
New York Supreme Court

Appellate Division—First Department

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, NA, 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),

**Appellate
Case No.:
2020-02716**

Petitioners,

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

(For Continuation of Caption See Inside Cover)

RESPONSIVE BRIEF FOR AMBAC ASSURANCE CORPORATION

PATTERSON BELKNAP WEBB
& TYLER LLP
*Attorneys for Appellant-Respondent
Ambac Assurance Corporation*
1133 Avenue of the Americas
New York, New York 10036
(212) 336-2000
hjricardo@pbwt.com

Appellants-Respondents

AEGON USA INVESTMENT MANAGEMENT, LLC, BLACKROCK FINANCIAL MANAGEMENT, INC., CASCADE INVESTMENT, LLC, FEDERAL HOME LOAN BANK OF ATLANTA, FEDERAL HOME LOAN MORTGAGE CORP., FEDERAL NATIONAL MORTGAGE ASSOCIATION, GOLDMAN SACHS ASSET MGMT L.P., VOYA INVESTMENT MGMT LLC, INVESCO ADVISERS, INC., KORE ADVISORS, L.P., METROPOLITAN LIFE INS. CO., PACIFIC INVESTMENT MGMT COMPANY LLC, TEACHERS INS. AND ANNUITY ASSOC. OF AMERICA, TCW GROUP, INC., THRIVENT FINANCIAL FOR LUTHERANS and WESTERN ASSET MGMT. CO.
(the “Institutional Investors”)

– and –

Appellants-Respondents

AMERICAN GENERAL LIFE INSURANCE COMPANY, AMERICAN HOME ASSURANCE COMPANY, LEXINGTON INSURANCE COMPANY, NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PA., THE UNITED STATES LIFE INSURANCE COMPANY IN THE CITY OF NEW YORK and THE VARIABLE ANNUITY LIFE INSURANCE COMPANY
(the “AIG Parties”)

– and –

Appellants-Respondents

ELLINGTON MANAGEMENT GROUP, L.L.C. and DW PARTNERS LP
(the “Ellington and DW Parties”)

– and –

Appellants-Respondents

TILDEN PARK INVESTMENT MASTER FUND LP on behalf of itself and its advisory clients, TILDEN PARK MANAGEMENT I LLC on behalf of itself and its advisory clients and TILDEN PARK CAPITAL MANAGEMENT LP on behalf of itself and its advisory clients
(the “Tilden Park Parties”)

– and –

Appellants-Respondents

PROPHET MORTGAGE OPPORTUNITIES LP, POETIC HOLDINGS VI LLC, POETIC HOLDINGS VII LLC and U.S. BANK NATIONAL ASSOCIATION, solely in its capacity as Indenture Trustee for the Prophet and Poetic Trusts
(the “Prophet and Poetic Parties”)

– and –

Appellant-Respondent

AMBAC ASSURANCE CORPORATION
(“Ambac”)

– and –

Appellants-Respondents

U.S. BANK NATIONAL ASSOCIATION, as NIM Trustee, U.S. Bank, solely in
its capacity as Indenture Trustee for the HBK Trusts
(the “HBK Parties”)

– against –

Respondent

NOVER VENTURES, LLC
 (“Nover”)

– and –

Respondent

D.E. SHAW REFRACTION PORTFOLIOS, L.L.C.
 (“D.E. Shaw”)

– and –

Respondent

STRATEGOS CAPITAL MANAGEMENT, LLC
 (“Strategos”)

– and –

Respondents

OLIFANT FUND, LTD., FFI FUND LTD. and FYI LTD.
 (the “Olifant Parties”)

– and –

Respondents

GMO OPPORTUNISTIC INCOME FUND
 and GMO GLOBAL REAL RETURN
 (the “GMO Parties”)

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
PRELIMINARY STATEMENT	1
COUNTERSTATEMENT OF QUESTION PRESENTED	2
ARGUMENT	3
THE RELEVANT PSAs REQUIRE THE WRITE-UP FIRST METHOD	3
A. The IAS Court Correctly Held That the PSAs’ Definition of “Certificate Principal Balance” Requires the Write-Up First Method.....	3
B. Another Court Recently Held That a Substantially Similar PSA Required the Write-Up First Method	9
CONCLUSION	12
PRINTING SPECIFICATIONS STATEMENT	13

TABLE OF AUTHORITIES

Page(s)

Cases

Admiral Ins. Co. v. Marriott Int’l, Inc.,
79 A.D.3d 572 (1st Dep’t 2010)6

In the Matter of the MASTR Adjustable Rate Mortgages Trust
2007-1, No. 62-TR-CV-18-46, Dkt. 177 (Minn. Dist. Ramsey
Cnty. Oct. 27, 2020).....9, 10, 11

PRELIMINARY STATEMENT¹

The IAS Court correctly held that the Governing Agreements² for the group of trusts it dubbed the “Write-Up First Trusts” unambiguously require Petitioners to write up the certificate balances prior to distributing the Allocable Shares of the settlement payment to holders (*i.e.*, the “Write-Up First Method”). As the IAS Court explained, the PSAs’ definition of “Certificate Principal Balance” (or analogous terms)³ requires that all “Subsequent Recoveries” received by the trusts be added to increase the certificate balances *before* any distributions are paid out to certificateholders.

HBK⁴ contends that the IAS Court erred in holding that the Write-Up First Method of distribution applies to the Write-Up First Trusts, including the HBK

¹ Capitalized terms not defined herein have the meanings given to them in Ambac’s opening brief or HBK’s opening brief.

² As noted in Ambac’s opening brief, the Governing Agreements for the Ambac Trusts are styled as PSAs. Accordingly, Ambac uses those two terms interchangeably.

³ The IAS Court analyzed the definition of “Certificate Principal Balance” set forth in the PSA of an exemplar trust from the Write-Up First Trust group (the BSABS 2005-AQ2 Trust), which is substantially similar to the definition of “Current Principal Amount” used in the Ambac Trust PSAs. (R.36.) To avoid confusion, Ambac uses the terminology from the exemplar trust discussed by the IAS Court.

⁴ Because HBK Master Fund L.P. holds indirect interests in the relevant RMBS trusts, its interests are now represented by U.S. Bank National Association (“U.S. Bank”). Following a dispute concerning the standing of indirect holders, U.S. Bank substituted for HBK as a party in this CPLR Article 77 proceeding and is acting in its capacity as Indenture Trustee for certain NIM Trusts at HBK’s direction. Given that U.S. Bank plays multiple roles in this action—and has separate counsel in its role as NIM Trustee acting at HBK’s direction—Ambac refers to these parties jointly as “HBK.”

Trusts and the Ambac Trusts.⁵ (HBK Br. at 22-27.)⁶ Despite arguing to the IAS Court that the PSAs clearly addressed the proper “order of operations,” HBK now contends that the PSAs are “silent” on this issue and that the Settlement Agreement therefore controls. (*Id.* at 22.) This Court should reject HBK’s new argument as inconsistent with the PSAs’ plain terms, as the IAS Court did below.

The IAS Court’s ruling concerning the order of operations applicable to the Write-Up First Trusts is also supported by recent authority on this issue. Just weeks ago, another court considering substantially similar contract language found that the relevant PSA required the trustee to use the Write-Up First Method in distributing an RMBS settlement payment. Thus, this Court should affirm the IAS Court’s ruling that the PSAs for the Write-Up First Trusts require the Write-Up First Method.⁷

COUNTERSTATEMENT OF QUESTION PRESENTED

Where the relevant PSAs contain a definition of “Certificate Principal Balance” that requires all Subsequent Recoveries to be added to the certificate

⁵ While the HBK Trusts and the Ambac Trusts do not overlap, they were both the subject of the IAS Court’s ruling concerning the proper order of operations for the Write-Up First Trusts. (R.36; R.41.) Thus, Ambac responds to HBK’s arguments in order to demonstrate why the IAS Court’s ruling on that issue should be affirmed.

⁶ “HBK Br.” refers to HBK’s opening brief, which was filed with this Court on November 2, 2020.

⁷ This contractual interpretation issue applies to all three Ambac Trusts, including the 2005 Trust and the 2006 Trusts. However, if this Court accepts Ambac’s argument in its opening brief that Ambac has a priority right to receive the entire Allocable Shares for the 2006 Trusts (Ambac Br. at 9-17), the Court need not reach the “order of operations” issue with respect to those trusts.

balance prior to any distribution of those funds, is the Write-Up First Method required?

Answer of the IAS Court: The IAS Court correctly answered “yes.”

ARGUMENT

THE RELEVANT PSAS REQUIRE THE WRITE-UP FIRST METHOD

The IAS Court correctly held that the PSAs control the “order of operations” for the Write-Up First Trusts, and that those contracts require the certificate balances to be written up on account of the Allocable Shares *prior* to distribution of those funds to holders. While HBK contends that the trusts’ PSAs do not address the order of operations, its arguments do not withstand scrutiny. Indeed, HBK did not even make these arguments before the IAS Court. This Court should reject HBK’s newly-adopted theory and affirm the IAS Court’s ruling concerning the Write-Up First Method.

A. The IAS Court Correctly Held That the PSAs’ Definition of “Certificate Principal Balance” Requires the Write-Up First Method

As the IAS Court explained, the Settlement Agreement provides that each Settlement Trust’s Allocable Share of the settlement payment must be distributed “*in accordance with the distribution provisions of the Governing Agreements . . . as though [it] was a ‘subsequent recovery’ relating to principal proceeds*” (R.32 (quoting Settlement Agreement Section 3.06(a)) (emphasis added).)

Accordingly, the IAS Court held that the trusts’ “Governing Agreements control where they specify the order of operations, and the Settlement Agreement controls only where the Governing Agreements do not specify such order.” (R.34.) With respect to the Write-Up First Trusts, the IAS Court correctly found that the PSAs require the Write-Up First Method of distribution. (R.41.)

The IAS Court found that the order of operations is provided by “the definition in the PSA of Certificate Principal Balance.” (R.36-37.) Because the distribution of any Subsequent Recoveries is based on the Certificate Principal Balances for each class of certificates, those balances must be calculated before any distribution can be performed. As the IAS Court explained, the calculation set forth in the PSAs’ definition of Certificate Principal Balance requires the write-up step to precede the distribution step:

[The] Certificate Principal Balance is the balance “as of any Distribution Date” of the Initial Certificate Principal Balance, plus . . . “*any* Subsequent Recoveries added to the Certificate Principal Balance of such Certificate[s] pursuant to Section 5.04(b),” less (i) all amounts distributed “in reduction of the Certificate Principal Balance thereof *on previous Distribution Dates* . . . and (ii) any Applied Realized Loss Amounts allocated to such Certificate[s] *on previous Distribution Dates*.” The definition of Certificate Principal Balance thus provides for deduction of payments of principal that were made “on previous Distribution Dates” and for deduction of losses that were allocated “on previous Distribution Dates.” In contrast, this definition provides for addition not only of previously distributed Subsequent Recoveries

but of “any” Subsequent Recoveries “as of any Distribution Date.” Had the drafters intended to include only previous subsequent recoveries in the calculation of Certificate Principal Balance and thereby to delay the write-up of such subsequent recoveries, they could have done so, as they did for other principal distributions and losses.

(R.37-38 (emphasis added).) In other words, because the Certificate Principal Balance is increased by “*any* Subsequent Recoveries”—including those received during the current period—but is reduced by only those distributions and losses allocated “on *previous* Distribution Dates,” this provision makes clear that Subsequent Recoveries received during the current period must be added to the Certificate Principal Balance before any distributions are made to certificateholders.

HBK argues that the PSAs are completely “silent” as to the order of operations and, therefore, the Settlement Agreement controls with respect to this issue. (HBK Br. at 22.) This contention is completely at odds with what HBK argued before the IAS Court, namely that the Governing Agreements unambiguously require the distribution to precede the write-up (*i.e.*, the “Pay First Method”). HBK argued below that “[b]ecause the order of payment and write-up is *not unaddressed* in the HBK Settlement Trust PSAs, the Court should simply apply the PSAs as written, and direct Petitioners to make distributions . . . as provided by Section 5.04(a) of the HBK Settlement Trust PSAs before writing up

certificate balances as provided by Section 5.04(b).” (R.4960 (emphasis added).)

The IAS Court rejected HBK’s construction of the PSAs and held that the plain language of the contracts requires the Write-Up First Method. (R.40-41.) HBK cannot change course on appeal and argue for the first time that the PSAs do not address the order of operations *at all*. See *Admiral Ins. Co. v. Marriott Int’l, Inc.*, 79 A.D.3d 572, 572 (1st Dep’t 2010) (holding that “a party is prohibited from arguing on appeal a theory not advanced before the court of original instance”).

In any event, the IAS Court rightly rejected HBK’s current argument, which other parties made below (but, tellingly, did not pursue on appeal).⁸ The court stated that the “need for interpretation of the[] [PSA] provisions does not mean that they are *silent* as to the order of operations.” (R.39 (emphasis added).) The IAS Court again emphasized that the definition of Certificate Principal Balance “expressly provides that ‘*any*’ Subsequent Recoveries are to be added to the balance”—without any temporal limitation. (*Id.* (emphasis added).) In contrast, the other components of the calculation are expressly limited to amounts distributed or allocated “on previous Distribution Dates.” (R.38.) This means that as of any given Distribution Date, the Certificate Principal Balance *includes* Subsequent Recoveries received since the prior Distribution Date, but *does not*

⁸ The Institutional Investors argued in favor of the Pay First Method before the IAS Court with respect to a much larger number of trusts than HBK, and the court rejected their argument. (R.38-39.) The Institutional Investors did not appeal the IAS Court’s ruling on the “order of operations” issue, despite filing a lengthy appellate brief concerning other issues.

include any distribution of principal or allocation of losses made since the prior Distribution Date. The IAS Court correctly held that this definition provides an order of operations for the Write-Up First Trusts and requires the certificate balances to be written up to account for the Allocable Shares *before* any distributions are made to certificateholders.

The definition of Certificate Principal Balance for the Write-Up First Trusts stands in stark contrast to the relevant definition for certain trusts that the IAS Court dubbed the “Pay First Trusts.” (R.41-42.) As the IAS Court explained, the PSA for one such trust (the BSABS 2005-SD2 Trust) requires the Pay First Method because it defines Certificate Principal Balance in a manner that *also* imposes a temporal limitation on the Subsequent Recoveries that are included in the calculation. The definition of Certificate Principal Balance “limits the Subsequent Recoveries to be added to the balance (i.e., written up) to ‘any Subsequent Recoveries allocated to such Class *on previous Distribution Dates*’”—precisely the language that was missing from the Write-Up First Trusts’ PSAs. (R.42 (emphasis added).)

The critical distinctions between the relevant definitions for the Write-Up First Trusts and the Pay First Trusts can be seen in the following table:

Trust	Definition of Certificate Principal Balance
Write-Up First Trust (BSABS 2005-AQ2)	As to any Certificate . . . 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 5.04(b), less the sum of (i) all amounts distributed with respect to such Certificate in reduction of the Certificate Principal Balance thereof <i>on previous Distribution Dates</i> pursuant to Section 5.04, and (ii) any Applied Realized Loss Amounts allocated to such Certificate <i>on previous Distribution Dates</i> .
Pay First Trust (BSABS 2005-SD2)	As to any Certificate . . . and as of any Distribution Date, the Initial Certificate Principal Balance of such Certificate, reduced by the sum of (i) all amounts distributed with respect to such Certificate in reduction of the Certificate Principal Balance thereof <i>on previous Distribution Dates</i> pursuant to Section 5.04, and (ii) in the case of any Subordinated Certificate, any Applied Realized Loss Amounts allocated to such Certificate <i>on previous Distribution Dates</i> , and increased by (iii) in the case of each such Class of Subordinated Certificates, any Subsequent Recoveries allocated to such Class <i>on previous Distribution Dates</i> pursuant to Section 5.04A.

(R.3530; R.3548 (emphasis added).) Because the PSAs for the Write-Up First Trusts, unlike the Pay First Trusts, do not impose any temporal limitation on the Subsequent Recoveries that are included in the calculation of the Certificate Principal Balance, those trusts’ balances must be written up to account for Subsequent Recoveries prior to any distribution of those funds.

HBK further argues that the PSAs’ inclusion of “orders of operations” for *other* types of calculations (and their asserted failure to do so with respect to

Subsequent Recoveries) demonstrates that the contracting parties “must have foreseen” this issue and “decided not to address it.” (HBK Br. at 26.) In other words, HBK contends that the drafters deliberately failed to specify how the trustees should sequence write-ups and distributions relating to Subsequent Recoveries. This suggestion is absurd on its face. It would be wholly illogical for the highly sophisticated parties to make a deliberate choice to withhold instructions concerning the order of operations relating to Subsequent Recoveries, which are received by the trusts in the normal course.

B. Another Court Recently Held That a Substantially Similar PSA Required the Write-Up First Method

Recently, another court held that substantially similar PSA language required the Write-Up First Method, agreeing with the IAS Court’s ruling on this issue. In *In the Matter of the MASTR Adjustable Rate Mortgages Trust 2007-1*, No. 62-TR-CV-18-46, Dkt. 177 (Minn. Dist. Ramsey Cnty. Oct. 27, 2020) (“*MASTR*”), petitioner Wells Fargo—which is likewise a Petitioner here—sought judicial instruction as to whether the relevant PSAs required the Write-Up First Method or the Pay First Method in distributing an RMBS settlement payment. Like the Settlement Agreement at issue here, the *MASTR* settlement agreement required the settlement proceeds to be treated as subsequent recoveries. In its petition, Wells Fargo recognized that “[t]he [PSA’s] definition of Certificate Principal Balance supports the ‘write up first’ method for processing Subsequent

Recoveries . . . because the definition suggests a specific order to the steps for calculating a Certificate Principal Balance.” (R.4765.) Wells Fargo reasoned that “the amount of Subsequent Recoveries included in the calculation [of the Certificate Principal Balance] encompasses Subsequent Recoveries applied in the current payment period, but **not** principal paid or Applied Realized Loss Amounts allocated in the current payment period.” (R.4766 (emphasis in original).) Wells Fargo concluded that “the provision appears to require the write up of Certificate Principal Balances *before* paying principal or allocating Applied Realized Loss Amounts for any given Distribution Date.” (*Id.* (emphasis added).)

The *MASTR* court agreed. It reasoned that the relevant PSAs’ definitions of Certificate Principal Balance “necessarily require the Trust Administrator to use the ‘write up first’ method rather than the ‘pay first’ method to properly calculate distributions.” *MASTR* at 4. The court further explained that the “‘pay first’ method” would be “inconsistent with the PSAs’ definitions of ‘Certificate Principal Balance’” and that it “lack[ed] support in the Trusts’ PSA language.” *Id.* Thus, the court ordered Wells Fargo to distribute the settlement payment at issue in accordance with the Write-Up First Method. *Id.*

The reasoning of *MASTR* applies with equal force here. As in *MASTR*, Wells Fargo and other Petitioners seek instruction on the distribution of an RMBS settlement payment under settlement terms that require the payment to be treated

as a Subsequent Recovery under the relevant PSAs. As in *MASTR*, the PSAs' definition of "Certificate Principal Balance" (or analogous terms) for the Write-Up First Trusts contains a "specific order to the steps" of the calculation, *id.*: the Certificate Principal Balance includes Subsequent Recoveries received in the current period but does *not* deduct principal paid or losses allocated in the current period. Thus, the PSAs require the Certificate Principal Balance to be written up *prior* to any distribution of the settlement payment.

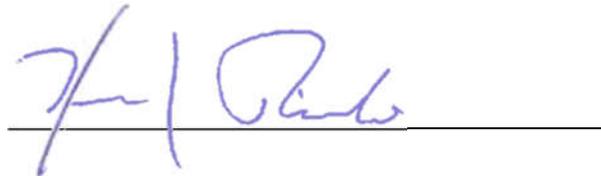
Consistent with this authority, the Court should affirm the IAS Court's holding that the PSAs for the Write-Up First Trusts require the use of the Write-Up First Method.

CONCLUSION

For the reasons stated above, the Court should affirm the IAS Court's ruling that the Petitioners must distribute the Allocable Shares due to the Write-Up First Trusts using the Write-Up First Method, in accordance with the trusts' PSAs.

Dated: New York, New York
December 2, 2020

Respectfully submitted,



PATTERSON BELKNAP WEBB &
TYLER LLP

Henry J. Ricardo

1133 Avenue of the Americas

New York, NY 10036-6710

Tel: (212) 336-2000

Fax: (212) 336-2222

hjricardo@pbwt.com

Attorney for Ambac Assurance Corporation

PRINTING SPECIFICATIONS STATEMENT

I hereby certify pursuant to 22 N.Y.C.R.R. § 1250.8(j) that the foregoing brief was prepared on a computer using Microsoft Word.

Type: A proportionally spaced typeface was used, as follows:

(i) Name of Typeface: Times New Roman

(ii) Point Size: 14

(iii) Line Spacing: Double

Word Count: The total number of words in this brief, inclusive of point headings and footnotes and exclusive of pages containing the table of contents, table of authorities, proof of service, and this Statement, is 2,692.