

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

In the Matter of the Application of

U.S. BANK NATIONAL ASSOCIATION (as
Trustee, Securities Administrator, Paying Agent,
and/or Calculation Agent under various Pooling
and Servicing Agreements),

Petitioner,

for judicial instructions under CPLR Article 77.

Index No. 656028/2021

IAS Part 53

Hon. Andrew Borrok, J.S.C.

**ANSWER OF TILDEN PARK
INVESTMENT MASTER FUND
LP**

Tilden Park Investment Master Fund LP (“Tilden Park”), for its Answer to the First Amended Petition (the “Petition”) of U.S. Bank National Association, solely in its capacity as trustee, securities administrator, paying agent, and/or calculating agent of certain RMBS trusts (the “Trustee”), Dkt. 33 (“Pet.”),¹ states as follows:

1. Tilden Park holds certificates in the BSABS 2005-HE2, BSABS 2006-AQ1, BSABS 2006-HE6, and BSABS 2007-AQ1 trusts (the “Tilden Park Trusts”).

2. In the Petition, the Trustee asks for instructions on two questions: (1) whether and how to increase Certificate Principal Balances based on Deferred Principal Collections; and (2) whether and how to distribute funds to, or increase the Certificate Principal Balances of, Primary Classes whose principal balances have reached zero. Pet. ¶2.

3. Tilden Park respectfully requests that, for the Tilden Park Trusts, the Court instruct the Trustee that: (1) it should apply Deferred Principal Collections to reverse its previous applications of Realized Losses to Primary Classes, and thus to increase those Classes’ Certificate

¹ Capitalized terms not defined here have the meaning ascribed in the Petition. See Dkt. 33.

Principal Balances; and (2) Retired Class Provisions do not bar the Trustee from increasing the Certificate Principal Balances of Primary Classes with balances of zero, including when it receives Deferred Principal Collections.

4. Tilden Park will appear at any hearing in this matter and reserves the right to submit further argument and evidence in merits briefing.

I. The Trustee Should Write Up Primary Classes When the Tilden Park Trusts Receive Deferred Principal Collections

5. The question of whether to write up RMBS certificate balances when borrowers make deferred principal payments only exists because U.S. government regulations forced the trusts' parties to change how they treat principal deferments. That change has caused certificate balances to incur artificial "losses," some of which deferred principal payments have now reversed.

6. The basic purpose of RMBS certificate balances is to govern how much trust capital a given class of certificates has a right to receive. In a typical RMBS trust, the certificate balance of a class of certificates depends on, among other factors, the payments that class has already received and the assets remaining in the trust to make future payments. If certificates receive payments or the trust suffers losses, the trustee typically decreases certificate balances (that is, "writes them down"). By contrast, if past losses are reversed, the trustee typically increases certificate balances (that is, "writes them up").

7. To carry out that purpose, RMBS governing agreements typically instruct trustees to decrease certificate balances when the trust incurs defined "Realized Losses" and to increase certificate balances when "Realized Losses" are reversed. The most common scenario where a RMBS trust incurs "Realized Losses" is when the servicer liquidates the trust's mortgage loans at a loss. The most common scenario where "Realized Losses" are reversed is when the trust receives a recovery on a previously liquidated loan.

8. The Tilden Park Trusts' governing agreements follow this approach. Section 5.05 of each agreement directs the Trustee to apply the sum of the loans' Realized Losses – defined as the “Applied Realized Loss Amount” – to reduce the certificates' “Certificate Principal Balance.” *See, e.g.*, Affirmation of Justin M. Ellis dated January 18, 2022 (“Ellis Aff.”) Ex. B, BSABS 2006-HE6 PSA § 5.05; *see also id.* § 1.01 (defining “Applied Realized Loss Amount”). Consistent with the basic principle of securitization that more junior certificates should bear losses before more senior certificates, Section 5.05 directs the Trustee to apply the Applied Realized Loss Amount to write down certificate balances in reverse order of seniority (*i.e.*, from the most junior certificates to the most senior ones). *See, e.g., id.* § 5.05.

9. The Tilden Park Trusts' governing agreements also contemplate that the Trustee might receive “Subsequent Recoveries” that reverse losses. “Subsequent Recoveries” occur if the master servicer receives funds “specifically related to a Mortgage Loan that was the subject of a liquidation or final disposition of any REO property . . . that resulted in a Realized Loss.” *See, e.g.*, Ellis Aff. Ex. B, BSABS 2006-HE6 PSA § 1.01. If the master servicer receives Subsequent Recoveries which reduce the amount of a Realized Loss, the Tilden Park Trusts' governing agreements instruct the Trustee to increase the certificate balances of the “Class of Certificates with the highest payment priority to which Realized Losses have been allocated.” *See id.* § 5.04(b). In other words, when Subsequent Recoveries come in, the Trustee must write up certificates in order of payment seniority (*i.e.*, from most senior to most junior). *Id.*

10. As the Petition explains, however, Deferred Principal Collections are not “Subsequent Recoveries” for two reasons. First, any loan for which a borrower makes a deferred principal payment, by definition, has not previously been the “subject of a liquidation or final disposition of a REO property,” because that loan is active and making payments. *See* Pet. ¶80.

11. Second, for the Tilden Park Trusts, the mortgage modifications that deferred principal payments do not create Realized Losses. *See* Pet. ¶¶ 77-78. Those trusts' governing agreements limit "Realized Losses" to amounts "with respect to each Mortgage Loan" or "each REO Property" that is subject to a "Final Recovery Determination," a "Deficient Valuation," a "Debt Service Reduction," or – for two of the Tilden Park Trusts – certain "Servicing Modification[s]." Ellis Aff. Ex. A, BSABS 2005-HE2 PSA § 1.01; *id.* Ex. B, BSABS 2006-HE6 PSA § 1.01; *id.* Ex. C, BSABS 2006-AQ1 PSA § 1.01; *id.* Ex. D, BSABS 2007-AQ1 PSA § 1.01. Principal deferments for active loans do not fit into any of those categories and thus are not "Realized Losses."

12. Specifically, a "Final Recovery Determination" happens only for liquidated loans, not active loans.² "Deficient Valuations" and "Debt Service Reductions" both refer only to orders by a bankruptcy court which reduce a borrower's obligations.³ For two Tilden Park Trusts, "Realized Losses" are limited to loans with "Final Recovery Determinations," "Deficient Valuations," and "Debt Service Reductions," and thus cannot include principal deferments. Ellis Aff. Ex. A, BSABS 2005-HE2 PSA § 1.01; *id.* Ex. B, BSABS 2006-HE6 PSA § 1.01.

13. While two other Tilden Park Trusts also define "Realized Losses" to include mortgage loans with "Servicing Modifications," principal deferments in those trusts still do not qualify

² *See, e.g.*, Ellis Aff. Ex. B, BSABS 2006-HE6 PSA § 1.01 (a "Final Recovery Determination" is, "with respect to any defaulted Mortgage Loan or any REO Property," a determination by the master servicer that no further funds will be recovered for that loan).

³ *See, e.g.*, Ellis Aff. Ex. B, BSABS 2006-HE6 PSA § 1.01 (a "Deficient Valuation" is a "valuation by a court of competent jurisdiction of the Mortgaged Property in an amount less than the then outstanding indebtedness under such Mortgage Loan, or any reduction in the amount of principal to be paid in connection with any Scheduled Payment that results in a permanent forgiveness of principal, which valuation or reduction results from an order of such court that is final and non-appealable in a proceeding under the Bankruptcy Code"); *id.* (a "Debt Service Reduction" is "a reduction by a court of competent jurisdiction in a proceeding under the Bankruptcy Code in the Scheduled Payment for such Mortgage Loan").

as “Realized Losses.” For those trusts, “Servicing Modifications” only include loan modifications that are “effected by the Master Servicer in accordance with the terms of [the governing] Agreement.” Ellis Aff. Ex. C, BSABS 2006-AQ1 PSA § 1.01; *id.* Ex. D, BSABS 2007-AQ1 PSA § 1.01. Principal deferments are not made “in accordance with the terms” of these governing agreements, because they were performed as required by HAMP, and not pursuant to any terms in the governing agreements. Indeed, neither of the relevant governing agreements empower the master servicer to perform such deferments. *Cf.* Ellis Aff. Ex. C, BSABS 2006-AQ1 PSA §§ 3.01, 3.09 (describing servicers’ powers); *id.* Ex. D, BSABS 2007-AQ1 PSA §§ 3.01, 3.09 (same).⁴

14. Moreover, for those trusts, “Realized Losses” only exist for loans with “Servicing Modifications” if “the interest portion of a monthly payment or the principal balance of such Mortgage Loan was reduced” or “any other amounts owing under the Mortgage Loan were forgiven.” Ellis Aff. Ex. C, BSABS 2006-AQ1 PSA § 1.01; *id.* Ex. D, BSABS 2007-AQ1 PSA § 1.01. Deferring the date when a principal payment is due does not “reduce” or “forgive” any principal. As a result, the deferred principal could not itself be a “Realized Loss.” Rather, the only “Realized Loss” that could result if a principal deferment were a “Servicing Modification” (and it is not) is the marginal reduction in a borrower’s monthly interest payments. However, remittance reports show that the Trustee has not actually treated such marginal reductions as “Realized Losses” in these trusts.

15. Deferred principal payments to the Tilden Park Trusts are not “Subsequent

⁴ Section 3.01 of each governing agreement also directs the master servicer to service the trusts’ loans “in accordance with customary and usual standards of practice of prudent mortgage loan servicers.” Ellis Aff. Ex. C, BSABS 2006-AQ1 PSA § 3.01; *id.* Ex. D, BSABS 2007-AQ1 PSA § 3.01. While the Trustee observes that federal statute deems HAMP modifications to be “standard industry practice,” Pet. ¶ 74 (citing 15 U.S.C. § 1639a(c)), those modifications are still not made “in accordance with the terms of” the governing agreements and thus do not qualify as “Servicing Modifications.”

Recoveries” that reverse Realized Losses because the trusts’ parties never intended to account for principal deferments as losses in the first place. Those trusts’ governing agreements do not treat principal deferments – which are temporary by their nature – as Realized Losses. Rather, as the Petition explains, servicers treat principal deferments as Realized Losses only because the U.S. Department of the Treasury directed them to do so as part of the HAMP program implemented after the 2007-2008 financial crisis. Pet. ¶¶ 73-74. Because principal deferments are only artificial “Realized Losses” imposed by HAMP (henceforth, “Regulatory Realized Losses”), the write-up rules for “Subsequent Recoveries” do not address what to do when borrowers reverse these “losses” by paying deferred principal.

16. While the “losses” caused by principal deferments are artificial, the impact of these Regulatory Realized Losses on certificate balances is quite real. When borrowers pay deferred principal, however, those “losses” are reversed for all practical purposes. Accordingly, consistent with the structure of the Tilden Park Trusts’ governing agreements, when the Trustee receives Deferred Principal Collections, it should reverse its previous allocation of Regulatory Realized Losses which decreased certificate balances or, in other words, increase Certificate Principal Balances accordingly.

17. Specifically, because HAMP regulations require the Trustee to treat Regulatory Realized Losses as Realized Losses, and because Deferred Principal Collections reverse the “losses” Regulatory Realized Losses cause, the way to treat Deferred Principal Collections that best fits the Tilden Park Trusts’ governing agreements is to perform Section 5.05’s loss-allocation process in reverse to undo the “losses” caused by Regulatory Realized Losses. In other words, when the Trustee receives deferred principal payments, it should increase Certificate Principal Balances in reverse order of previously allocated losses. While Deferred Principal Collections are not

Subsequent Recoveries, and thus not subject to the write-up process for Subsequent Recoveries, writing up certificate balances based on those funds recognizes that, when the Trustee receives them, it should no longer account for the artificial Regulatory Realized Losses that the Deferred Principal Collections have reversed.

18. Two other textual features of the Tilden Park Trusts' governing agreements confirm that the Trustees should follow this approach. First, the definition of Applied Realized Loss Amount in each Tilden Park Trust is negative – and thus requires increasing certificate balances – when Deferred Principal Collections are taken into account. Each trust's governing agreement defines the Applied Realized Loss Amount as “the sum of the Realized Losses with respect to the Mortgage Loans which have been applied in reduction of the Certificate Principal Balance of a Class of Certificates pursuant to Section 5.05 of this Agreement which have not previously been reimbursed or reduced by any Subsequent Recoveries applied to such Applied Realized Loss Amount.” *See, e.g.*, Ellis Aff. Ex. B, BSABS 2006-HE6 PSA § 1.01.

19. Because of HAMP regulations, the Trustee has included Regulatory Realized Losses as Realized Losses when computing the Applied Realized Loss Amount used to adjust certificate balances. But because Deferred Principal Collections reverse whatever “loss” occurred from Regulatory Realized Losses, those collections may effectively render Realized Losses negative for the affected loans in the month they are received.⁵ Thus, if Deferred Principal Collections make the sum of Realized Losses negative for a given distribution date, the Applied Realized Loss Amount will also be negative, and applying that amount will increase certificate balances.

⁵ Regulatory Realized Losses are not “Realized Losses” under the governing agreements and, accordingly, a Regulatory Realized Loss may be a negative amount regardless of how “Realized Losses” are defined in a particular governing agreement.

20. Second, each of the Tilden Park Trusts' governing agreements has a "Loss Allocation Limitation" that underscores how reversing Regulatory Realized Losses is necessary to carry out the parties' intent. "Loss Allocation Limitations" require that allocations of Realized Losses not increase a Tilden Park Trust's overcollateralization. *See, e.g.*, Ellis Aff. Ex. B, BSABS 2006-HE6 PSA § 5.05(b) (no loss allocations "shall be made on a Distribution Date to any Class of Certificates to the extent that such allocation would result in the reduction of the aggregate Certificate Principal Balance of all the related Certificates" to "less than the aggregate Stated Principal Balance of all of the related Mortgage Loans"). As the Trustee explains, however, failing to write up certificate balances based on deferred principal will make these trusts artificially appear more overcollateralized, because the trusts' certificate balances will continue to reflect artificial "losses" from Regulatory Realized Losses without accounting for funds that reverse those "losses." Pet. ¶¶ 126-131.

21. Finally, failing to write up certificate principal balances in the Tilden Park Trusts based on Deferred Principal Collections would be commercially unreasonable and absurd. When Deferred Principal Collections are received upon the final payoff of a loan (as they typically are), such a loan would be treated as if it has not been fully repaid. In that way, such a result would extend Treasury regulations to override the Tilden Park Trusts' governing agreements far beyond either those regulations' text or their intended scope. That result would needlessly punish Primary Classes by imposing on them artificial Regulatory Realized Losses they were never meant to incur, only to have the deferred principal that should reverse such losses instead go to Class C certificates. *See* Pet. ¶ 131. Such pointless redistribution from senior to junior classes would violate the fundamental principle of securitization that junior classes should bear losses before senior ones.

22. Tilden Park thus respectfully requests that when the Trustee receives Deferred

Principal Collections in the Tilden Park Trusts going forward,⁶ it should write up the Certificate Principal Balances of the Primary Classes in reverse order of previously allocated losses.

II. The Retired Class Provisions Should Not Affect the Trustee's Treatment of Deferred Principal Collections

23. The “Retired Class Provisions” in the Tilden Park Trusts’ governing agreements do not affect the proper treatment of Deferred Principal Collections. As the Petition acknowledges, the First Department recently held that, despite such clauses, “zero-balance certificates are eligible for write-ups and distributions.” *Wells Fargo Bank v. Aegon USA Inv. Mgmt., LLC*, 198 A.D.3d 156, 163 (1st Dep’t 2021); see Pet. ¶112. That holding controls the second question on which the Trustee seeks judicial instruction. While certain parties have sought permission to appeal to the Court of Appeals from that decision, Pet. ¶113, the decision in *Wells Fargo* remains binding precedent unless overturned.

24. In *Wells Fargo*, the First Department explained that the definitions of Certificate Principal Balance at issue in those trusts provided that “all certificates are eligible” to have their balances increased. 198 A.D.3d at 163. By contrast, Retired Class Provisions “relate solely to distributions and nowhere state that zero-balance certificates are ineligible to be written up.” *Id.*⁷ Such provisions merely state that once the Trustee has taken certain formal steps to “retire” certificates with zero balances and withdraw them from circulation, those certificates are no longer eligible to receive distributions they might otherwise receive. *Id.* Because the certificates at issue

⁶ Tilden Park does not request that the Court order the reversal or unwinding of any prior write-ups for the Tilden Park Trusts. Tilden Park also does not oppose the Trustee’s request that the Court find that its historical treatment of deferred or forborne amounts was a good faith application of the Tilden Park Trusts’ governing agreements. See Pet. ¶152(c).

⁷ While the First Department’s opinion concerned write-ups on account of Subsequent Recoveries, nothing in its reasoning suggested that whether zero-balance certificates could be written up turned on whether the reason for those write-ups would be Subsequent Recoveries or another reason.

had not been formally withdrawn, they were eligible for write-ups. *Id.*

25. *Wells Fargo* directly applies to the Retired Class Provisions in the Tilden Park Trusts. Just like the trusts at issue in *Wells Fargo*, the definition of Certificate Principal Balance in the Tilden Park Trusts' governing agreements provides that recoveries should increase the balance of any Class A and Class M certificates without regard to whether they have a zero balance. *See, e.g.*, Ellis Aff. Ex. B, BSABS 2006-HE6 PSA § 1.01. Just like the Retired Class Provisions at issue in *Wells Fargo*, the Retired Class Provisions in the Tilden Park Trusts concern only certificates that have been formally "retired" and say nothing about whether (or how) trustees should increase certificate balances. *See, e.g., id.* § 5.04(b). And just as in *Wells Fargo*, the Trustees have never formally withdrawn certificates in the Tilden Park Trusts with zero balances. *Wells Fargo* is therefore on point and requires that the Trustee not use the Retired Class Provisions to bar increases in the Certificate Principal Balances of certificates with current balances of zero. Thus, while the Trustee has formerly interpreted the "Retired Class Provision to prohibit write-ups to zero-balance Primary Classes," Pet. ¶ 116, *Wells Fargo* requires a different treatment moving forward.⁸

REQUEST FOR RELIEF

Tilden Park respectfully requests that the Court enter judgment:

- a. Instructing the Trustee to allocate Deferred Principal Collections for the Tilden Park Trusts either currently held in escrow or received after the date of the Trustee's original Petition to increase the Certificate Principal Balances of the Primary Classes in reverse

⁸ As with the treatment of Deferred Principal Collections, Tilden Park neither asks that past application of any Retired Class Provisions in the Tilden Park Trusts be reversed nor opposes the Trustee's requested instruction that its prior practice was undertaken in good faith.

- order of previously allocated losses pursuant to Section 5.05 of each Tilden Park Trust governing agreement;
- b. Instructing the Trustee to follow the procedure described above whether or not any Primary Class has a Certificate Principal Balance of zero; and
 - c. Granting Tilden Park such other relief as may be just and proper.

January 18, 2022
New York, New York

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CERTIFICATE OF SERVICE

I hereby certify that, on January 18, 2022, I caused the foregoing Answer of Tilden Park Investment Master Fund LP to be served on all counsel of record by filing it with the Court's NYSCEF system.

/s/ Justin M. Ellis _____