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), Petitioners, For Judicial Instructions under CPLR Article 77 on the Administration and Distribution of a Settlement Payment.	Index No. 657387/2017

REPLY MEMORANDUM OF LAW OF DW PARTNERS LP AND ELLINGTON MANAGEMENT GROUP, L.L.C. IN SUPPORT OF THEIR MEMORANDUM ON THE MERITS OF PETITION FOR JUDICIAL INSTRUCTION UNDER ARTICLE 77 AS TO CERTAIN REMAINING DISPUTED TRUSTS

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Respondents DW Partners LP ("DW") and Ellington Management Group, L.L.C. ("Ellington" and together with DW, "Respondents"), by and through their undersigned counsel, respectfully submit this Reply Brief.[1] The arguments advanced by Nover, the Opposing Respondents, and HBK in their Response Briefs do not conform with the plain meaning or intent of the SA, and thus do nothing to undermine the conclusions that this Court must (1) direct the Petitioners to follow the terms of Section 3.06(b) of the SA (the "SA Write-Up Instruction") and write up any certificates to which losses were previously allocated in the reverse order of previously allocated losses; (2) permit future write-ups and distributions to Zero Balance Classes; and (3) direct Petitioners to use the Write-Up First Method.[2]

ARGUMENT

I. THE SA REQUIRES THAT EACH CERTIFICATE IN THE SETTLEMENT TRUSTS TO WHICH LOSSES HAVE BEEN PREVIOUSLY ALLOCATED BE WRITTEN UP, AND THE GOVERNING AGREEMENTS ARE IN ACCORD.

In the Nover Resp. Br., Nover continues to assert, incorrectly, that only the Governing Agreements for the Exhibit E Settlement Trusts dictate which certificates are "eligible" for write-ups, and that directing the Petitioners to write-up only subordinate certificates will honor the expectations of investors in the Settlement Trusts. Nover Resp. Br. at 2. Nover's positions are incorrect because (a) Nover ignores the plain language of both the Governing Agreements and

[1] This Reply Brief addresses the Response Briefs submitted by (1) Nover Ventures, LLC and The Bank of New York Mellon Trust Company, N.A., as Indenture Trustee of the Duke IX Indenture (collectively, "Nover") (the "Nover Resp. Br.") (Doc. No. 698) as to Exs. E and F; (2) the Institutional Investors (the "II's") and the AIG Parties ("AIG" and, together with the II's, the "Opposing Respondents") (the "II Resp. Br.") (Doc. No. 663) as to Exs. D and G; (3) U.S. Bank National Association, as Trustee of the NIMs Trusts, at the direction of Poetic Holdings VI LLC, Poetic Holdings VII LLC, and HBK Master Fund LP ("HBK") (the "HBK Resp. Br.") (Doc. No. 677) as to Ex. G; and (4) U.S. Bank National Association, as Trustee of the NIMs Trusts, at the direction of HBK (the "HBK Write-Up Resp. Br.") (Doc. No. 676) as to Ex. D. Respondents' Opening Brief and Opposition Brief are referred to herein as "Opening Br." (Doc. No. 645) and "Resp. Br." (Doc. No. 708), respectively.

[2] Unless otherwise noted, capitalized terms not otherwise defined herein shall have the meanings ascribed to them in the Opening Br.

the SA, and specifically Section 3.06(b) of the SA; and (b) there is no conflict between the SA Write-Up Instruction and the Governing Agreements, as the Governing Agreements do not address write-ups for bulk settlement payments like the Allocable Shares, and thus the parties to the SA were free to, and did, determine the process for applying write-ups based upon same.

A. The SA Write-Up Instruction Clearly Dictates Which Certificates in the Settlement Trusts Should Be Written-Up.

The Nover Resp. Br. advances the misguided argument that even if the terms of the SA control as to the Exhibit E Trusts, the SA, at most, suggests only an order of operations, but "does not provide any guidance as to which certificates are ***eligible*** to be written-up."[3] Nover Resp. Br. at 2. Nover suggests, "the Governing Agreements alone provide that information. . . ." *Id.* While Nover argues that the SA "unambiguously defers to the Governing Agreements" in Sections 3.06(a), 7.05, and 7.13,[4] Nover ignores that the SA Write-Up Instruction of Section 3.06(b)—the only section that addresses write-ups—does not. Nover Resp. Br. at 3.

The SA Write-Up Instruction specifies that Petitioners shall "apply . . . the amount of the Allocable Share for that Settlement Trust in the reverse order of previously allocated losses, to increase the balance of ***each class of securities*** (other than any class of REMIC residual interests) ***to which such losses have been previously allocated*** . . . ." SA § 3.06(b) (emphasis added). The SA thus plainly provides that ***any*** certificate, other than REMIC residual interests, to which losses have been previously allocated, ***is eligible*** to be written up. The fact that the SA Write-Up Instruction specifically carves out REMIC residual interests demonstrates that the

[3] As in the Resp. Br., the arguments in this Section I.A apply with equal force to the Exhibit F issue and compel the finding that the SA Write-Up Instruction controls over any of the purportedly conflicting provisions of the Governing Agreements identified in Exhibits E and F to the Petition.

[4] Respondents dispute that SA Sections 7.05 and 7.13 require deference to the Governing Agreements. Opening Br. at I.B.2; Resp. Br. at I.B.

drafters meant to designate the precise certificates that would be eligible for write-ups, and they placed no restriction on senior certificates, other than the prior allocation of losses.

Respondents have acknowledged that Section 3.06(a) directs Petitioners to defer to the Governing Agreements to make ***distributions***; yet, the drafters did not include any such direction in the SA Write-Up Instruction. *Compare* SA § 3.06(a) *with* SA § 3.06(b). Had the drafters intended that Petitioners defer to the Governing Agreements as to write-ups, they would have included language to that effect in the SA Write-Up Instruction, just as they did in the subsection immediately prior. Because they did not, Petitioners need not look beyond the SA Write-Up Instruction. This "hybrid" approach that Nover criticizes (*see* Nover Resp. Br. at 10-11)—*i.e.*, follow the Governing Agreements as to distributions and the SA as to write-ups—is precisely what the SA calls for. As such, the Court should order Petitioners to follow the express language of the SA Write-Up Instruction and write up any class to which losses have been allocated.

B. There Is No Conflict between the Governing Agreement Write-Up Instructions and the SA Write-Up Instruction.

Both Respondents' and Tilden Park's prior briefs demonstrate that, even if this Court determines that the Governing Agreement write-up instructions apply to the Allocable Shares for the Exhibit E Trusts, such instructions do not prohibit Petitioners from writing up senior certificates. Indeed, the write-up instructions in the Governing Agreements do not, by their own terms, apply to the Allocable Shares, as the Governing Agreements do not contemplate bulk settlement payments such as these. As such, the SA drafters' instructions should control. Nover responds, incorrectly, that this issue was litigated in the prior Article 77 proceeding involving the SA. Nover Resp. Br. at 12. Nover misinterprets the subject of such proceeding and its impact.

As an initial matter, while *res judicata* bars objection to the SA's terms, including the objection that such terms constitute an unlawful amendment to the Governing Agreements, it

does not extend to disputes over the interpretation of the SA, which were not and could not have been raised in the prior Article 77 proceeding. In support, Respondents adopt, and incorporate herein by reference, Point I.A of Tilden Park's Reply Brief. As such, the Court is not restrained by any prior proceedings or rulings from interpreting the SA, as such questions regarding interpretation are to be resolved in the instant proceeding as a matter of first impression.

Upon close examination of the SA Write-Up Instruction and the Governing Agreement write-up instructions for the Exhibit E Trusts that purport to limit write-ups to subordinate certificates (the "Subordinate Write-Up Provisions"), it is evident that there is no conflict between the two. The Subordinate Write-Up Provisions apply only to "Subsequent Recoveries." As such, they are inapplicable to the Allocable Shares, which are not Subsequent Recoveries, but are merely treated "as though" they were ***for distribution purposes*** (SA § 3.06(a)), not for write-up purposes (SA § 3.06(b)). Further, the Subordinate Write-Up Provisions apply only to a subset of Subsequent Recoveries—those that (1) are received by the Master Servicer and (2) reduce the Realized Loss for a specific loan. Neither applies to the Allocable Shares. *See* Opening Br. at I.A.3; Resp. Br. at I.B.; Tilden Park Opening Brief (Doc. No. 515) at III.A.2.

Nover also argues that the definitions of "Certificate Principal Balance" ("CPB") and "Current Principal Amount" ("CPA") in the Governing Agreements require that Subsequent Recoveries only be applied to specified certificates. However, as Respondents discuss in their prior briefs, any failure to address senior certificate write-ups in the Subordinate Write-Up Provisions is likely the result of scrivener's error. Indeed, the definitions of CPB or CPA in several Governing Agreements, excerpts of which are set forth in Exhibit 1 hereto, expressly contemplate senior write-ups and/or contain references to write-up sections that do not actually exist. *See, e.g.*, Ex. 1; Kushner Aff. to Opening Br., Ex. A (SAMI 2007-AR4 PSA) Art. I

(definition of CPA). In sum, the language of the SA directs Petitioners to write-up each class, and the Governing Agreements are not to the contrary, as they do not address bulk settlements or their resulting write-ups.[5] The Court should therefore issue an Order consistent with the SA, and direct Petitioners to write up all classes to which losses have been previously allocated.

II. THE RETIRED CLASS PROVISION DOES NOT PRECLUDE WRITE-UPS OR FUTURE DISTRIBUTIONS TO SO-CALLED "ZERO BALANCE CLASSES."

HBK and the Opposing Respondents each have maintained that the Retired Class Provision plainly prevents both the write-up of, and future distribution to, any Zero Balance Classes. However, HBK's and the Opposing Respondents' response briefs do nothing to dispel the notion that (1) the Retired Class Provision applies only when a certificate's balance has been reduced to zero ***as a result of its full receipt of Principal Funds***; (2) the Retired Class Provision does not address or limit write-ups; and (3) the SA Write-Up Instruction expressly requires the write-up of "each class . . . to which losses have been previously allocated." SA § 3.06(b).[6]

HBK admits that the Retired Class Provision is contained only in the section of the Governing Agreements pertaining to "Distributions,"[7] but argues that the Retired Class Provision makes no distinction between classes reduced to zero due to realized losses or due to payment in full. HBK Resp. Br. at 3-4. This argument ignores that the Governing Agreements contain a distinct waterfall provision for reducing CPBs due to each of (1) distributions and (2) losses; and

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[5] Nover also argues that limiting write-ups to subordinate certificates will not run contrary to the Governing Agreement's Credit Enhancement features as "[s]enior certificates will still receive distributions ahead of subordinate certificates, and subordinate certificates must still be the first certificates to realize losses (*i.e.* will still be written down before senior certificates)." Nover Resp. Br. at 8. This could not be further from the truth. If only subordinate certificates are written up, senior certificates will receive less principal than they otherwise will receive if write-ups are applied properly, while subordinate certificates will receive the benefit of such write-ups instead. This approach would turn the concepts of subordination and credit enhancement on their heads.

[6] This positions in this section II as to the Exhibit G issue are advanced on behalf of DW only.

[7] *See* HBK Resp. Br. 3 ("The Retired Class Provision appears in the section of the PSAs titled "Distributions," following the provisions that set out the 'waterfall' of distributions that the Trustee must make to each class of certificates on any given Distribution Date.").

only the waterfall for distributions contains a Retired Class Provision, while the waterfall for losses, which repeatedly mentions reduction of CPBs to zero, does not. *See* Kushner Reply Affirmation ("Kushner Reply Aff."), Ex. A (BSABS 2006-HE3 PSA) (the "BSABS PSA") §§ 6.04 (the Distribution waterfall); 6.05 (the Realized Loss Allocation waterfall).

Further, reviewing the Retired Class Provision in the context of the Governing Agreements as a whole confirms that the Retired Class Provision applies only where a CPB is reduced to zero as a result of a full and final distribution of all amounts owed. First, the terms of the Governing Agreements describing the process for retirement are contained in the section pertaining to the "Final Distribution on the Certificates," and set forth that, in order for a certificate to be retired, it must (1) be surrendered to the Securities Administrator and (2) receive a "final distribution." *See, e.g., id.* at § 11.02. Second, the Governing Agreements provide that distributions are to be made "to each Certificateholder of record" subject only to the "final distribution." *See, e.g., id.* § 6.04(c). The Zero Balance Classes at issue have not been surrendered nor have they received a final distribution; instead, they remain "Outstanding" per the Governing Agreements. *Id.*, Art. I (defining "Outstanding").

HBK attempts to characterize the Final Distribution provision as unrelated to the Retired Class Provision, arguing that the latter somehow creates a distinct retirement process. This effort fails, as it would require the Court to read into the Governing Agreement terms that do not exist[8] while ignoring the only interpretation that harmonizes and gives effect to all provisions and the general purpose of the Governing Agreements—that retirement occurs only upon full and final distribution. *Insurance Corp. of New York v. Central Mut. Ins. Co.*, 47 A.D.3d 469, 471 (1st Dep't. 2008) ("A contract should be 'read as a whole, and every part will be interpreted with

[8] *E.g.*, HBK Resp. Br. at 10 ("nothing in the text of the 'Final Distribution' section claims that it is exclusive, or that it sets out the only set of circumstances under which a class of certificates may enter retirement.").

reference to the whole; and if possible it will be so interpreted as to give effect to its general purpose'" (internal citations omitted)).

HBK also strains to interpret the Retired Class Provision as restricting write-ups, when it says nothing of the sort, by taking the extreme position that once a class has been reduced to zero ***either*** by distributions ***or*** allocation of losses, "every future Distribution Date is indisputably a Distribution Date after the Distribution Date on which those classes were reduced to zero, and therefore a date on which those classes are not entitled to distributions." HBK Resp. Br. at 8. HBK ignores that the Governing Agreements contemplate that if CPB has been written down because of Realized Losses, it is to be written up again when Subsequent Recoveries are received. Kushner Reply Aff., Ex. A (BSABS PSA) § 6.04(b) ("In addition to the foregoing distributions [in Section 6.04(a)]," any Subsequent Recoveries shall 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 . . . ."). Further, because *both* the write-up provision in Section 6.04(b) and the Realized Loss Allocation waterfall in Section 6.05 *follow* the Retired Class Provision found in Section 6.04(a), the language, "notwithstanding the foregoing" in the SA Write-Up Instruction has no implication here. *Id.* §§ 6.04(a), 6.04(b), 6.05. The Retired Class Provision thus cannot be interpreted in isolation, but only in the context of the whole Governing Agreements and their purpose. *See Insurance Corp. of New York*, 47 A.D.3d at 471.

Finally, HBK's interpretation ignores that the Governing Agreements' definition of CPB provides for the write-up of "any Certificate." *See* BSABS PSA § 1.01 (definition of CPB). While HBK attempts to argue that this definition fails to provide that *any* certificate is entitled to write-ups (*see* HBK Br. at 4), a close reading of this definition reveals otherwise:

> As to ***any Certificate*** (other than the Class CE Certificates or Class R Certificates) ***and as of any Distribution Date***, the Initial Certificate Principal Balance of such

> Certificate ***plus, in the case of a Class A Certificate and Class M Certificate, any Subsequent Recoveries added to the Certificate Principal Balance of such Certificate pursuant to Section 6.04(b)*** . . .

Id. (emphasis added). Under this definition, when calculating the CPB of ***any certificate*** as of ***any distribution date*** (which necessarily includes any distribution date after a CPB is reduced to zero), Petitioners must account for the receipt of any Subsequent Recoveries by writing-up balances pursuant to Section 6.04(b). Neither of these provisions excludes Zero Balance Classes; in fact, they mandate write-ups to all classes. Thus, Respondents request that this Court direct Petitioners to ignore the Retired Class Provisions as to the Exhibit G Trusts.

III. PETITIONERS MUST APPLY THE WRITE-UP FIRST METHOD.

The Opposing Respondents fail in the II Resp. Br. to raise any persuasive challenge to the propriety of the Write-Up First Method.[9] In sum, Opposing Respondents argue that the SA requires the Pay First Method and that the Governing Agreements are silent as to order of operations. II Resp. Br. at I.A, I.B. Opposing Respondents are wrong in both respects.

As to the first point, SA Section 3.06(a) governs the *method* for distributing the Allocable Shares to investors but does not speak to any order of operations. Section 3.06(a) simply states that each Settlement Trust's Allocable Share shall be deposited into the related Settlement Trust's collection or distribution account "for further distribution to Investors in accordance with the distributions provisions of the Governing Agreements." It does not specify *when* those distributions should be made or any order of operations. Only Section 3.06(b) contains a temporal instruction—that Petitioners apply write-ups "[a]fter the distribution of the Allocable Share to a Settlement Trust," not after distribution *to investors*, as Opposing Respondents claim.

[9] The positions in this section III as to the Exhibit D issue are advanced with respect to the GPMF 2006-AR1 Settlement Trust and on behalf of Ellington only. Relevant excerpts of the GPMF 2006-AR1 PSA are attached as Ex. B to the Kushner Reply Aff.

The final sentence of Section 3.06(b) does not affect this outcome. As Respondents discussed in their Opposition Brief, this sentence is meant only to clarify that the SA Write-Up Instruction shall not affect the distribution methodology called for in Section 3.06(a). Resp. Br. at 23-24. Indeed, even if Pay First is used, write-ups will still affect the distribution of the Settlement Payment, as it could result in several scenarios in which a portion of the Settlement Payment remains undistributed after the initial distribution, in which case it will be held over to future months and affect future distributions. *See id.* at 24. Thus, this final sentence cannot possibly be interpreted to mean that Section 3.06(b) is not permitted to affect the distribution of the Settlement Payment in any manner, as it will under either order of operations.

Further, as Respondents discuss in their Opposition Brief (*see* Resp. Br. at III.A.3), Opposing Respondents place far too much weight on other global settlements in arguing that the SA requires the Pay First Method. In three of the four settlements on which Opposing Respondents rely, the issue of whether the Write-Up First or Pay First Method should be used was never litigated or ruled upon by a court. While this Court did rule that the Pay First Method should be used to distribute funds from the Countrywide Settlement, the language in that agreement was not "virtually identical" to the language of the SA, but varied in critical ways. *See id.* at 20 n. 10. Where courts have been tasked with determining the order of operations as to language that is in fact substantively identical to the SA,[10] courts have held that Write-Up First is the appropriate method. *Id.* at 22 n. 12; *see also* Ex. 2 hereto, providing relevant excerpts; Kushner Reply Aff. Ex. C, Ex. D.

[10] As discussed in Section I.B., *supra*, no interpretive questions were requested by Petitioners or could have been raised in the prior Article 77 Proceeding pertaining to the SA. As such, the Opposing Respondents' argument that the Court has already approved the Pay First Method is inaccurate.

As to the Opposing Respondents' second point, the Governing Agreements are not silent as to the order of operations between distributions and write-ups, at least with respect to the GPMF 2006-AR1 Settlement Trust at issue for Ellington. The plain language of the GPMF 2006-AR1 PSA, including the definition of CPA, calls for the Write-Up First Method because, prior to making any distributions, Petitioners must determine and calculate the CPB of each certificate. *See* Kushner Reply Aff., Ex. B (GPMF 2006-AR1 PSA) Art. I (defining "Class A Principal Distribution Amount" and CPA). Distributions are then made to Certificateholders based on the CPA as of a particular Distribution Date, and thus can be made only after the calculation of CPA, which includes any increase in CPA pursuant to the application of Subsequent Recoveries. In short, none of the additional arguments put forth by the Opposing Respondents or HBK[11] adequately refutes the fact that the plain language of both the SA and the Governing Agreements supports the Write-Up First Method for the GPMF 2006-AR1 Trust.

CONCLUSION

A plain reading of the SA and the Governing Agreements compels the conclusion that (1) the SA Write-Up Instruction controls and Petitioners must write-up *any* certificate, including seniors, to which Realized Losses have been previously allocated; (2) the Retired Class Provision should not be enforced or applied to prevent the write-up of, or future distribution to, Zero Balance Classes; and (3) as to order of operations, Petitioners must use the Write-Up First Method. Respondents respectfully request that this Court enter an order reflecting the same.

[11] HBK argues that the Governing Agreements control the order of operations and call for the Pay First Method across the board. Even if the Court agrees with this argument, which Respondents dispute, it is plainly not the case with respect to the GPMF 2006-AR1 Settlement Trust, on which HBK has not appeared.

Dated: October 10, 2018
New York, New York

Respectfully submitted,

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