the prevailing order of operations approach require Pay First, rather than Write-Up First. In so doing, HBK simply ignores that, in each of

---

13-14. However, Judge Chapman's view of the significance of this sentence changed after counsel for the paying agent focused her on the trust-by-trust language of Section 3.06(c) quoted above. *See* Hearing Tr. (Sheeren Aff., Ex. 13) at 50:2-54:17. Moreover, as Judge Chapman noted at the end of the hearing, the meaning of the Lehman settlement agreement was not before her at that time; she therefore made no rulings construing its terms. *See id*. at 53:2-13; 55:15-21.

these PSAs, the definition of Certificate Principal Balance, for any given distribution date, specifically includes subsequent recoveries received by the trust in the most recent calendar month.[10] In other words, as explained in Tilden Park's Answer and opening brief, the PSA instructs the Trustee to write up the Certificate Principal Balance by the amount of these subsequent recoveries *before* making a distribution (Write-Up First), rather than paying first and writing up after. *See* Tilden Answer [Dkt. No. 129] at 4-8; Tilden Br. 1-11, 14-18.

HBK does not even try to rebut this dispositive showing. Instead, HBK appears to contend that, as a practical matter, it is not possible for a trustee to determine whether a write-up is required until after it has made the distribution. *See* HBK Br. at 5 ("Only after the distribution of such funds are accounted for can the accounting for those funds be addressed in subsection (b) of Section 5.04."); *id.* at 9 ("A trustee cannot determine [whether the amount of a Realized Loss has been reduced by Subsequent Recoveries] except by paying distributions first."). This is nonsense. Trustees routinely employ the Write-Up First Method to account for global settlement payments, and none (to our knowledge) have ever claimed that they are unable to compute the

[10] The PSAs governing the Settlement Trusts in which HBK claims an interest (the "HBK Settlement Trust PSAs") are the same in this regard as the other Write-Up First PSAs. *See, e.g.,* Sept. 14, 2018 Affirmation of Anna Vinogradov, Dkt. No. 518 ("Vinogradov Aff.") Ex. A (BSABS 2005-AQ2, Art. I) (Definition of Certificate Principal Balance ("Certificate Principal Balance: . . . [A]s of any Distribution Date, the Initial Certificate Principal Balance of such Certificate plus . . . **any Subsequent Recoveries added to the Certificate Principal Balance of such Certificate pursuant to Section 5.04(b)**, less the sum of (i) all amounts distributed with respect to such Certificate in reduction of the Certificate Principal Balance thereof on previous Distribution Dates pursuant to Section 5.04, and (ii) any Applied Realized Loss Amounts allocated to such Certificate on previous Distribution Dates.") (emphasis added); *see also id.*, Section 5.04(a)(2)(A)(ii) (each class of certificates shall be paid, in order of priority, "until the Certificate Principal Balance thereof is reduced to zero"); Section 5.04(b) ("If, after taking into account such Subsequent Recoveries, the amount of a Realized Loss is reduced, the amount of such Subsequent Recoveries will be applied to increase the Certificate Principal Balance of the Class of Certificates with the highest payment priority to which Realized Losses have been allocated, but not by more than the amount of Realized Losses previously allocated to that Class of Certificates pursuant to Section 5.05.").

amount of the write-up. Nor does the Petition, in its discussion of order of operations, say that use of Write-Up First would pose any particular accounting difficulties.[11]

To the extent HBK means to argue that Pay First is required because the PSA section addressing distributions (Section 5.04(a)) appears prior to the section addressing write-ups (Section 5.04(b)), this conclusion simply doesn't follow. The PSAs do not indicate that there is any temporal relation between these two sections; they are not sequential steps, but instead address separate and distinct subjects, each appearing in its own subsection of Section 5.04. Moreover, it is clear that at least some of the actions directed by Section 5.04*(b)* occur *prior to* those required by Section 5.04*(a)*: Section 5.04(b) requires the Master Servicer to deposit Subsequent Recoveries into the Protected Account pursuant to Section 4.01(b)(iii), and Section 4.01(b) in turn requires such deposits to be made "on a daily basis within one Business Day of receipt" of all Subsequent Recoveries – *i.e.*, prior to the distributions required by Section 5.04(a). Vinogradov Opp. Aff. Ex. E (BSABS 2005-AQ2 PSA § 4.01(b)).

D. The OC Release Provisions of the Pay First Trusts Must Be Enforced as Written

1. The Plain Language of the Governing Agreements Requires OC Release for Pay First Trusts

As the Trustees note, overcollateralization[12] resulting in the distribution of a portion of the settlement proceeds through the excess cashflow waterfall is compelled by the terms of the

[11] In addition, HBK's contention rests on a misreading of the PSAs. HBK says a trustee cannot determine whether the amount of a Realized Loss has been reduced by Subsequent Recoveries (and thus whether a write-up is warranted) without knowing the specific amounts each certificate will receive, or whether such amounts will be received pursuant to the Excess Cashflow distribution provisions. This is simply not true. To determine that a Realized Loss has been reduced by Subsequent Recoveries, one need know only that those Subsequent Recoveries will be distributed to ***any*** class of certificates on a particular distribution date. The definition of Realized Loss makes this clear. *See* Vinogradov Opp. Aff. Ex. E (BSABS 2005-AQ2 PSA, Art. I) (Definition of Realized Loss) ("[T]o the extent the Master Servicer receives Subsequent Recoveries with respect to any Mortgage Loan, the amount of the Realized Loss with respect to that Mortgage Loan will be reduced to the extent such recoveries are distributed to ***any*** Class of Certificates or applied to increase Excess Spread on any Distribution Date.") (emphasis added).

Pay First OC Trusts' Governing Agreements.[13] *See* Petition ¶ 28 (under the Pay First Method, "any portion of the Settlement Payment (*i.e.*, overcollateralization amount) in excess of the overcollateralization target would constitute overcollateralization release amount and be distributed as excess cashflow."). The Trustees are correct that the terms of the Governing Agreements dictate this result.[14] Those agreements require the overcollateralization amount to be calculated "[w]ith respect to any Distribution Date." *See, e.g.,* September 28, 2018 Affirmation of Anna Vinogradov in Support of Response Brief of Tilden Park ("Vinogradov Opp. Aff.") Ex. A (BSABS 2007-AC2 PSA, Art. I) (Definition of Overcollateralization Amount). The aggregate certificate balance used for the calculation must "tak[e] into account the payment of principal . . . on such Certificates" on that distribution date. *Id.*[15] This means that, within the calculation of the overcollateralization amount for the distribution date that includes the Settlement Payment distribution, the aggregate certificate balance will be ***decreased***

---

[12] As explained in the Petition, OC Trusts are trusts that are structured to have an aggregate mortgage loan balance in excess of the aggregate principal balance of all certificates, thereby providing a cushion to protect Certificateholders from losses. Petition ¶ 25. The amount by which the aggregate mortgage loan balances exceed the aggregate certificate balances is known as the "overcollateralization amount." *Id.* Once the overcollateralization amount surpasses the "overcollateralization target," funds in excess of that target amount are considered the "overcollateralization release amount" and are distributed as excess cashflow – not to pay down the principal balance of the certificates, but instead to compensate certificates for unpaid realized losses. Petition ¶ 26.

[13] The Pay First OC Trusts in which Tilden Park holds certificates are listed in Exhibit 4 to Tilden Park's answer. Tilden Park's arguments concerning overcollateralization apply only to those and similar trusts.

[14] Trustees in Article 77 proceedings concerning other RMBS settlements have also interpreted the relevant governing agreements as requiring an overcollateralization release in connection with the settlement payment. *See* Vinogradov Opp. Aff. Ex. B (Countrywide Petition) ¶ 25 ("[I]f the Trustee applies the distribution and write up provisions of the Governing Agreements in the OC Trusts as it has done historically (paying the Allocable Share to Certificateholder *before* writing up Certificate Principal Balances), in most of the OC Trusts substantial amounts of each Allocable Share will flow to less senior, subordinated Certificateholders even though overcollateralization in the OC Trust is far short of the OC Target."); Vinogradov Opp. Aff. Ex. C (Lehman Petition) ¶ 41 ("[A]ny portion of the Settlement Payment (*i.e.*, overcollateralization amount) in excess of the overcollateralization target would constitute overcollateralization release amount and be distributed as excess cashflow.").

[15] The Governing Agreement for each of the Trusts listed in Exhibit 4 to Tilden Park's answer contains provisions that are either identical or substantially similar to those quoted in the text above.

by the amount of the Settlement Payment.[16] Consequently, the overcollateralization amount – the difference between the aggregate (unchanged) mortgage loan balances and the aggregate (lowered) certificate balances – will be raised and may exceed the overcollateralization target amount for a number of Pay First OC Trusts. Petition ¶ 28. The resulting overcollateralization release amount should then be distributed through the excess cashflow waterfall, typically flowing first to Class A certificates to reimburse them for any interest shortfalls and then for unpaid realized loss amounts. Petition ¶ 30.

No legal basis exists to deviate from the PSAs' unambiguous terms, which are dispositive and must be followed. *See Schron v. Troutman Sanders LLP*, 986 N.E.2d 430, 433 (N.Y. 2013). As noted above, the definition of overcollateralization amount in the Pay First OC Trusts' Governing Agreements states that the aggregate certificate balance used to calculate the overcollateralization amount must "tak[e] into account the ***payment*** of principal . . . on such Certificates" on that distribution date. *See, e.g.*, Vinogradov Opp. Aff. Ex. A (BSABS 2007-AC2 PSA, Art. I) (Definition of Overcollateralization Amount) (emphasis added). The plain meaning of this language is that the aggregate certificate balance must be decreased to account for the forthcoming payment on a particular distribution date, and the overcollateralization amount should be calculated using the lowered balance.

2. The Institutional Investors' Reading of the Definition of Overcollateralization Amount Is at War With Its Text

The Institutional Investors argue that aggregate certificate balances must also be written ***up*** when the overcollateralization amount is calculated, cancelling out the decrease of balances on account of the payment. But this additional step contradicts the plain text of the

[16] Generally, as the Trustees note, "[t]he applicable Governing Agreements provide that in determining the amount of the aggregate certificate principal balances for this calculation, it should be assumed that all principal funds are being applied as principal amount to reduce such balances." Petition ¶ 28.

overcollateralization amount definition. The definition requires the Trustees to subtract from the aggregate mortgage loan balance "the aggregate Certificate Principal Balance of the Certificates (other than the Class C Certificates and the Class P Certificates) on such Distribution Date (***after taking into account the payment of principal*** other than any Extra Principal Distribution Amount on such Certificates)." *See, e.g.*, Vinogradov Opp. Aff. Ex. A (BSABS 2007-AC2 PSA, Art. I) (Definition of Overcollateralization Amount) (emphasis added); *see also* II/AIG Br. 17. The overcollateralization amount definition does not state that the aggregate certificate balance should take into account any write-up that is to occur in the future, after the distribution; it refers only to "the *payment*." *Id.* (emphasis added.)

The Institutional Investors, without any justification, ask the Court to read the term "payment" to mean *both* the payment and the write-up. II/AIG Br. 17-18 ("[I]n calculating the Overcollateralization Amount, the trustees must 'tak[e] into account' the settlement payment itself. There are two steps the trustees must take into account. The ***first*** step the Trustees must take into account is . . . the distribution . . . . The ***second*** step the Trustees must take into account, however, is the equal and offsetting write-<u>up</u> of certificate balances associated with the receipt of subsequent recoveries."). This reading simply has no basis in the text. In the Countrywide Article 77 proceeding, Justice Scarpulla rejected the Institutional Investors' similar invitation to insert the additional step of a write-up into the definition of "Principal Distribution Amount," a term relating to overcollateralization in the relevant Countrywide PSAs.[17] *In re Bank of N.Y. Mellon*, 56 Misc. 3d at 222 ("The Standard Intex method . . . adds an extra step—the addition of the Allocable Share—that is not reflected anywhere in the definition of the Principal Distribution Amount. While AIG and the Institutional Investors assert that the text of

[17] While the term "Principal Distribution Amount" is not at issue in this case, the text of the overcollateralization amount definition is equally plain.

the Governing Agreements support distribution according to the Standard Intex method, there is no textual basis in the Governing Agreements for adding the Allocable Share to the calculation of the Principal Distribution Amount."). Instead, Justice Scarpulla held that the trustees were required to follow the plain text of the PSAs and distribute a portion of the settlement payment to junior certificates with realized losses. *Id.* at 221-25. Here, as in *Countrywide*, the Governing Agreements require an overcollateralization release for certain trusts, and nothing in the Settlement Agreement suggests or permits a different outcome.

3. The Institutional Investors' Claims of Absurdity and Commercial Unreasonableness Cannot Overcome the Plain Language of the Governing Agreements

Apparently recognizing that their textual argument is untenable, the Institutional Investors ask the Court to rewrite the Governing Agreements on the ground that the requisite overcollateralization release that will result from the Settlement Payment is an absurd and commercially unreasonable result. II/AIG Br. 18-19. But courts will not look beyond the language of the contract where, as here, it is clear. *In re Bank of N.Y. Mellon*, 56 Misc. 3d at 224 ("I may not look beyond the four corners of the relevant agreement to determine the parties' intent, when the contract language itself is clear."); *id.* at 225 ("Where the 'parties set down their agreement in a clear, complete document, their writing should as a rule be enforced according to its terms. Evidence outside the four corners of the document as to what was really intended but unstated or misstated is generally inadmissible to add to or vary the writing.") (quoting *W.W.W. Assocs., Inc. v. Giancontieri*, 77 N.Y.2d 157, 162, 565 N.Y.S.2d 440 (1990)).

Further, overcollateralization resulting in the distribution of a portion of the Settlement Payment through the excess cashflow waterfall is neither absurd nor commercially unreasonable. In fact, Justice Scarpulla rejected the same argument in the second Countrywide Article 77 proceeding, holding that "***it is neither an absurd or unenforceable result that*** . . . ***the*** majority

of the Allocable Share [will] be distributed to certificates with realized losses, particularly because the parties anticipated that this result might occur." *In re Bank of N.Y. Mellon*, 56 Misc. 3d at 223-24 (emphasis added). She noted that "[e]ven if this distribution can be characterized as unusual, terms that are 'novel or unconventional' do not render a result absurd." *Id.* at 224.

Nor do the PSAs' subordination features or the poor performance of the trusts render the overcollateralization absurd. While the subordination features generally protect senior certificates, as in Countrywide, "the parties plainly understood when they negotiated the Settlement Agreement that there could be instances where the Governing Agreements' general subordination scheme may not apply." *Id.* at 222. And distributing a portion of the Settlement Payment to certificates that have suffered applied realized losses makes sense in light of the trusts' poor performance and the purpose of the Settlement Agreement – to reimburse the trusts for the losses they have experienced. The Institutional Investors cannot avoid a result they find economically undesirable by labeling it absurd.

4. *Countrywide* Strongly Supports Overcollateralization Release for Pay First Trusts

The Institutional Investors' reliance on the *settlement* of some of the Countrywide trusts – rather than the *court's holding* as to the Countrywide trusts in which the overcollateralization release issue was fully adjudicated – is completely misplaced. The avoidance of overcollateralization with respect to 512 trusts in the second Countrywide Article 77 proceeding (the "Non-Litigated Trusts") is a red herring because, as the Institutional Investors concede, those trusts settled and the trustee there was directed to avoid overcollateralization in the Non-Litigated Trusts "***by agreement among the parties***." II/AIG Br. 20 (emphasis added). The settlement of the Non-Litigated Trusts obviously carries no precedential value. *See Expressview Dev., Inc. v. Town of Gates Zoning Bd. of Appeals*, 147 A.D.3d 1427, 1429, 46 N.Y.S.3d 725, 728 (4th Dep't 2017); *see also High Country Home Health, Inc. v. Thompson*, 359 F.3d 1307, 1314–15 (10th Cir. 2004) ("[S]ettlement agreements have no precedential weight . . . ."); *Illinois-Masonic Med. Ctr. v. Sebelius*, 859 F. Supp. 2d 137, 148 n.11 (D.D.C. 2012) ("Parties settle cases for all sorts of reasons. . . . [T]he settlement does not create a binding precedent.").

Further, like the orders in this case severing certain trusts and directing the Trustees to distribute their Allocable Shares pursuant to the parties' agreement, the Partial Severance Order and Partial Final Judgment ("Countrywide Severance Order") concerning the Non-Litigated Trusts was expressly not intended to establish a precedent for distributions in other trusts. By its terms, the Countrywide Severance Order provided that it was not even precedential *in that case*. Rather, it was "rendered without prejudice to the claims, contentions or defenses of any party in respect of the Remaining Trusts." Sheeren Aff. Ex. 9, at 6. It further provided that it "will in no way represent the law of the case as to, or otherwise be deemed to resolve any issue pertaining to, the Remaining Trusts." *Id.* Parties to the second Countrywide Article 77, including Tilden Park, reached a settlement as to the Non-Litigated Trusts that, by its nature, has no bearing on whether an overcollateralization release was required by the PSAs of those trusts. Accordingly, this order provides no support for avoiding overcollateralization in the Settlement Trusts.

By contrast, the overcollateralization release issue *was* litigated with regard to fourteen trusts in the second Countrywide Article 77 proceeding (the "Litigated Trusts"). With regard to those trusts, Justice Scarpulla held that the trustee was required to follow the plain language of the governing agreements by distributing a portion of the allocable share via a lower waterfall section to junior certificates with realized losses, *i.e.* permitting an overcollateralization release. *In re Bank of N.Y. Mellon*, 56 Misc. 3d at 225. While the specific language in the Litigated Trusts' governing agreements differed from the language at issue here, Justice Scarpulla's adherence to the plain text of the documents and her holding regarding the commercial reasonableness of an overcollateralization release are fully applicable here. *See id.* at 223-25.

III. The Settlement Agreement Imposes a Uniform Write-Up Methodology

As Tilden Park established in its opening brief, the Settlement Agreement write-up instruction requires the Trustees to write up all certificates that have sustained losses, including senior certificates and zero-balance certificates. *See* Tilden Br. 19-20. The Settlement Agreement supersedes any conflicting provisions of the Governing Agreements, and any objections to the Settlement Agreement's terms – including on the ground that they conflict with the Governing Agreements – are barred by *res judicata*. *See id.* 5-10.

A. Senior Bonds With Losses Should Be Written Up

Nover alone urges the Court to ignore the Settlement Agreement and limit the write-up to subordinate classes, relying on the phrase "Subordinate Certificates" in some PSA write-up instructions. Nover claims that the Settlement Agreement "*does not* define precisely which certificate classes are eligible to be written-up." Nover Br. 9-10 (emphasis in original). This is plainly wrong. Section 3.06(b) of the Settlement Agreement does define the classes that are eligible to receive the write-up: "***each class*** of securities (other than any class of REMIC residual interests) ***to which such losses have been previously allocated***." Settlement Agmt. §3.06(b) (emphasis added).[18] The phrase "***each*** class" could not more clearly apply to ***all*** bonds. "Each" means "all considered one by one." *Webster's Third International Dictionary* 713 (4th ed. 1976); *In re Turner's Will*, 208 N.Y. 261, 265 (1913) ("'Each' means 'every one of any number separately considered.'") (quotation omitted). Because Section 3.06(b) applies to ***all*** bonds other

[18] Nover's quotation of this provision misleadingly omits, without ellipsis, the phrase "to which such losses have been previously allocated" – the key words that delineate which classes receive write-ups. *See* Nover Br. 10.

than REMIC residual interests, the Trustees should write up senior bonds that have suffered losses.

The drafters of the Settlement Agreement could have easily provided that only classes permitted to be written up under the Governing Agreements would receive write-ups. However, they chose not to do so, because their purpose in drafting the write-up instruction was to compensate investors (including senior investors) that had suffered losses, a point confirmed by witnesses at the prior Article 77 proceeding. *See* Vinogradov Opp. Aff. Ex. D, at 368:7-9. Accordingly, the Court should reject Nover's argument and direct the Trustees to implement the Settlement Agreement's instruction by writing up all classes that have incurred losses.[19]

In any event, there is no conflict between the write-up instructions in the Settlement Agreement and those in certain Governing Agreements that purport to limit write-ups to "subordinate" bonds. As Tilden Park's opening brief explained, these Governing Agreement write-up instructions apply only to Subsequent Recoveries ***that are received by the Master Servicer and reduce the Realized Loss for a specific loan***. *See* Tilden Br. 20-21. Because the Settlement Payment fails to satisfy these two conditions, it does not trigger the Governing Agreements' write-up instructions, so they simply do not apply. *Id.*

Nover ignores the limited scope of the Governing Agreements' write-up instructions. Instead, it points to differing write-up instructions between groups or classes in the same trust, which it says show that the use of the term "subordinate" in some PSA write-up provisions was intentional. *See* Nover Br. 7-8. But the intentional nature of those provisions is irrelevant,

[19] Nover also argues (at 7) that the PSA write-up methodology must be followed because investors relied on it when purchasing certificates. But investors had ample opportunity to object to the Settlement Agreement's write-up instruction on that ground in the prior Article 77 proceeding. Any such objection is now barred by *res judicata*. *See In re Bank of N.Y. Mellon*, 56 Misc. 3d at 217.

because as just noted, those PSA write-up provisions are not triggered by the Settlement Payment.

B. Certificates With Zero Balances Should be Written Up

HBK, Poetic and Prophet argue that "retired class provisions" in certain PSAs forbid writing up bonds with zero balances. HBK/P&P Br. 5-12; *see also* II/AIG Br. 25 (taking same position, but with little argument or elaboration). This argument ignores the Settlement Agreement's plain text. Unlike Section 3.06(a), which delegates the order of operations to the PSAs, Section 3.06(b) specifies a method of writing up bonds: the Trustees must apply Settlement funds "***in the reverse order of previously allocated losses***, to increase the balance of ***each class*** of securities" other than REMIC residual interests. Settlement Agmt. §3.06(b) (emphasis added). As noted above (at p. 20), "each" means "all considered one by one," thus mandating the write-up of ***all*** classes except residual interests, to the extent they have been allocated losses. Had the Settlement Agreement's drafters meant to preclude the writing up of zero balance bonds, they would have excluded such classes from this directive, as they did for residual interests.

In any event, contrary to HBK and P&P's assertions, the PSAs' "retired class provisions" do not bar ***writing up*** "retired" bonds. To the contrary, the PSAs make clear that "retired" bonds remain "outstanding," and any outstanding bond can be written up. *See* Tilden Br. 23-24; Vinogradov Aff. Ex. G (BSABS 2005-HE9 PSA, Art. I) (definition of "Outstanding"); *id.* §5.04(b). Had the drafters of these PSAs wished to bar the write-up of zero balance classes, they would have said so, following the example of other PSAs that do explicitly say "retired" bonds are not entitled to write-ups. Tilden Br. 24; Vinogradov Aff. Ex. I (GE-WMC 2006-1 PSA, Art. I) (definition of "Highest Priority"), §4.01(g). At least one of the Trustees has recognized that retired class provisions do not bar write-ups: In a prior settlement relating to a similar trust

(BSABS 2007-AQ2), U.S. Bank correctly followed the retired class provisions by writing up bonds with zero balances. *See* Axonic Answer [Dkt. 159] at 13 n.11.

Thus, formerly "retired" certificates can have their balances increased above zero, making them once again entitled to distributions. Tilden Br. 23; *see also* Petition ¶ 57.

CONCLUSION

For the foregoing reasons, as well as those set forth in Tilden Park's opening brief, the Court should grant the relief requested in Tilden Park's Answer.

September 28, 2018
New York, New York

/s/ Jonathan L. Hochman
Jonathan L. Hochman
Anna Vinogradov
Schindler Cohen & Hochman LLP
100 Wall Street
15th Floor
New York, N.Y. 10005
T: (212) 277 6330
F: (212) 277 6333
jhochman@schlaw.com
avinogradov@schlaw.com

/s/ Philip Bentley
Philip Bentley
Andrew Pollack
Kramer Levin Naftalis & Frankel LLP
1177 Avenue of the Americas
New York, N.Y. 10036
(212) 715 9100
(212) 715 8000
pbentley@kramerlevin.com
apollack@kramerlevin.com

Attorneys for Tilden Park Investment Master Fund LP, Tilden Park Management I LLC and Tilden Park Capital Management LP, on behalf of themselves and their advisory clients (collectively, "Tilden Park")