Exhibit 3

To be Argued by:
DANIELLE L. ROSE
(Time Requested: 15 Minutes)

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),

Petitioners,

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

(For Continuation of Caption See Inside Cover)

Appellate Case No.: 2020-02716

OPENING BRIEF FOR HBK PARTIES

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New York County Clerk's Index No. 657387/17

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")

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CASES

U.S. Bank National Association ("U.S. Bank"), solely in its capacity as Indenture Trustee for certain NIM Trusts holding direct interests in certain RMBS trusts (the "HBK Trusts") and solely at the direction of HBK Master Fund L.P. ("HBK"), by its undersigned counsel, respectfully submits this brief in support of its appeal from the Decision and Order of Supreme Court for the County of New York (Friedman, J.) ("Supreme Court"), entered February 13, 2020.[1]

PRELIMINARY STATEMENT

Supreme Court's Decision should be reversed because it erroneously decided three trust administration and distribution issues affecting the HBK Trusts. As shown herein, the agreements governing the HBK Trusts compel reversal of the Decision and Order.

[1] Pursuant to Supreme Court's order (Dkt. No. 471) (the "Substitution Order") and at the direction of HBK, U.S. Bank, solely in its capacity as Indenture Trustee under the NIM Trusts referenced on R. 5386 (which hold a direct interest in the HBK Trusts), substituted into the Supreme Court proceedings in place of HBK. This memorandum reflects the positions of HBK. U.S. Bank, in its capacity as Indenture Trustee under certain other NIM Trusts, pursuant to the Substitution Order and acting at the direction of Poetic Holdings VI LLC, Poetic Holdings VII LLC (collectively, "Poetic") and Prophet Mortgage Opportunities Fund LLP ("Prophet"), separately appeared in the proceedings before Supreme Court. In that separate capacity, U.S. Bank, acting at the direction of Poetic and Prophet, is separately filing a joinder that adopts certain arguments set forth herein. Further, U.S. Bank's capacity in its role as NIM Trustee hereunder is a separate and distinct capacity from that of U.S. Bank in its role as Petitioner and Trustee of the RMBS trusts at issue in the underlying settlement.

In 2014, JPMorgan Chase & Co. and the trustees of several hundred trusts backed by residential mortgages (often referred to as RMBS trusts) entered into a settlement agreement to resolve various claims (the "Settlement Agreement"). The Settlement Agreement required JPMorgan to pay approximately $4.5 billion, which was allocated among the various trusts. The Settlement Agreement provides that each trust's share is to be (i) treated as if the funds were "subsequent recoveries" relating to principal; and (ii) distributed to classes of certificates in accordance with the trust's governing agreements.

The Settlement Agreement also addresses the sequence, or order of operations, for applying the subsequent recoveries. It provides that each trust's share should first be distributed and, after payment, the relevant class certificate principal balances increased (the "Pay First Method"). But the Settlement Agreement also requires adherence to each trust's governing agreement, which terms the Settlement Agreement does not alter. As a practical matter, this means that, where a trust governing agreement addresses the order of operations, those terms control. But where a trust governing agreement is silent on the order of operations, the Pay First Method applies.

In 2017, the RMBS trustees petitioned Supreme Court for instruction as to how to interpret various administration and distribution provisions in the governing agreements. Following briefing and argument, Supreme Court issued its Decision

and Order. As to the HBK Trusts, the Decision and Order generally resolved matters by reference to an exemplar pooling and servicing agreement (the Bear Stearns Asset Backed Securities Trust 2005-AQ2), which has relevant terms substantially identical to those in the other HBK Trusts.

Supreme Court's Decision and Order should be reversed as to the HBK Trusts. *First*, Supreme Court erroneously held that, upon receipt of subsequent recoveries, the RMBS trustees for the HBK Trusts must increase, or "write up," a class's certificate principal balance *before* distributing the settlement funds (the "Write-Up First Method"). But the pooling and servicing agreements governing the HBK Trusts (the "HBK Trust PSAs") do not contain any terms addressing the order of operations, much less requiring the Write-Up First Method. Consequently, the Settlement Agreement's Pay First Method controls instead.

Second, Supreme Court erroneously disregarded an HBK Trust PSA provision that prohibits trust distributions to certain classes of certificates. The HBK Trust PSAs each contain an unambiguous term requiring, without exception, that certain classes be retired and no longer receive distributions after their certificate principal balances have been reduced to zero. In allowing these zero balance classes to be written up and receive distributions, Supreme Court erroneously found such classes "retired" only until the Trust receives subsequent recoveries. The contracts contain no such exception.

Third, Supreme Court erroneously substituted its view as to what the PSA overcollateralization terms should have said instead of applying what the unambiguous PSA terms in fact provide. The HBK Trusts are "overcollateralization" trusts, meaning that they started with more assets than liabilities and, as relevant here, have a separate "excess cashflow" waterfall through which certain overcollateralization amounts are distributed. This overcollateralization feature is fundamental to the HBK Trusts' structure.

Once the Pay First Method is properly implemented, some portion of the settlement payment allocated to the HBK Trusts should be distributed through the excess cashflow waterfall. Supreme Court was, however, apparently worried that the settlement funds created only temporary, or somehow illusory, overcollateralization, which did not correspond to the overcollateralization trusts' actual performance. Supreme Court thus declined to follow the plain and unambiguous terms governing the excess cashflow calculations and effectively disallowed such distributions. Under New York law, Supreme Court was not, however, authorized to alter the PSAs. New York courts must enforce the unambiguous contractual terms agreed to by sophisticated parties.

In short, this Court should give effect to the plain language of the HBK Trust PSAs and reverse the portions of Supreme Court's Decision and Order pertaining to the HBK Trusts in order to: (1) apply the Settlement Agreement's Pay First Method

to the HBK Trusts; (2) enforce the plain language of the retired class provision; and (3) give effect to the overcollateralization provisions.

QUESTIONS PRESENTED

1. The governing agreements of certain RMBS trusts explicitly resolve the sequence, or order of operations, for applying subsequent recoveries to classes of certificates. The HBK Trust PSAs do not explicitly specify whether the Write-Up First Method or Pay First Method applies. Did Supreme Court err by holding that the definition of certificate principal balance in the HBK Trust PSAs requires the application of the Write-Up First Method?

Answer: Yes. The HBK Trusts are silent on the order of operations and, in that circumstance, the Settlement Agreement's Pay First Method applies.

2. When certain class certificate principal balances have been reduced to zero, the HBK Trust PSAs state that such certificates are "retired and will no longer be entitled to distributions" on any subsequent distribution date. Did Supreme Court err in holding that these zero balance classes may nevertheless be written up and receive future distributions?

Answer: Yes. Certain HBK Trust classes of certificates cannot be written up or receive future distributions after their certificate principal balances have been reduced to zero.

3. The HBK Trust PSAs require certain overcollateralization amounts to be distributed through an excess cashflow waterfall. The overcollateralization amount available for distribution is calculated by reference to the certificate principal balance "after taking into account the payment of principal." Did Supreme Court err in holding that the RMBS trustees for the HBK Trusts must take into account the certificate principal balance following the payment of principal as well as application of subsequent recoveries?

Answer: Yes. Under the HBK Trust PSAs, the overcollateralization amount takes into account the class certificate principal balance after payment of principal and does not include increases to class certificate principal balances due to subsequent recoveries.

STATEMENT OF THE CASE

A. The Settlement Agreement

This appeal concerns the distribution of funds received by various RMBS trusts as a result of the Settlement Agreement. Under the Settlement Agreement, each of the over 300 participating RMBS trusts received a share of the settlement payment (the "Allocable Share"). The Settlement Agreement provides that each such Allocable Share shall be (i) treated under the respective governing agreement as "a 'subsequent recovery' relating to principal proceeds available for distribution on the immediately following distribution date," and (ii) distributed "in accordance with the distribution provisions of the Governing Agreements." (R. 418 (Settlement Agreement § 3.06(a)).) By its terms, the Settlement Agreement does not "amend[] . . . any term of any Governing Agreement." (R. 424 (Settlement Agreement § 7.05); *see also* R. 53 (Order at 28) ("[T]he Settlement Agreement does not supersede or override the Governing Agreements.").)[2]

[2] The HBK Trusts are listed on R. 4969. The governing agreements for the HBK Trusts are the HBK Trust PSAs. They contain substantively identical terms relevant to the questions presented here. For ease of reference, this brief cites to the BSABS 2005-AQ2 PSA, as Supreme Court analyzed that trust in addressing the order of operations for the HBK Trusts and its provisions related to retired classes and overcollateralization are substantively identical to those that Supreme Court addressed in evaluating those issues.

The Settlement Agreement also mandates that the RMBS trustees first "distribute each Settlement Trust's Allocable Share," and then "*[a]fter* the distribution of the Allocable Share," increase the relevant class certificate principal balances. (R. 418 (Settlement Agreement § 3.06(b)).)

B. The HBK Trust PSAs

The HBK Trust PSAs contain various provisions addressing how payments shall be distributed among the classes of certificates when borrowers make payments on the residential mortgage loans backing the HBK Trusts. There are three separate "waterfalls"—contractual provisions governing monthly distributions—for payments of interest funds, principal funds, and, when applicable, excess cashflow to classes of certificates.[3]

The HBK Trust PSAs also recognize that, in certain circumstances, the Trusts may receive amounts with respect to mortgage loans that were previously foreclosed upon and thereby liquidated. These are known as "subsequent recoveries." (R. 1019 (PSA § 1.01) ("Subsequent Recoveries").) As discussed above, under the Settlement Agreement, each trust will treat its Allocable Share as if such funds were "subsequent recoveries of principal." (R. 418 (Settlement Agreement § 3.06(a)).)

[3] The interest waterfall is not relevant to the questions presented here.

The issues here turn on how the settlement funds, or subsequent recoveries (the "Subsequent Recoveries"), should be distributed within the HBK Trusts, given the terms of the HBK Trust PSAs and the Settlement Agreement. Several HBK Trust PSA provisions, found in Sections 5.04(a) and 5.04(b) along with defined terms used therein, inform this analysis.

1. The Principal Waterfall and the Certificate Principal Balance Definition

Section 5.04(a) of the HBK Trust PSAs governs monthly principal distributions. Available "Principal Funds" are paid to the various classes of certificates, in order of priority, until the "Certificate Principal Balance thereof is reduced to zero." (*See* R. 3532–3535 (PSA § 5.04(a)(2)).)

A class Certificate Principal Balance is the aggregate principal amount owed to a class on the "Distribution Date," meaning the date each month that the trust distributes funds to classes. (R. 3530 (PSA § 1.01) (defining "Certificate Principal Balance").) When a trust is established, most classes of certificates are assigned an Initial Certificate Principal Balance.

Over time, a class Certificate Principal Balance may be reduced in two ways. First, each time a class receives a principal payment, the corresponding Certificate Principal Balance is then reduced by that amount. Second, if the mortgage loans backing the trust sustain losses—for example, because a borrower defaults on its

payment obligations—the HBK Trust PSAs direct that such losses are allocated to various classes "after the actual distributions to be made on such date." (*See* R. 3539–3542 (PSA § 5.05) ("Allocation of Realized Losses").) These losses likewise reduce the Certificate Principal Balance amount.

As explained below, the HBK Trusts also specify a process by which a class Certificate Principal Balance can be increased, or "written up," if an HBK Trust receives a Subsequent Recovery—and thereby receives some portion of the principal the trust previously recognized as a loss. (R. 3537 (PSA § 5.04(b)).)

Taken together, as of any given Distribution Date, a class Certificate Principal Balance is equal to its Initial Certificate Principal Balance, minus the principal payments made and losses realized on prior Distribution Dates, plus Subsequent Recoveries added thereto pursuant to Section 5.04(b). The definition of "Certificate Principal Balance" in the HBK Trust PSAs provides:

> As to any Certificate (other than the Class CE Certificates or any Class R 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 on previous Distribution Dates pursuant to Section 5.04, and (ii) any Applied Realized Loss Amounts allocated to such Certificate on previous Distribution Dates.

(R. 3530 (PSA § 1.01) ("Certificate Principal Balance").) The Certificate Principal Balance thus operates as a ledger, tracking the amounts owed to each class on a given Distribution Date.

2. The Excess Cashflow Waterfall

In addition to the principal waterfall, the HBK Trust PSAs each contain an "Excess Cashflow" waterfall set forth in Section 5.04(a)(3). (R. 3535–3536 (PSA § 5.04(a)(3)).) The HBK Trusts are overcollateralization trusts, meaning that they began with an excess of assets (the collateral) over liabilities (the outstanding principal balance of the certificates), and have mechanisms for both increasing and paying out that overcollateralization over the Trust's life. (*See* R. 370–71 (Pet. ¶¶ 24–26).) Where the amount of funds available for distribution exceeds certain defined thresholds set forth in the HBK Trust PSAs, that excess is distributed through the "Excess Cashflow" waterfall, which is "separate and apart" from the principal waterfall. (R. 374 (Pet. ¶ 30).)

If an HBK Trust has adequate funds to have a positive "Overcollateralization Release Amount," then funds flow through the Excess Cashflow waterfall in accordance with its terms. To determine the "Overcollateralization Release Amount," the PSA compares the "Overcollateralization Target Amount"—namely, the amount of overcollateralization the trust seeks to have—with the "Overcollateralization Amount" calculated pursuant to the PSA. (*See* R. 5292 (PSA

§ 1.01) (defining "Overcollateralization Amount," "Overcollateralization Release Amount," and "Overcollateralization Target Amount").)

The Overcollateralization Amount is calculated by reference to the Certificate Principal Balance "after taking into account payment of principal." As to any Distribution Date, the Overcollateralization Amount means:

> . . . the excess, if any, of the aggregate Stated Principal Balance of the Mortgage Loans as of the last day of the related Due Period . . . over the aggregate Certificate Principal Balance of the Certificates (other than the Class CE and 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* R. 5292 (PSA § 1.01) ("Overcollateralization Amount").)

When the Overcollateralization Amount exceeds the Overcollateralization Target Amount, the resulting sum—the Overcollateralization Release Amount—is then combined with the "Remaining Excess Spread" (an amount derived from any excess of interest funds over certain specified targets) to constitute "Excess Cashflow." (*See* R. 5206 (PSA § 1.01) (defining "Excess Cashflow," "Extra Principal Distribution Amount," and "Excess Spread"); R. 3532 (PSA § 5.04(a)(1)) (defining the calculation and payment of Excess Spread).)

As the RMBS trustees recognized in their Petition (*see* R. 372–75 (Pet. ¶¶ 28–34)), if the Pay First Method were applied to an overcollateralization trust, the trust's

receipt of its Allocable Share could result in distributions under the Excess Cashflow waterfall.

3. The Retired Class Provision

Following the waterfall provisions, the HBK Trust PSAs address situations where certain class Certificate Principal Balances have been reduced to zero and such classes are "retired" (the "Retired Class Provision"). The Retired Class Provision—set forth at the end of Section 5.04(a)—provides:

> In addition, notwithstanding the foregoing, on any Distribution Date after the Distribution Date on which the Certificate Principal Balance of a Class of Class A or Class M Certificates has been reduced to zero, that Class of Certificates will be retired and will no longer be entitled to distributions, including distributions in respect of Prepayment Interest Shortfalls or Basis Risk Shortfall Carry Forward Amounts.

(R. 3536 (PSA § 5.04(a)); *see also* (R. 382 (Pet. ¶ 54).)

Thus, once those class Certificate Principal Balances have "been reduced to zero" and "notwithstanding" the other distribution provisions set forth in Section 5.04(a), the Retired Class Provision mandates that such classes "will be retired and will no longer be entitled to distributions." This restriction applies regardless of whether the class Certificate Principal Balance is reduced due to monthly principal payments or the allocation of realized losses. No matter why the reduction occurs, if, on a Distribution Date, these classes are "reduced to zero" ("Zero Balance Classes"), they are "retired" and are "no longer . . . entitled to distributions."

The RMBS trustees recognized in their Petition that the Retired Class Provision "appears to preclude any further distributions" to certain classes identified in the applicable PSAs "if the aggregate certificate principal balance of such class has been reduced to zero, no matter whether the Zero Balance Classes have been reduced to zero as a result of realized losses or because they have been paid in full as to their initial certificate principal balance." (R. 382 (Pet. ¶ 55).)

4. The Subsequent Recovery Provision

The HBK Trust PSAs then address—in Section 5.04(b)—how the trustees should apply Subsequent Recoveries among the various classes (the "Subsequent Recovery Provision"). Subsequent Recoveries are "applied to increase the Certificate Principal Balance of the Class of Certificates with the highest payment priority to which Realized Losses have been allocated." (R. 3537 (PSA § 5.04(b)).) Then, remaining subsequent recoveries are "applied to increase the Certificate Principal Balance of the Class of Certificates with the next highest payment priority . . . and so on." (*Id*.) Further, "[a]ny such increases shall be applied to the Certificate Principal Balance of each Certificate of such Class in accordance with its respective Percentage Interest." (*Id.*)

The Subsequent Recovery Provision does not, however, address the sequence, or order of operations, for increasing class Certificate Principal Balances upon

receipt of Subsequent Recoveries and does not call for the RMBS trustees to apply either the Write-Up First Method or the Pay First Method.

C. The Decision and Order

In its Decision and Order, Supreme Court resolved three issues germane to the administration and distribution of each HBK Trust's Allocable Share. Supreme Court held that: (i) the definition of "Certificate Principal Balance" in the HBK Trust PSAs mandates that the Write-Up First Method be applied; (ii) the Certificate Principal Balance of Zero Balance Classes can be increased, or "written up," enabling such classes to receive future Trust distributions despite the Retired Class Provision; and (iii) the Overcollateralization Amount must be calculated so that no trust's Allocable Share is distributed through the Excess Cashflow waterfall. Supreme Court resolved each of these issues solely by interpreting trust governing agreements and the Settlement Agreement, and without any discovery.

1. The Order of Operations

As to the order of operations, Supreme Court first analyzed whether the Settlement Agreement's Pay First Method applied to all trusts. Supreme Court held that some governing agreements indisputably mandate either the Write-Up First Method or the Pay First Method and, in such circumstances, the governing agreement terms control the order of operations. Where, however, the governing

agreements are silent on the order of operations, Supreme Court held that the Settlement Agreement's Pay First Method applies. (R. 34 (Order at 9).)

As to the HBK Trusts, Supreme Court held that the exemplar PSA (for the BSABS 2005-AQ2 Trust) requires that the HBK Trusts apply the Write-Up First Method. (R. 35–41 (Order at 10–16).) Supreme Court acknowledged that the HBK Trust PSAs' order-of-operations provisions were not "as explicit[]" as certain other RMBS trusts and that the Subsequent Recovery Provision—Section 5.04(b))—does not address the order of operations. (R. 14 (Order at 39).) Supreme Court nonetheless held that the definition of "Certificate Principal Balance" mandates the Write-Up First Method for the HBK Trusts.

Supreme Court reasoned that, as to reductions to the Certificate Principal Balance for payments of principal and realized losses, the definition requires the RMBS trustees to subtract payments of principal made "on previous Distribution Dates" and losses allocated "on previous Distribution Dates." By contrast, Supreme Court stressed, Subsequent Recoveries are not limited to "previous Distribution Dates." Rather, as to Subsequent Recoveries, the definition includes "any Subsequent Recoveries added to the Certificate Principal Balance of such Certificate pursuant to Section 5.04(b)." Supreme Court held that, because this clause refers to Subsequent Recoveries "added" (in the past tense) but not specifically on a "previous Distribution Date," the HBK Trust PSAs must require the RMBS trustees to apply

the Write-Up First Method (and thereby add Subsequent Recoveries to the Certificate Principal Balances immediately prior to monthly distributions of principal). (R. 39–40 (Order at 14–15).)

2. Zero Balance Class Distributions

Supreme Court recognized that the Retired Class Provision "expressly prohibit[s] distributions to zero balance classes." (R. 63 (Order at 38).) Notwithstanding this prohibition, Supreme Court noted that such Retired Class Provisions "do not address write-ups of certificate balances in connection with subsequent recoveries." (*Id.*) Then turning to the Subsequent Recovery Provision, Supreme Court stated that such provision does "not limit the classes that may be written up on account of subsequent recoveries." (*Id.*) Based on the Subsequent Recovery Provision, Supreme Court held that Zero Balance Classes may be increased, or "written up," to the extent of realized losses previously allocated. And, upon the Zero Balance Classes being written up, Supreme Court found these classes would be entitled to receive distributions under Section 5.04(a). Supreme Court concluded that such outcome accords with the Settlement Agreement's objective: to "compensate investors for losses in connection with the mortgage loans." (R. 64 (Order at 39).)

3. Excess Cashflow Distributions

The Petition informed Supreme Court that, if the Pay First Method were applied to overcollateralization trusts, then under the governing agreements' terms, "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." (R. 372–73 (Pet. ¶ 28).)

Even though the Petition did not seek instruction on the issue, Supreme Court held that, as to overcollateralization trusts, the RMBS trustees should interpret the Overcollateralization Amount so that there will be no Overcollateralization Release Amount distributed through the Excess Cashflow waterfall. (R. 49–50 (Order at 24–25).)

Supreme Court recognized that to calculate the "Overcollateralization Amount," the RMBS trustees were required to subtract the relevant class's Certificate Principal Balance "after taking into account the payment of principal." Supreme Court held, however, that this necessarily means—regardless of whether the trust follows the Write-Up First Method or the Pay First Method—the RMBS trustees should take into account "both a reduction of the balance in the amount of principal to be paid out, and an increase of the balance in the amount of the Subsequent Recovery to be distributed." (R. 49 (Order at 24).) Supreme Court explained that this outcome was appropriate because otherwise there would be a

"diversion of distributions to junior certificate holders," which in Supreme Court's view would contravene the "payment priority structure typical of the Trusts." (R. 50–51 (Order at 25–26).)

STANDARD OF REVIEW

On appeal, this Court should "'examine the contract's language de novo.'" *Dreisinger v. Teglasi*, 130 A.D.3d 524, 527 (1st Dep't 2015) (quoting *Duane Reade, Inc. v. Cardtronics, LP*, 54 A.D.3d 137, 140 (1st Dep't 2008)).

Under New York law, a contract "should as a rule be enforced according to its terms." *W.W.W. Assocs. v. Giancontieri*, 77 N.Y.2d 157, 162 (1990). In analyzing the terms, "courts look to the objective meaning of contractual language," particularly in commercial contracts, as here, "'negotiated at arm's length by sophisticated, counseled businesspeople.'" *In re Bank of N.Y. Mellon*, 56 Misc. 3d 210, 225 (Sup. Ct. N.Y. Cty. 2017) (quoting *Ashwood Capital, Inc. v. OTG Mgt., Inc.*, 99 A.D.3d 1 (1st Dep't 2012)). Words in a contract "must be given their plain and ordinary meaning." *Vigilant Ins. Co. v. Bear Stearns Companies, Inc.*, 10 N.Y.3d 170, 177 (2008) (internal citation and quotation marks omitted); *see also In re Bank of N.Y. Mellon*, 56 Misc. 3d at 225 (finding that the "objective meaning" of RMBS PSA "plain language" controls).

Where sophisticated parties do not address a potential contingency in a contract, New York courts "will not imply a term where the circumstances

surrounding the formation of the contract indicate that the parties, when the contract was made, must have foreseen the contingency at issue and the agreement can be enforced according to its terms." *Reiss v. Fin. Performance Corp.*, 97 N.Y.2d 195, 199 (2001) (discussing *Haines v. City of New York*, 41 N.Y.2d 769 (1977)). "[W]here a contract 'was negotiated between sophisticated, counseled business people negotiating at arm's length,' courts should be especially 'reluctant to interpret an agreement as impliedly stating something which the parties have neglected to specifically include.'" *2138747 Ontario, Inc. v. Samsung C & T Corp.*, 31 N.Y.3d 372, 381 (2018) (quoting *Vermont Teddy Bear Co. v. 538 Madison Realty Co.*, 1 N.Y.3d 470, 472 (2004)).

Further, applying the agreement as written means that "courts may not by construction add or excise terms, nor distort the meaning of those used and thereby make a new contract for the parties under the guise of interpreting the writing.'" *Vermont Teddy Bear Co.*, 1 N.Y.3d at 472 (quoting *Reiss*, 97 N.Y.2d at 199). Thus while courts may carry out the parties' intention by supplying terms "in those limited instances where some absurdity has been identified or the contract would otherwise be unenforceable," a court should not supply terms merely because a contract contains "novel or unconventional" terms, particularly where, as here, "sophisticated, counseled business people" negotiated the contract's terms at arm's length. *Jade Realty LLC v. Citigroup Commercial Mortg. Tr. 2005-EMG*, 83 A.D.3d

567, 568 (1st Dep't 2011) (quoting *Wallace v. 600 Partners Co.*, 86 N.Y.2d 543 (1995)), *aff'd* 20 N.Y.3d 88 (2012).

ARGUMENT

I. SUPREME COURT ERRED BY DIRECTING THE RMBS TRUSTEES TO APPLY THE WRITE-UP FIRST, RATHER THAN PAY FIRST, METHOD TO THE HBK TRUSTS.

Supreme Court erred by holding that the RMBS trustees should apply the Write-Up First Method to the BSABS 2005-AQ2 Trust and, by extension, the HBK Trusts. The HBK Trust PSAs do not address the order of operations for applying Subsequent Recoveries. Consequently, the Settlement Agreement—which indisputably requires that the Pay First Method be applied in such circumstances—governs the order of operations for the HBK Trusts.

A. The HBK Trust PSAs Are Silent on the Order of Operations.

The Settlement Agreement provides that each trust's Allocable Share is to be treated as if it were a Subsequent Recovery of principal. Supreme Court correctly held that: (i) if the governing agreements specify the order of operations for Subsequent Recoveries, the Allocable Share must be distributed in accordance with those terms, but (ii) if a trust's governing agreements do not resolve the order of operations, then its Allocable Share shall be distributed in accordance with the Settlement Agreement's Pay First Method.

The HBK Trust PSAs do not address the order of operations. The definition of "Subsequent Recoveries" is silent as to whether the RMBS trustees should increase Certificate Principal Balances before or after distributing Subsequent Recoveries. (R. 1019 (PSA § 1.01) ("Subsequent Recoveries").)

The Subsequent Recovery Provision, Section 5.04(b), is likewise silent. As Supreme Court itself acknowledged, Section 5.04(b) does not mention, much less resolve, the order of operations. (R. 36–37 (Order at 11–12).) That provision specifies how Subsequent Recoveries are applied to the various classes of certificates by payment priority. Thus, "the Class of Certificates with the highest payment priority to which Realized Losses have been allocated" benefit from Subsequent Recoveries first, and those classes of certificates are written up before other classes of certificates. (R. 3537 (PSA § 5.04(b)).) Then, remaining Subsequent Recoveries are "applied to increase the Certificate Principal Balance of the Class of Certificates with the next highest payment priority . . . and so on." (*Id.*)

The definition of "Certificate Principal Balance" also does not resolve the order of operations. In the HBK Trust PSAs, Certificate Principal Balance means, in relevant part:

> As to any Certificate (other than the Class CE Certificates or any Class R 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 on previous Distribution Dates pursuant to Section 5.04, and (ii) any Applied Realized Loss Amounts allocated to such Certificate on previous Distribution Dates.

(R. 3530 (PSA § 1.01) ("Certificate Principal Balance").)

The Certificate Principal Balance thus operates as a ledger for the trustees. Over time, the RMBS trustees adjust a class's Certificate Principal Balance up (based on the receipt of Subsequent Recoveries pursuant to Section 5.04(b)) or down (based on the distribution of principal or the application of realized losses). This definition does not, however, resolve the timing—meaning whether classes are written up for specific Subsequent Recoveries before or after the payment of principal on the relevant Distribution Date.

Supreme Court erred by holding that this definition resolves the order of operations. The Certificate Principal Balance contains one reference to Subsequent Recoveries: it includes "any Subsequent Recoveries added to the Certificate Principal Balance of such Certificates pursuant to Section 5.04(b)." But, as discussed above, Section 5.04(b) does not address the order of operations. So if amounts are added pursuant to that provision, there is no basis to determine when such amounts are added.

Likewise, the fact that the Certificate Principal Balance definition refers elsewhere to payments of principal made "on previous Distribution Dates" and

losses allocated "on previous Distribution Dates" does not resolve the order of operations for Subsequent Recoveries. Again, the Subsequent Recoveries must be added "pursuant to Section 5.04(b)." And Section 5.04(b) indisputably does not resolve that sequence. The clause "previous Distribution Dates" used for different concepts (prior distributions of principal, prior allocations of losses) cannot breathe meaning into Section 5.04(b). Supreme Court erred by finding that it did.

Indeed, Supreme Court's reasoning demonstrates its flawed interpretation. It found that "[t]he definition of Certificate Principal Balance in these PSAs expressly provides that 'any' Subsequent Recoveries are to be added to the balance." (R. 40 (Order at 15).) That, however, is not what the definition says. It does not say "any Subsequent Recovery *to be* added . . . as of any Distribution Date." The definition says that it includes "any Subsequent Recoveries added to the Certificate Principal Balance of such Certificates pursuant to Section 5.04(b)." The absence of an order of operations in Section 5.04(b) means that Certificate Principal Balance definition is necessarily silent on that issue as well.

Had the parties to the HBK Trust PSAs intended to specify an order of operations for Subsequent Recoveries, they would have stated so explicitly, as some RMBS trust governing agreements do. (R. 38–39 (Order at 13–14) (quoting other PSAs that require "the write-up of the Class Principal Amount will occur 'prior to giving effect to distributions'").) In fact, the HBK Trust PSAs specify an order of

operations for other actions. Under Section 5.05(a), realized losses are applied to write down Certificate Principal Balances "after the actual distributions to be made on such date." (R. 3540 (PSA § 5.05(a)).) The inclusion of an order of operations as to realized losses shows that the parties to the contract "must have foreseen the contingency at issue" (*Reiss*, 97 N.Y.2d at 199)—here, the sequence for applying Subsequent Recoveries—and decided not to address it.

B. Consequently, the Settlement Agreement's Pay First Method Controls.

As Supreme Court held, if the governing agreements do not specify the order of operations, the Settlement Agreement's order of operations governs. (R. 35 (Order at 10).) And the Settlement Agreement mandates that the Pay First Method be applied. (R. 30 (Order at 5).)

Supreme Court's holding—that where a trust's governing agreements are silent on the order of operations, the Settlement Agreement acts as a "gap filler" (R. 53 (Order at 28))—is correct. Under New York law, silence on a contractual term does not create ambiguity. *Reiss*, 97 N.Y.2d at 199; *see also Greenfield v. Philles Records, Inc.*, 98 N.Y.2d 562, 573 (2002) (same). Rather, silence allows a contracting party to elect how to apply a term. *See Trustees of Freeholders & Commonalty of Town of Southampton v. Jessup*, 173 N.Y. 84, 89–91 (1903) (where construction contract did not specify the material to be used, contracting party could

select it); *Schmidt v. Magnetic Head Corp*., 97 A.D.2d 151, 158 (2d Dep't 1983) (where agreement did not contain provision addressing process to select successor for minority director, majority shareholders were free to designate successor); *see also, e.g.*, *Kirschten v. Research Insts of Am., Inc.*, No. 94 Civ. 7947 (DC), 1997 WL 739587, at *9–10 (S.D.N.Y. Sept. 24, 1997) (where contract did not specify sequence for listing authors' names, publisher permitted to select sequence).

II. SUPREME COURT ERRED IN HOLDING THAT THE TRUSTEES MAY "WRITE UP" ZERO BALANCE CLASSES AND DISTRIBUTE FUNDS TO SUCH CLASSES.

Supreme Court also erred in holding that the HBK Trust PSAs permit and, indeed, require the RMBS trustees to write up the Zero Balance Classes upon receipt of Subsequent Recoveries.

Supreme Court's holding erroneously alters an unambiguous commercial contract among "sophisticated, counseled businesspeople" to conform to its own view of the overall objectives and structure of the contracts. *2138747 Ontario, Inc. v. Samsung C & T Corp*., 31 N.Y.3d 372, 381 (2018) (quoting *Vermont Teddy Bear Co. v. 538 Madison Realty Co.*, 1 N.Y.3d 470, 472 (2004)). Supreme Court was instead required to give the contract terms "their plain and ordinary meaning." *Vigilant Ins. Co. v. Bear Stearns Companies, Inc*., 10 N.Y.3d 170, 177 (2008) (internal citation and quotation marks omitted).

A. The Retired Class Provision Prohibits Distributions to Zero Balance Classes.

As discussed above, the HBK Trust PSAs mandate that when certain class Certificate Principal Balances have "been reduced to zero," such classes "will be retired and will no longer be entitled to distributions." (R. 3536 (PSA § 5.04(a)).)[4] Thus, if there is a distribution after such class's Certificate Principal Balance has been reduced to zero, that class is both "retired" and "no longer entitled to distributions."

The Retired Class Provision makes no exceptions. It does not matter how or why such class Certificate Principal Balance has been reduced to zero. The class could be reduced to zero by receiving the full amount of expected principal payments or through the allocation of realized losses. (*See also* R. 382 (Pet. ¶ 55).) Nor does the provision allow the RMBS trustees to reverse the retirement: the restriction

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[4] As set forth above, the Retired Class Provision reads in its entirety:

> In addition, notwithstanding the foregoing, on any Distribution Date after the Distribution Date on which the Certificate Principal Balance of a Class of Class A Certificates or Class M Certificates has been reduced to zero, that Class of Certificates will be retired and will no longer be entitled to distributions, including distributions in respect of Prepayment Interest Shortfalls or Basis Risk Shortfall Carry Forward Amounts.

(R. 3536 (PSA § 5.04(a)); *see also* R. 382 (Pet. ¶ 54).)

applies to such classes of certificates on any Distribution Date after the Certificate Principal Balance "has been reduced to zero."

Despite this clear and unambiguous provision, Supreme Court held that (i) the Certificate Principal Balances of the Zero Balance Classes could be increased; and then (ii) such classes could receive future distributions. Supreme Court thus held that the Retired Class Provision applies only temporarily, while the retired class's Certificate Principal Balance is zero. The decision should be reversed.

First, Supreme Court's interpretation of the clause—that the Zero Balance Classes will not receive distributions until they are written up—improperly fails to give effect to both commands that the certificates "will be retired and will no longer be entitled to distributions." (R. 382 (Pet. ¶ 54); R. 3537 (PSA § 5.04(a))); *see also Natixis Real Estate Capital Tr. 2007-HE2 v. Natixis Real Estate Holdings, L.L.C.*, 149 A.D.3d 127, 134 (1st Dep't 2017) (interpreting RMBS PSA based on the well-established principle that "contract provisions should be harmonized, if reasonably possible, so as not to leave any provision without force and effect . . . .") (internal citation and quotation marks omitted).

The term "retired"—which signifies finality through a permanent reduction of the certificate balance—must be given a meaning apart from "no longer entitled to receive distributions," as the Retired Class Provision imposes both conditions on Zero Balance Classes. *See also Matter of Dex Media, Inc. v. Tax Appeals Trib. of*

the Dep't of Taxation & Fin. of the State of N.Y., 180 A.D.3d 1281, 1283 (3d Dep't 2020) (a contract should be interpreted so that "every word and every provision is to be given effect [and that n]one should needlessly be given an interpretation that causes it to duplicate another provision or to have no consequence" (quoting *Nielsen v. Preap*, 139 S. Ct. 954, 969 (2019)) (alterations in original)).

Thus even if the Subsequent Recovery Provision could apply to a Zero Balance Class, it would still not apply here because a "retired" security is one that no longer has any rights, whether to distributions, write-ups, or anything else. *See, e.g.*, *Zahn v. Transamerica Corp.*, 63 F. Supp. 243, 246 (D. Del. 1945) ("After the retirement of a class of stock, all rights adhering to the shares of that class are in the very nature of things destroyed."), *rev'd on other grounds*, 162 F.2d 36 (3rd Cir. 1947); *Application of Silberkraus*, 250 N.Y. 245 (1929) ("On the retirement of a class of stock, all rights adhering to the shares of that class are destroyed."). Here, as the RMBS trustees recognized in their Petition (R. 382 (Pet. ¶ 55)), the natural reading of a retired class means one that no longer has the right to be written up. Indeed, the Retired Class Provision's command that a Zero Balance Class will continue to be retired on any Distribution Date after the date on which its balance was reduced to zero confirms this. It would be contrary to the meaning of "retired" for such a class to nonetheless be written up.

Second, the Subsequent Recovery Provision does not contain any language purporting to override the retirement provision applicable to Zero Balance Classes. Other PSAs, unlike the HBK Trust PSAs, do include such language. (*See* R. 11016 (write-up provision of JPMAC 20015-FLD1 PSA specifying that "any such Class for which the related Class Principal Amount has been reduced to zero" can be written up); and R. 11020 (retirement provision of RAMP 2005-EFC4 PSA specifying that zero-balance classes "will not be entitled to further distributions pursuant to Section 4.02 (other than in respect of Subsequent Recoveries)").)

Third, the Subsequent Recovery Provision does not permit the write up of Zero Balance Classes in any event. Under Section 5.04(b), write-ups are applied in order of each class's payment priority and in accordance with each certificate's Percentage Interest. The Subsequent Recovery Provision states that it is:

> applied to increase the Certificate Principal Balance of the Class of Certificates with the highest payment priority to which Realized Losses have been allocated . . . any remaining Subsequent Recoveries will be applied to increase the Certificate Principal Balance of the Class of Certificates with the next highest payment priority . . . and so on. . . . . Any such increases shall be applied to the Certificate Principal Balance of each Certificate of such Class in accordance with its respective Percentage Interest.

(R. 3537 (PSA § 5.04(b)).)

Under the HBK Trust PSAs, a Zero Balance Class has neither payment priority nor a percentage interest, which means it is not entitled to write-ups. The

"payment priority" of the certificates is set out in the immediately preceding waterfall section of the PSA, which provides for payments to be made to each class of certificates "in order of priority." (R. 3532–3537 (PSA § 5.04(a)).) Since a Zero Balance Class is no longer entitled to distributions, and may never again be entitled to payments, it cannot be the class with the "highest payment priority." Similarly, a certificate's "Percentage Interest" represents that certificate's share in the distributions owed to the class to which it belongs. (*See, e.g.*, R. 3275 (example definition of Percentage Interest).) Pursuant to the HBK Trust PSA terms, a Zero Balance Class has no interest, in distributions or otherwise, and thus it has no Percentage Interest.

Finally, under the HBK Trust PSAs, even if a Zero Balance Class somehow could be written up and have a Certificate Principal Balance greater than zero, the Retired Class Provision still applies. The Retired Class Provision states that, "notwithstanding" all of the "foregoing" waterfall distribution provisions found in Section 5.04(a), distributions are prohibited after a class's certificate principal balance is reduced to zero. "It is well settled that trumping language such as a 'notwithstanding' provision 'controls over any contrary language' in a contract." *Warberg Opportunistic Trading Fund, L.P. v. GeoResources, Inc.*, 112 A.D.3d 78, 83 (1st Dep't 2013) (internal quotation omitted). This inclusion of the "'notwithstanding' clause clearly signals the drafter's intention that the provision of

the 'notwithstanding' section override conflicting provisions . . . ." *CNH Diversified Opportunities Master Account, L.P. v. Cleveland Unlimited, Inc.*, --- N.Y.3d ---, 2020 NY Slip Op 05976, at *6 (2020) (quoting *Cisneros v. Alpine Ridge Group*, 508 U.S. 10, 18 (1993)). Thus even if a Zero Balance Class could be written up upon the Trust's receipt of Subsequent Recoveries, the "notwithstanding" clause means that those certificates will not be "entitled to distributions" even if they would otherwise be entitled to a payment under the "foregoing" waterfalls.

In short, had the parties to the HBK Trust PSAs intended for a Zero Balance Class to be eligible for write-ups and distributions, the Retired Class Provision would apply only "while the Certificate Principal Balance of a class of certificates is zero," or "after the balance has been reduced to zero, unless it has subsequently been written up." But it did not, and a court may not read limitations into a contract. *See Nomura Home Equity Loan, Inc., Series 2006-FM2 v. Nomura Credit & Capital, Inc.*, 30 N.Y.3d 572, 581 (2017) ("Courts may not, through their interpretation of a contract, add or excise terms or distort the meaning of any particular words or phrases, thereby creating a new contract under the guise of interpreting the parties' own agreements.").

B. The Settlement Agreement's "Purpose" Cannot Supersede the Unambiguous Retired Class Provision.

To the extent Supreme Court purported to interpret the Retired Class Provision to conform the HBK Trust PSAs to what it regarded as "the purpose of the Settlement Agreement," Supreme Court erred.

First, under New York law, the contracts must be enforced as written, regardless of whether the result accords with Supreme Court's expectations of how the securitizations at issue should work. *See Greenfield*, 98 N.Y.2d at 569–570; *see also Caruso v. Ward*, 146 A.D.2d 22, 29–30 (1st Dep't 1989) ("A court should not make or vary a contract to accomplish its notions of abstract justice or moral obligation . . . ."). Indeed, the Settlement Agreement, on its face, explicitly did not alter any of the covered trusts' governing agreements. (R. 414 (Settlement Agreement § 2.06); *see also* R. 53 (Order at 28) (finding that the Settlement Agreement "unequivocally provides" that it does not, and cannot, alter the distribution provisions of the PSAs).)

Supreme Court, too, does not have the authority to rewrite the HBK Trust PSAs in the pursuit of accomplishing its understanding of the Settlement Agreement's abstract goals. Yet Supreme Court's Decision and Order will alter future HBK Trust distributions, as the Zero Balance Classes revived by the Decision

and Order will become entitled to "future principal and interest" payments even after the Allocable Share is distributed. This constitutes error.

Second, in any event, enforcing the Retired Class Provision as written accords with the purposes of the HBK Trust PSAs and the Settlement Agreement. The Retired Class Provision is just one component of a complex agreement among sophisticated, counseled parties allocating many risks, benefits, rights, and obligations. *See 2138747 Ontario, Inc.*, 31 N.Y.3d at 381. To be sure, the Zero Balance Classes may not benefit from the Retired Class Provision. But the Retired Class Provision benefits all other classes. The sophisticated parties agreed upon the terms and the risks set forth by their terms, and the contracts should be enforced as written.

III. SUPREME COURT ERRED BY REFUSING TO GIVE EFFECT TO THE EXCESS CASHFLOW WATERFALL.

Supreme Court also erred by nullifying the Excess Cashflow waterfall with respect to the HBK Trusts' Allocable Shares. (R. 41–42 (Order at 16–17).) As discussed above, the HBK Trusts have an overcollateralization feature whereby if, on any given Distribution Date, the HBK Trusts' assets exceed the Trusts' liabilities by a certain amount, certain funds are released through the "Excess Cashflow" waterfall. Here, for the reasons demonstrated above, the Pay First Method should apply to the HBK Trusts. Supreme Court's ruling addressing the application of the

overcollateralization structure in trusts applying a Pay First Method constituted error. It requires RMBS trustees to take into account the Certificate Principal Balances following payment of principal and write up of Subsequent Recoveries, even though the HBK Trust PSAs specify that only the former and not the latter should be taken into account. This brief also appeals that ruling.

A. Under the HBK Trust PSAs, the Overcollateralization Amount Must Be Determined Based on the Certificate Principal Balance After "Payment of Principal."

Under the HBK Trust PSAs, the Overcollateralization Amount is determined by reference to the Certificate Principal Balance "after taking into account the payment of principal." (*See* R. 5292 (PSA § 1.01).) Notwithstanding this definition, as discussed above, Supreme Court ruled that RMBS trustees for overcollateralization trusts should also take into account the "increase of the balance in the amount of the Subsequent Recovery to be distributed." (R. 49 (Order at 24).)

In a trust applying the Write-Up First Method, Supreme Court's interpretation functionally yields the same result regardless of whether the Overcollateralization Amount is interpreted based on its actual words (as required) or Supreme Court's expanded definition. This is because, in a Write-Up First trust, Subsequent Recoveries would be applied to write up the Certificate Principal Balances before principal is paid. So if an RMBS trustee takes into account the Certificate Principal Balance "after payment of principal," Subsequent Recoveries have necessarily

already been applied to the Certificate Principal Balances. Consequently, as a logical matter, Supreme Court's erroneous interpretation of the Overcollateralization Amount definition does not matter to trusts following the Write-Up First Method.

By contrast, where the Pay First Method governs, Supreme Court's ruling fundamentally alters the HBK Trusts' overcollateralization feature because the RMBS trustees must take into account not only the payment of principal but also "an increase of the balance in the amount of the Subsequent Recovery to be distributed." (R. 49 (Order at 24).) The payment of principal and the write-up for Subsequent Recoveries are, however, distinct steps that occur in a prescribed order. Adding a second step—which the HBK Trust PSAs do not mandate, either explicitly or implicitly—constitutes clear error. *See Nomura*, 30 N.Y.3d at 581 ("A court may not "through . . . [its] interpretation of a contract, add or excise terms . . . .")

A hypothetical demonstrates the way in which Supreme Court's re-writing of the Overcollateralization Amount produces a different outcome than the HBK Trust PSAs require. Let's assume a trust had aggregate mortgage loan balances (collateral) of $100 million, with outstanding Certificate Principal Balances (liabilities) of $100 million and an overcollateralization target of $15 million. As to this trust, the payment of a $20 million Allocable Share (treated as a Subsequent Recovery) would trigger the overcollateralization feature. If the trust's Allocable Share were $20 million, the value of the collateral would remain $100 million, but

the liabilities would be reduced from $100 million to $80 million, given that the Overcollateralization Amount is determined by reference to the Certificate Principal Balance "after taking into account the payment of principal" (here, $20 million). The Overcollateralization Amount would thus be $20 million ($100 million of assets over $80 million of liabilities). The Overcollateralization Release Amount would then be $5 million (the amount by which the $20 million exceeds the $15 million Overcollateralization Target Amount), which would be distributed under the Excess Cashflow waterfall. (R. 373 (Pet. ¶ 29).)

By contrast, if the Overcollateralization Amount were determined by the Certificate Principal Balances "after taking into account payment of principal and an increase of the balance in the amount of the Subsequent Recovery," then the Overcollateralization Amount in the hypothetical above would be eliminated and reduced to zero. The $100 million Certificate Principal Balance would remain the same: it would be reduced by taking into account the "payment of principal" (subtracting $20 million) and increased by "the amount of the subsequent recovery" (adding $20 million). This outcome erroneously nullifies the HBK Trust PSAs' unambiguous overcollateralization provisions.

B. New York Law Does Not Authorize Supreme Court to Add Words to an Unambiguous Contractual Term.

Supreme Court tried to justify its decision to eliminate the Excess Cashflow distributions based on equitable principles. Here, Supreme Court reached this decision to prevent "diversion of distributions to junior certificate holders," which Supreme Court believed would contravene the "payment priority structure typical of the Trusts." (R. 51 (Order at 26).) Essentially, Supreme Court sought to scuttle what it believed was an unintended consequence of temporary overcollateralization caused by the settlement as opposed to "real" overcollateralization, meaning that resulting from the trusts' overall sound performance.

But it does not matter if Supreme Court believed its rationale to be equitable and just, it still contravenes New York law. The HBK Trust PSA overcollateralization provisions are unambiguous. And New York courts cannot rewrite unambiguous contractual terms negotiated by sophisticated parties to protect some abstract objective identified by the courts—here, what Supreme Court perceived as the appropriate order of priority among certificateholders in a hypothetical typical trust.

These are contracts among sophisticated parties that unambiguously specify how distributions must be made, and such contracts must be enforced under New York law. If the plain language of the HBK Trust PSAs results in Excess Cashflow

distributions, that is the intent of the agreement, not a "diversion." The court must look to "the objective meaning of contractual language," negotiated at arm's length by sophisticated, counseled entities, regardless of whether such terms match up to a "general subordination scheme." *Bank of N.Y. Mellon*, 56 Misc. 3d 210, 222, 225 (holding that "the general intent of the governing agreements to protect senior certificateholders over junior certificateholders" could not control over specific contractual language that required a different result).

In any event, Supreme Court's assumptions as to the appropriate relationship between typical "junior" and "senior" classes were incorrect. As to the HBK Trusts, "junior" classes are sometimes paid before the "senior" classes under the PSAs' detailed distribution scheme. For instance, if a "Stepdown Date" is reached, "junior" classes may (and routinely do) receive substantial payments before "senior" classes are paid in full. (*See* R. 3532-3535 (PSA § 5.04(a)(2)(A) and (B)).) The "Excess Cashflow" waterfalls likewise often make payments to "junior" classes while "senior" classes are still outstanding. (R. 3535-3537 (PSA § 5.04(a)(3)).)[5] Supreme Court's assumption that "senior" classes must always receive distributions before

[5] Nor do the overcollateralization provisions always benefit "junior" over "senior" certificateholders. The Excess Cashflow waterfall under Section 5.04(a)(3) respects each class's position in the payment waterfall by making payments to senior classes that have suffered realized losses in the same order in which losses were allocated, along with accumulated interest shortfalls.

"junior" classes disregards the intricate contractual structure governing the HBK Trusts.

CONCLUSION

For the reasons set forth above, U.S. Bank, solely in its capacity as Indenture Trustee for certain NIM Trusts holding direct interests in the HBK Trusts and solely at the direction of HBK, respectfully requests that this Court reverse Supreme Court's decision as it relates to the HBK Trusts and direct the RMBS trustees: (i) to apply the Pay First Method to each HBK Trust's Allocable Share; (ii) to enforce the Retired Class Provision by its plain terms and not increase, or "write up," Zero Balance Classes upon the HBK Trust's receipt of Subsequent Recoveries; and (iii) to give effect to the overcollateralization provisions and, where an HBK Trust's Allocable Share results in Overcollateralization Release Amounts, distribute excess cashflow as directed by the HBK Trust PSAs.

Dated: New York, New York
November 2, 2020

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STATEMENT PURSUANT TO CPLR § 5531

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, 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 Distribution of a Settlement Payment.

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1. The index number of the case in the court below is 657387/17.

2. The full names of the original Petitioners are as set forth above. There have been no changes.

3. The action was commenced in Supreme Court, New York County.

4. The action was commenced on December 15, 2017 by filing of a Petition. Respondents D.E. Shaw Refraction Portfolios, L.L.C, HBK Master Fund L.P., Olifant Fund, Ltd., FFI Fund Ltd., FYI Ltd., Ellington Management Group L.L.C., Prophet Mortgage Opportunities LP, Poetic Holdings VI LLC and Poetic Holdings VII LLC, FT SOF IV Holdings, LLC, Fir Tree Capital Opportunity Master Fund, L.P., Fir Tree Capital Opportunity Master Find III, L.P., Tilden Park, AEGON USA Investment Management, LLC, BlackRock Financial Management, Inc., Cascade Investment, LLC, the Federal Loan Bank of Atlanta, the Federal Home Loan Mortgage Corporation (Freddie Mac), the Federal Mortgage Association (Fannie Mae), Goldman Sachs Asset Management L.P., Voya Investment Management LLC, Invesco Advisers, Inc., Kore Advisors, L.P., Metropolitan Life Insurance Company, Pacific Investment Management Company LLC, Teachers Insurance and Annuity Association of America, the TCW Group, Inc., Thrivent Financial for Lutherans, Western Asset Management Company, 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, The Variable Annuity Life Insurance Company, GMO Opportunistic Income Fund, GMO Global Real Return (UCITS) Fund, Axonic Capital LLC, Nover Ventures, LLC, Strategos Capital Management, LLC filed their Responses to Petition on January 29, 2018.

5. This is an Article 77 Proceeding.

6. This appeal is from the Decision and Order of the Honorable Marcy S. Friedman, dated February 13, 2020, which held, as relevant to this appeal, that (1) the settlement payment write-up should be made using the subsequent recovery write-up instructions in the associated pooling and servicing agreements ("PSAs"), unless the relevant PSA is silent as to the write-up mechanics, in which case the Settlement Agreement write-up instruction should be applied as a "gap filler"; (2) the Petitioners should not write up the certificate principal balances of senior certificates in connection with the settlement payment in trusts where the PSA write-up instructions only indicate a write-up of subordinated certificates; and (3) with respect to calculating the overcollateralization amount as to certain "Pay First" trusts, Petitioners should take into account both a reduction of the certificate principal balance and an increase of the certificate principal balance prior to making any distribution.

7. This appeal is on the full reproduced record.