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

In the matter of the application of U.S. BANK NATIONAL ASSOCIATION and U.S. BANK TRUST COMPANY, NATIONAL ASSOCIATION (each separately as Trustee, Securities Administrator, Paying Agent, and/or Calculation Agent, as applicable, under various Pooling and Servicing Agreements), Petitioners, for judicial instructions pursuant to CPLR Art. 77.	Index No. 656028/2021 Motion Seq. No. 15 **Hon. Andrew Borrok** **(IAS Part 53)**

RESPONDENTS OLIFANT FUNDS, RELIANCE PARTIES, AND TACONIC FUNDS MEMORANDUM OF LAW IN OPPOSITION TO PIMCO AND HBK'S MOTION FOR A STAY OR ADJOURNMENT IN THE ALTERNATIVE

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Pursuant to the Order to Show Cause entered on November 6, 2023, respondents Olifant Fund, Ltd., FFI Fund Ltd., FYI Ltd. (collectively the "Olifant Funds"), Reliance Standard Life Insurance Company, Safety National Casualty Corporation, Stephen Finkelstein, NAV LLC (collectively, the "Reliance Parties"), Taconic Master Fund 1.5 LP, Taconic Opportunity Master Fund LP, and Park Royal II LLC (collectively, the "Taconic Funds," and together with the Olifant Funds and the Reliance Parties, the "ORT Respondents") hereby oppose the motion for a stay, or adjournment in the alternative, filed by respondents Pacific Investment Management Company LLC ("PIMCO") and HBK Master Fund L.P. ("HBK"). Doc. No. 341; Mot. Seq. No. 15 (hereafter, the "Motion").

As the Motion explains, there is only partial overlap between the *Wells Fargo* case[1] and this proceeding filed by U.S. Bank National Association and U.S. Bank Trust Company, National Association (collectively, "U.S. Bank" or the "Trustee"). This proceeding seeks judicial instruction on two distinct issues: (1) the treatment of Post-Zero Balance Collections; and (2) the treatment of Deferred Principal Collections. *See* Second Am. Pet. (hereafter, "Petition") ¶ 2, Doc. No. 290.[2] The second of these questions is almost identical to the issue presented in *Wells Fargo*, while the first is completely different. As explained below, a stay would only delay resolution of the first issue for no good reason and would perpetuate, not avoid, inconsistency as to the second issue.

[1] *In re Wells Fargo Bank, National Association*, Index No. 154984/2021 (Sup. Ct. N.Y. Cnty.).

[2] Capitalized terms, unless otherwise defined, will have the definitions specified in the Second Amended Petition or applicable governing documents. The exhibits attached to the Ricardo Affirmation filed herewith are cited as Ex. __.

ARGUMENT

1. Post-Zero Balance Collections

This proceeding should not be stayed because there is a distinct issue raised by the Petition—the treatment of Post-Zero Balance Collections—that was not decided in *Wells Fargo* and that would not be resolved by any appeal in *Wells Fargo*. Determining the proper treatment of Post-Zero Balance Collections requires (1) addressing the effect of the Retired Class Provision and, assuming the Retired Class Provision imposes no obstacle, (2) crafting a solution to a problem that is not squarely addressed by the governing agreements. Because the *Wells Fargo* appeal will not address either of these issues, there is no justification to stay this proceeding pending the *Wells Fargo* appeal.

To start, it is important to recognize the difference between Deferred Principal Collections, which are at issue in *Wells Fargo* (where they are called Deferred Principal Proceeds), and Post-Zero Balance Collections, which are not. As this Court has recognized in a dispute over an RMBS clean-up call, Deferred Principal Collections are essentially *balloon payments of principal* that was previously deferred. *See* Transcript of Proceedings at 31, 35, *Deer Park Road Mgmt. Co. LP v. Nationstar Mortg. LLC*, Index No. 654474/2022 (Sup. Ct. N.Y. Cnty. Sept. 6, 2023) (Doc. No. 76). Post-Zero Balance Collections, on the other hand, are *payments of any kind* that arrive after the balances of the Primary Classes are reduced to zero. *See* Petition ¶ 10. If Deferred Principal Collections happen to arrive after the Primary Classes have zero balances, those payments are *both* Deferred Principal Collections and Post-Zero Balance Collections. But that overlapping area is far from the entire universe of Post-Zero Balance Collections. Ordinary course collections of principal and interest (*i.e.*, any collections *other than* deferred principal) that arrive after the Primary Classes have zero balances are Post-Zero Balance Collections, *but are not Deferred Principal Collections*.

The Subject Trusts have received and will continue to receive these ordinary course collections, which constitute Post-Zero Balance Collections, but are not Deferred Principal Collections. SACO 2006-4 provides a concrete example of this. As of April 2022, the Primary Classes had zero balances and there was $3 million in collateral generating Post-Zero Balance Collections. Ex. 1 at pp. 1, 4.[3] This potential universe of Post-Zero Balance Collections, roughly $3 million, far exceeded the amount of deferred principal at that time, approximately $138,819. Ex. 2. By then, the Trustee had already escrowed over $374,000 in Post-Zero Balance Collections while it awaits decision in this matter. Ex. 1 at p. 3. Those escrowed amounts will only grow as the collateral balance becomes additional Post-Zero Balance Collections over time. In fact, as of the most recent reporting period, the Trustee had already escrowed over $1.4 million in Post-Zero Balance Collections for SACO 2006-4. Ex. 3 at p. 3.

The Petition admits that one of the reasons why the Trustee is not applying Post-Zero Balance Collections to write up and make distributions to zero-balance Primary Classes is U.S. Bank's view that the Retired Class Provision prohibits such write-ups and distributions. This is the case despite the fact that the First Department's decision in *In re Wells Fargo Bank, Nat'l Ass'n*, 198 A.D.3d 156 (1st Dep't 2021), denying reargument, 38 N.Y.3d 1179 (N.Y. 2022) (referred to in the Motion as "*JPM II*") decided precisely the opposite as to these same PSAs. The Petition expressly acknowledges that U.S. Bank's present approach *disregards the First Department's decision in JPM II* as to the Retired Class Provision:

> For routine distributions for the Subject Trusts, Petitioners' general practice is to apply the Retired Class Provision to prevent both distributions *and* write-ups to zero-balance Primary Classes. This general practice differs from the JPM II Appellate Opinion and JPM II Trial Court Order, though appears to be consistent with the

[3] The ORT Respondents reference April 2022 because the Trustee produced in discovery data about deferred principal as of that month. Ex. 2.

> position of the aforementioned party seeking further review of the JPM II Appellate Opinion (and certain other parties in JPM II).

Petition ¶ 113 (footnote and citation omitted). Thus, the Trustee is not writing up and paying distributions to zero-balance Primary Classes, in part, because it continues to construe the Retired Class Provision as prohibiting such write-ups and distributions, even though the First Department squarely held that "zero-balance certificates are eligible for write-ups and distributions." *JPM II*, 198 A.D.3d at 163. U.S. Bank should be ordered to comply with *JPM II* forthwith.

In explaining its decision to disregard *JPM II*, U.S. Bank cites a September 2021 motion for leave to appeal *JPM II* to the Court of Appeals, but that motion was denied on November 16, 2021.[4] Petition ¶¶ 25, 112-13. A stay of this proceeding would allow U.S. Bank to continue to disregard the First Department's decision as to the Retired Class Provision for at least another two years. While the Motion suggests that this connection between Post-Zero Balance Collections and *JPM II* weighs in favor of a stay (*see* Motion at 3-4), the Motion has it entirely backwards. A stay would only allow U.S. Bank to continue its incorrect approach for at least another two years.

While an order directing U.S. Bank to comply with *JPM II* would remove *one obstacle* to write-ups of and distributions to zero-balance Primary Classes (U.S. Bank's improper application of the Retired Class Provision), that alone would not resolve the treatment of Post-Zero Balance Collections because another obstacle would remain. The Petition explains that the PSAs do not

[4] Subsequent motions to appeal filed in the Court of Appeals were "denied on the grounds that the order sought to be appealed from did not finally determine the proceeding." Petition ¶ 25. The current Motion refers to a Proposed Final Judgment in the JPM proceeding filed on October 27, 2023 (Motion at 3), but when and whether HBK can reach the Court of Appeals, presumably after another unsuccessful First Department appeal, is speculative. *JMP II* is binding now.

include a mechanism for writing up Primary Classes with funds that do not qualify as Subsequent Recoveries. Petition ¶ 93 ("Post-Zero Balance Collections . . . do not appear to qualify as Subsequent Recoveries"). Without a viable mechanic to write up zero-balance Primary Classes (such as a write-up analogous to that caused by Subsequent Recoveries), ordinary course Post-Zero Balance Collections cannot be paid to zero-balance Primary Classes under the principal or interest waterfall. Nor can any Post-Zero Balance Collections be paid through the Excess Cashflow waterfall because these funds do not meet the definition of Excess Cashflow.[5] Without a decision by the Court, Post-Zero Balance Collections will remain trapped in the Subject Trusts indefinitely. As noted above, this is not an academic issue. Certain Subject Trusts are already generating Post-Zero Balance Collections and these amounts could potentially exceed $173 million. *Id.* ¶¶ 84-85. It is therefore critical to resolve this issue, instead of deferring that resolution for at least another two years, so that these Post-Zero Balance Collections can be distributed to their rightful recipients.

Because the treatment of Post-Zero Balance Collections is an entirely different issue that was not decided in *Wells Fargo*, was not fully resolved by *JPM II*, and will not be resolved by the *Wells Fargo* appeal, the ORT Respondents wish to present evidence on that question to explain why the most appropriate solution is to treat Post-Zero Balance Collections the same way as Subsequent Recoveries. We estimate this would take two trial days and would include limited factual testimony from the Trustee and an expert retained by the ORT Respondents. If a merits hearing occurs, we understand that HBK would offer a fact witness and an expert witness of its own.

[5] As the Petition explains, there can only be Excess Cashflow if the Overcollateralization Target Amount is exceeded, which it is not for any of the Subject Trusts. Petition ¶ 95.

Finally, the Motion's reference to Post-Zero Balance Collections and Deferred Principal Collections being "intertwined" overstates the point the Petition was making on this front. As to ordinary course Post-Zero Balance Collections (*i.e.*, those that are not also Deferred Principal Collections), the only connection is that the resolution of the Deferred Principal Collections issue may affect the *quantum* of Post-Zero Balance Collections for any given Subject Trust. Because U.S. Bank has not been writing up certificate balances when Deferred Principal Collections arrive, this failure has improperly reduced Primary Class balances, contributing to their reduction to zero in some cases. *See* Id. ¶ 9. At that point, all proceeds from the securitized mortgage loans are Post-Zero Balance Collections. This tendency of the Trustee's treatment of Deferred Principal Collections to increase the amount of Post-Zero Balance Collections is the connection the Petition was referring to. *See* Id. ¶¶ 2, 121. But this *economic connection*, whereby the Trustee's improper treatment of Deferred Principal Collections has exacerbated a different problem, does not mean that the two *legal issues* before the Court are intertwined. They are not. Simply put, a decision on the proper treatment of Deferred Principal Collections will not decide how Post-Zero Balance Collections should be handled.

2. Deferred Principal Collections

Turning to the question that *is* common to both actions (the treatment of Deferred Principal Collections, or Deferred Principal Proceeds as they are called in *Wells Fargo*), the ORT Respondents are ***NOT*** asking the Court to hold a trial on the merits of this question. As the Motion contends, that would be a waste of judicial resources because this Court has already decided the same issue in *Wells Fargo*. More specifically, this Court has already decided that

Deferred Principal Collections are Subsequent Recoveries as a matter of law. *See* Motion at 2. Thus, nothing stands in the way of this Court making the same determination in this case *now*.[6]

While the Motion claims that a stay would avoid inconsistent outcomes, the opposite is true. This Court has instructed one RMBS trustee, Wells Fargo, to treat Deferred Principal Collections as Subsequent Recoveries, but the RMBS trustee seeking instruction here, U.S. Bank, is doing the opposite, *i.e.*, it is *not* treating Deferred Principal Collections as Subsequent Recoveries. *See* Petition ¶ 17 ("Petitioners do not treat Deferred Principal Collections as Subsequent Recoveries"). The best way to avoid inconsistent outcomes would be for the Court to enter an order now directing U.S. Bank to treat Deferred Principal Collections as Subsequent Recoveries, just like Wells Fargo is doing. This can be done with the stroke of a pen without a trial, and it makes more sense than staying this proceeding, which would allow U.S. Bank to continue acting contrary to this Court's ruling in *Wells Fargo* for at least another two years. A stay would not avoid a conflict with the ruling in *Wells Fargo*. To the contrary, deciding the appropriate treatment of Deferred Principal Collections promptly is necessary to end the existing conflict between U.S. Bank's current practice and this Court's ruling in *Wells Fargo*.

The Motion also argues that a stay is needed to avoid a conflict with a *potential future decision* by the First Department reversing this Court's ruling in *Wells Fargo*. *See* Motion at 5. This supposed conflict is entirely hypothetical and might never occur. One could advance this same argument to seek a stay of the *Wells Fargo* ruling itself pending appeal, but we are not

[6] The ORT Respondents (other than the Taconic Funds, which have taken no position on the treatment of Deferred Principal Collections in this proceeding) agree that Deferred Principal Collections should be treated like Subsequent Recoveries, although they have advanced a different rationale for doing so than that adopted by the Court. *See* Doc. Nos. 178; 268. The trusts at issue in this proceeding do not include the language found in *Wells Fargo* to limit write-ups to subordinate certificates, so senior certificates can be written-up here.

aware of anyone seeking such a stay in the *Wells Fargo* matter. Additionally, if the Court enters a stay and declines to decide the proper treatment of Deferred Principal Collections here, the only parties who will be heard on this question in the First Department are the parties to *Wells Fargo*. Several of the ORT Respondents and the Petitioners here are not parties to *Wells Fargo*.[7] These parties, who will plainly be affected by an appellate decision in *Wells Fargo*, should have the opportunity to be heard on this common issue in the First Department. A stay would effectively freeze these parties out of participating in an appeal.

CONCLUSION

For the foregoing reasons, this Court should deny PIMCO and HBK's motion for a stay, or adjournment in the alternative.

Dated: November 20, 2023

By: */s/ Henry J. Ricardo*

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[7] Reliance Standard Life Insurance Company, Safety National Casualty Corporation, and NAV LLC are parties to *Wells Fargo*. *See Wells Fargo*, Doc. Nos. 142, 220.

CERTIFICATION OF COMPLIANCE

This memorandum complies with the word count limit of Commercial Division Rule 17 because it contains 2393 words, excluding the parts of the brief exempted by Rule 17. This word count was prepared based on the Microsoft Word count function.

Dated: November 20, 2023
New York, New York

By: /s/ *Henry J. Ricardo*

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