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To be Argued by:
DIANA M. CONNER
(Time Requested: 15 Minutes)

New York Supreme Court

Appellate Division—First Department

Appellate Case No.: 2020-02716

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)

BRIEF FOR RESPONDENTS OLIFANT FUNDS

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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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PRELIMINARY STATEMENT[1]

The IAS Court resolved several complex contractual issues relevant to the Petitioners' distribution of the $4.5 billion settlement payment from JPMorgan Chase & Co. and its affiliates ("JPMorgan") to the certificateholders of hundreds of residential mortgage-backed securities ("RMBS") trusts (the "Settlement Trusts") that have suffered substantial losses. Olifant Fund, Ltd., FFI Fund Ltd., and FYI Ltd. (the "Olifant Funds") appeared in this CPLR Article 77 proceeding as interested certificateholders and prevailed on all relevant issues before the IAS Court.

Despite the IAS Court's thorough and well-reasoned opinion, HBK[2] appeals a plethora of rulings concerning the proper interpretation of the Settlement Trusts' governing agreements ("Governing Agreements"), which are generally styled as pooling and servicing agreements ("PSAs"). As relevant to the Olifant Funds, HBK argues that the IAS Court erred in holding (1) that certificates whose balances have been written down to zero (also known as "zero-balance certificates") are eligible to receive write-ups and distributions relating to the

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[1] Capitalized terms not defined herein have the meanings given to them in HBK's opening brief.

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

settlement payment, and (2) that the Write-Up First "order of operations" applies to the group of trusts that the court dubbed the "Write-Up First Trusts," including the trusts in which HBK and the Olifant Funds hold interests.[3] The Prophet and Poetic Parties[4] join in HBK's arguments with respect to the first issue.

As the IAS Court recognized, HBK's arguments disregard the plain language of the relevant trusts' PSAs. First, the PSAs expressly permit *all* certificates to be written up on account of "Subsequent Recoveries," including zero-balance certificates. Because the Settlement Agreement requires the Settlement Trusts' allocable shares of the settlement payment ("Allocable Shares") to be treated as Subsequent Recoveries under the PSAs, zero-balance certificates are eligible to receive write-ups and distributions relating to those funds. Indeed, it would be illogical to allow certificates whose balances have been written down to nominal amounts to potentially receive millions of dollars in compensation from

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[3] The remaining trusts in which the Olifant Funds hold certificates are BSABS 2006-IM1 and SACO 2005-WM3 (the "Olifant Trusts"). While the trusts in which HBK holds an interest (the "HBK Trusts") do not overlap with the Olifant Trusts, they were both the subject of the IAS Court's rulings concerning (1) the eligibility of zero-balance certificates to receive write-ups and distributions relating to the settlement payment, and (2) the proper "order of operations" for the Write-Up First Trusts. (R.36; R.41; R.60-64.) Thus, the Olifant Funds respond to HBK's arguments in order to demonstrate why the IAS Court's rulings should be affirmed.

[4] Prophet Mortgage Opportunities Fund LLP ("Prophet") and Poetic Holdings VI LLC and Poetic Holdings VII LLC (together, "Poetic") hold both direct and indirect interests in certain Settlement Trusts. U.S. Bank substituted for Prophet and Poetic as a party in this proceeding with respect to certain trusts in which they hold indirect interests and is acting in its capacity as Indenture Trustee for certain NIM Trusts at their direction. U.S. Bank has separate counsel in its role as NIM Trustee. The Olifant Funds refer to these parties jointly as the "Prophet and Poetic Parties."

the settlement payment, but to prohibit certificates whose balances have been written down to zero due to losses from receiving *any* portion of the settlement payment. Such a fundamentally unfair result is not required by the trusts' PSAs.

Contrary to HBK's arguments, the so-called "Retired Class Provision" does not compel a different result; it merely states that certificates that have been paid in full and formally withdrawn from circulation are no longer entitled to distributions under the trusts' distribution "waterfalls." Because the certificates at issue have not been paid off or formally retired, the Retired Class Provision is irrelevant.

Second, the IAS Court correctly found that the PSAs for the Write-Up First Trusts require Petitioners to use the Write-Up First Method in distributing the trusts' Allocable Shares. As the court explained, the PSAs' definition of "Certificate Principal Balance" contains an inherent order of operations: it requires that all Subsequent Recoveries received by the trusts must be added to increase the certificate balances *before* any distributions are paid out to certificateholders. Accordingly, the IAS Court's rulings should be affirmed.

COUNTERSTATEMENT OF QUESTIONS PRESENTED

1. Where the relevant contracts expressly permit all RMBS certificates to be written up on account of Subsequent Recoveries, without exception, may certificates whose balances have been reduced to zero receive write-ups and distributions relating to Subsequent Recoveries?

Answer of the IAS Court: The IAS Court correctly answered "yes."

2. Where the relevant contracts contain a definition of "Certificate Principal Balance" that requires all Subsequent Recoveries to be added to the certificate balance prior to any distribution of those funds, is the Write-Up First order of operations required?

Answer of the IAS Court: The IAS Court correctly answered "yes."

BACKGROUND

A. The Settlement Agreement

As explained in the Appellants' opening briefs, the Settlement Agreement provides that the Settlement Trusts' Allocable Shares of the $4.5 billion settlement payment must be treated as "Subsequent Recoveries" under each trust's Governing Agreement. (R.418 (Settlement Agreement Section 3.06(a)).) In general terms, Subsequent Recoveries function as reversals of Realized Losses that were previously allocated to a class of certificates. In the ordinary course, the trusts might receive Subsequent Recoveries through additional collections on mortgage loans that previously experienced losses. In the Settlement Agreement, the parties agreed that the extraordinary, one-time settlement payment from JPMorgan would be treated as a Subsequent Recovery and distributed in accordance with the requirements of each Settlement Trust's PSA.

B. The Article 77 Proceeding

After the Settlement Agreement was approved by the New York Supreme Court in August 2016,[5] the Petitioners initiated this Article 77 proceeding seeking judicial instruction concerning the proper method by which to distribute certain Settlement Trusts' Allocable Shares. As relevant here, two key issues were disputed: (i) with respect to the Settlement Trusts identified on Exhibit G to the Petition (the "Exhibit G Trusts"), whether the "Retired Class Provision" precludes zero-balance certificates from receiving write-ups and distributions relating to the settlement payment, and (ii) with respect to the Write-Up First Trusts, whether the Write-Up First or the Pay First "order of operations" was appropriate.

C. The Relevant PSA Provisions

Under the relevant PSAs, funds collected by the trusts in the normal course are distributed pursuant to Section 5.04(a)'s "waterfall"—i.e., the distribution provision which provides a specific order of payment priority for each class of certificates, with the "senior" classes having higher payment priorities than the more "junior" classes. (R.3532-3536.) Before distributing funds to holders on any given distribution date, the Trustee must calculate the Certificate Principal Balance of each class of certificates. The Certificate Principal Balance represents the maximum amount of principal distributions that a particular class may receive on

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[5] *See Matter of U.S. Bank N.A. v. Federal Home Loan Bank of Boston*, No. 652382/2014, 2016 WL 9110399 (Sup. Ct., N.Y. Cty., Aug. 12, 2016).

any given distribution date. Each class of certificates is assigned an Initial Certificate Principal Balance, and that balance is reduced over time due to either (a) the class's receipt of distributions of principal or (b) the allocation of Realized Losses to that class. (R.3530.) The junior classes of certificates are generally allocated Realized Losses before any such losses are allocated to the senior classes.

In the event that the trusts receive Subsequent Recoveries (like the Allocable Shares at issue here), the PSAs permit all certificates to have their balances written up on account of such funds to reverse Realized Losses previously allocated to those classes. Specifically, the PSAs define the "Certificate Principal Balance" of "any Certificate" as follows:

> As to *any Certificate* . . . and as of any Distribution Date, the Initial Certificate Principal Balance of such Certificate plus, in the case of a Class A Certificate and Class M Certificate, *any Subsequent Recoveries added to the Certificate Principal Balance of such Certificate pursuant to Section 5.04(b)*, less the sum of (i) all amounts distributed with respect to such Certificate in reduction of the Certificate Principal Balance thereof 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 (emphasis added).) This definition does not contain any limitation relating to classes of certificates whose balances have been reduced to zero.

PSA Section 5.04(b) then provides that write-ups relating to Subsequent Recoveries will be allocated in the following manner: "Subsequent Recoveries will

be applied to increase the Certificate Principal Balance of *the Class of Certificates with the highest payment priority to which Realized Losses have been allocated*, but not by more than the amount of Realized Losses previously allocated to that Class of Certificates . . . ." (R.3537 (emphasis added).) Like the definition of Certificate Principal Balance, this provision contains no limitation concerning zero-balance certificates.

At the end of Section 5.04(a)'s distribution waterfall is a one-sentence provision which HBK refers to as the "Retired Class Provision." This provision states that "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." (R.3536 (emphasis added).) Section 10.02, which is titled "Final Distribution on the Certificates,"[6] later explains that certificate "retirement" is a formal, multi-step process that is initiated by the Trustee when the certificate has been paid in full. (SR.2.)[7] At the end of the retirement process, holders must "surrender" their certificates to the Trustee, thereby withdrawing the certificates from circulation altogether. (*Id.*)

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[6] The provision concerning the "Final Distribution on the Certificates" is located in PSA Section 10.02 for the exemplar trust (BSABS 2005-AQ2) and one of the Olifant Trusts (SACO 2005-WM3). (SR.2-3; SR.7-8.) This provision is located in PSA Section 11.02 for the other Olifant Trust (BSABS 2006-IM1). (SR.5.)

[7] Cites to "SR" are to the Supplemental Record on Appeal, which is being filed along with this brief.

D. The IAS Court's Decision

On February 13, 2020, the IAS Court issued a lengthy ruling addressing all the issues raised in the Petition. (R.25-71.) With respect to the Exhibit G Trusts, the court rejected the argument put forth by HBK and others that the Retired Class Provision prohibits zero-balance certificates from receiving write-ups and distributions relating to the settlement payment. The IAS Court reasoned that the PSAs' "write-up provisions do not limit the classes that may be written up on account of subsequent recoveries"; rather, they "provide for the balances of *all* classes of certificates to be written up by subsequent recoveries, although only to the extent of realized losses previously allocated to a class." (R.63 (emphasis added).) Accordingly, the court held that zero-balance certificates may be written up on account of the Allocable Shares and, as a natural consequence, may subsequently receive distributions of those and other funds. (R.63-64.)

In addition, the IAS Court held that the PSAs for the Write-Up First Trusts require the Write-Up First order of operations. (R.36-41.) The court reasoned that the PSAs' definition of Certificate Principal Balance describes a calculation with a particular sequencing of the write-up and distribution steps: it requires the trusts' certificate balances to be written up to account for the Allocable Shares *before* any distributions of those funds are made to certificateholders.

HBK appealed the IAS Court's ruling with respect to both of these issues, and the Prophet and Poetic Parties appealed the court's ruling with respect to zero-balance certificates.

STANDARD OF REVIEW

The questions presented are legal issues subject to *de novo* review by this Court. *See In re Part 60 RMBS Put-Back Litig.*, 155 A.D.3d 482, 483 (1st Dep't 2017); *Gulf Ins. Co. v. Transatlantic Reins. Co.*, 13 A.D.3d 278, 279 (1st Dep't 2004) ("a de novo standard of review applies because the IAS court interpreted a contract provision . . . as a matter of law") (citation omitted).

ARGUMENT

I. THE IAS COURT CORRECTLY HELD THAT ZERO-BALANCE CERTIFICATES ARE ELIGIBLE FOR WRITE-UPS AND DISTRIBUTIONS

The IAS Court correctly held that the PSAs for the Exhibit G Trusts permit zero-balance certificates to receive write-ups and distributions relating to the settlement payment. As the IAS Court explained, nowhere in the PSAs does it state that zero-balance certificates are ineligible to be written up on account of Subsequent Recoveries. (R.62-63.) Rather, the PSAs expressly "provide for the balances of *all* classes of certificates to be written up by subsequent recoveries, although only to the extent of realized losses previously allocated to a class." (R.63 (emphasis added).) This ruling should be affirmed.

A. The PSAs Expressly Permit All Classes of Certificates to Be Written Up on Account of Subsequent Recoveries

As the IAS Court recognized, the PSAs' definition of "Certificate Principal Balance" is integral to the certificate write-up process. (R.36-41.) The Certificate Principal Balance of each class must be calculated before the Trustee can make any distributions to holders. For the relevant trusts, the definition of Certificate Principal Balance provides that all certificates are eligible to be written up on account of Subsequent Recoveries, without exception. This definition states that "[a]s to *any Certificate* . . . and as of any Distribution Date," the Certificate Principal Balance includes "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) . . . ." (R.3530 (emphasis added).) This provision does not exclude zero-balance certificates from receiving write-ups relating to Subsequent Recoveries; rather, it provides that "*any* Certificate" may receive such write-ups pursuant to Section 5.04(b). (*Id.* (emphasis added).)

PSA Section 5.04(b), in turn, specifies how write-ups relating to Subsequent Recoveries will be allocated among the certificate classes. As the IAS Court stressed, this provision likewise permits the write-up of zero-balance classes:

> If, after taking into account such Subsequent Recoveries, the amount of a Realized Loss is reduced, the amount of such Subsequent Recoveries will be applied to *increase*

> *the Certificate Principal Balance of the Class of Certificates with the highest payment priority to which Realized Losses have been allocated*, but not by more than the amount of Realized Losses previously allocated to that Class of Certificates pursuant to Section 5.05; provided, however, to the extent that no reductions to a Certificate Principal Balance of any Class of Certificates currently exists as a result of a prior allocation of a Realized Loss, such Subsequent Recoveries will be applied as Excess Spread. The amount of any remaining Subsequent Recoveries will be applied to *increase the Certificate Principal Balance of the Class of Certificates with the next highest payment priority*, up to the amount of such Realized Losses previously allocated to that Class of Certificates pursuant to Section 5.05, and so on.

(R.63 (citing PSA Section 5.04(b)) (emphasis added).) In other words, Section 5.04(b) requires Subsequent Recoveries to be applied in the order of the certificates' payment priorities under the Section 5.04(a) distribution waterfall.[8] It only limits the permissible write-ups to the "amount of Realized Losses previously allocated to that Class of Certificates." (*Id.*)

This limitation makes sense because Subsequent Recoveries like the Allocable Shares at issue here are intended to function as "reversals" of prior Realized Losses on the certificates. Because many zero-balance certificates have experienced substantial losses that have not been repaid, those certificates are entitled to be written up in accordance with their payment priorities, per Section

[8] Indeed, HBK acknowledges that Section 5.04(b) "specifies how Subsequent Recoveries are applied to the various classes of certificates *by payment priority*." (HBK Br. at 23 (emphasis added).)

5.04(b). Indeed, it would be absurd to allow a certificate whose balance has been reduced to $1 to have its losses reversed—and to potentially receive significant sums from the settlement payment—but to *prohibit* a certificate whose balance has been reduced to $0 from receiving any recovery. Such a reading of the contract would be commercially unreasonable and therefore untenable. *See Cole v. Macklowe*, 99 A.D.3d 595, 595 (1st Dep't 2012) ("[A] contract should not be interpreted to produce an absurd result, one that is commercially unreasonable, or one that is contrary to the intent of the parties.").

HBK's argument would lead to another absurd result: significant portions of the settlement payment might go to the holders of "residual" certificates, which are equity-like certificates that have lower payment priorities than the zero-balance certificates at issue here. Given that the residual certificateholders did not suffer any of the losses that the settlement payment was intended to compensate, it would be perverse to allow those holders to receive the trusts' Allocable Shares, while leaving the holders of zero-balance certificates without *any* compensation for their losses. Such a result would be inconsistent with both the structure of the transactions and Section 5.04(b), in particular.

B. The Retired Class Provision Does Not Compel a Different Result

Despite the provisions discussed above, HBK contends that the so-called "Retired Class Provision" located at the end of Section 5.04(a)'s waterfall prohibits

zero-balance certificates from being written up on account of Subsequent Recoveries because it states that "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." (HBK Br. at 14, 28.) HBK misinterprets this provision, which relates solely to distributions and says nothing about the write-up of zero-balance certificates. As explained above, such write-ups are plainly permissible under the PSA. (R.63-64.) In any event, the Retired Class Provision merely states the unremarkable proposition that once a certificate has been paid in full and formally "retired," it is no longer entitled to receive the distributions that it might have otherwise received under the waterfall. Because the certificates at issue have neither been paid in full nor subsequently retired, that provision is entirely irrelevant to the issues before the Court.

The significance of Section 5.04(a)'s reference to "retired" certificates is made clear when that passage is read in conjunction with Section 10.02—the only other reference to "retired" certificates in the PSA. As noted above, Section 10.02 is titled "Final Distribution on the Certificates" and provides a detailed procedure for formally retiring and withdrawing from circulation any certificates that have been paid in full. (SR.2.) It states:

> If on any Determination Date, (i) the Master Servicer determines that there are no Outstanding Mortgage Loans

> and no other funds or assets in the Trust Fund other than the funds in the Protected Account, the Master Servicer shall direct the Trustee to send a final distribution notice promptly to each Certificateholder or (ii) the Trustee determines that a Class of Certificates *shall be retired after a final distribution on such Class*, the Trustee shall notify the Certificateholders within five (5) Business Days after such Determination Date that *the final distribution in retirement of such Class of Certificates* is scheduled to be made on the immediately following Distribution Date. Any final distribution made pursuant to the immediately preceding sentence will be made only upon presentation and surrender of the related Certificates at the Corporate Trust Office of the Trustee.

(*Id.* (emphasis added).) Thus, pursuant to Section 10.02, the "retirement" of a class of certificates requires several steps: (1) a determination by the Trustee that retirement is appropriate, (2) notice to certificateholders, (3) a final distribution to the class, and (4) presentation and surrender of the certificates at the Trustee's offices.

The meaning of "retired" set forth in Section 10.02 is consistent with the plain meaning of that term when used in reference to bonds, *see* BLACK'S LAW DICTIONARY (11th ed. 2019) (defining "retire" as "[t]o pay in full; settle . . . <to retire the debt>" and "[t]o withdraw from the market or from circulation"); WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 1939 (unabr. 2002) (defining "retire" as "to withdraw from circulation or from the market : take up or pay :

RECALL, REDEEM"),[9] as well the use of that term by New York courts, *see, e.g.*, *Application of Erie R.R. Co.*, 260 A.D. 268, 270 (3d Dep't 1940) (stating that bonds were "retired" when the issuer "pa[id] its notes in full" and "[t]he noteholders returned to the [issuer] the series A and series B bonds"), *aff'd*, 284 N.Y. 673 (1940). It is also consistent with the Internal Revenue Service's definition of the word "retired" in its guidance concerning bonds issued by real estate mortgage investment conduits ("REMICs"), like those at issue here. *See* IRS Tax Map 2018, https://taxmap.irs.gov/taxmap2018/pubs/p550-009.htm (last visited December 1, 2020) ("A debt instrument is *retired* when it is reacquired or redeemed by the issuer and canceled.") (emphasis added).

Accordingly, when the PSA is read as a whole—as it must be[10]—it is clear that certificates only become "retired" once they have been fully repaid and formally withdrawn pursuant to Section 10.02. The Retired Class Provision merely clarifies at the end of Section 5.04(a)'s distribution waterfall that, notwithstanding that waterfall, certificates that have been fully paid "will be

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[9] *See also* BALLENTINE'S LAW DICTIONARY (3rd ed. 2010) (defining "retire" as "[t]o take up or pay an obligation voluntarily" and "[t]o withdraw negotiable paper from circulation"); CAMBRIDGE BUSINESS ENGLISH DICTIONARY (2020), https://dictionary.cambridge.org/us/dictionary/english/retire (last visited December 2, 2020) (defining "retire" as "to pay back a debt or loan completely: The funds were used to retire debt and to finance expansion."); AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE 1488 (4th ed. 2000) (defining "retire" as "[t]o take out of circulation: retired the bonds"); BARRON'S DICTIONARY OF FINANCE AND INVESTMENT TERMS 607 (8th ed. 2010) (defining "retirement" as "repayment of a debt obligation" and "cancellation of stock or bonds that have been reacquired or redeemed").

[10] *See Dreisinger v. Teglasi*, 130 A.D.3d 524, 528 (1st Dep't 2015).

retired" pursuant to Section 10.02 and "will no longer be entitled to distributions" thereafter (R.3536)—as one would expect after a certificate has been surrendered and taken out of circulation. It is undisputed that the zero-balance certificates at issue here have neither been fully repaid nor withdrawn from the market pursuant to Section 10.02; rather, they have significant outstanding losses and are still actively traded. Indeed, those certificates would not be the subject of this Article 77 proceeding had they been retired. Thus, the Retired Class Provision does not apply.

HBK ignores the detailed description of certificate "retirement" provided in Section 10.02 and, instead, reads the Retired Class Provision in isolation. HBK claims that this provision states that certificates are *automatically* retired when their balances are reduced to zero for any reason, including due to allocation of Realized Losses. (HBK Br.[11] at 28-35.) HBK's myopic reading of the PSA violates fundamental principles of contract interpretation. Contracts must be "read as a whole" and "every part will be interpreted with respect to the whole." *Richard Feiner & Co. Inc. v. Paramount Pictures Corp.*, 95 A.D.3d 232, 233 (1st Dep't 2012). Accordingly, the Retired Class Provision must be construed in light of Section 10.02, which makes clear that certificates are only considered "retired" once the Trustee has taken several affirmative steps to accomplish that end—

[11] "HBK Br." refers to HBK's opening brief, which was filed with this Court on November 2, 2020.

including paying off the certificates and withdrawing them from circulation. (SR.2.) The mere reduction of the certificate balances to zero is insufficient.

HBK's interpretation of the PSA is flawed for the additional reason that it would render Section 10.02 entirely meaningless. *See Corhill Corp. v. S.D. Plants, Inc.*, 9 N.Y.2d 595, 599 (1961). Under HBK's reading, Section 10.02's formal procedure for retiring paid-off certificates would be completely unnecessary because such certificates would *already* be deemed "retired" under the Retired Class Provision, even without such formalities. As HBK itself stresses, "contract provisions should be harmonized, if reasonably possible, so as not to leave any provision without force and effect . . . ." (HBK Br. at 29 (quoting *Natixis Real Estate Capital Trust 2007-HE2 v. Natixis Real Estate Holdings, L.L.C.*, 149 A.D.3d 127, 134 (1st Dep't 2017)).) The only way to harmonize the Retired Class Provision with Section 10.02 is to recognize that certificate "retirement" does not occur until the Trustee has taken the steps described in Section 10.02—which can only be taken in connection with a "final distribution" in repayment of the certificate, not upon allocation of Realized Losses. (SR.2.) It is only *after* the Section 10.02 retirement process is complete that the Retired Class Provision applies; that provision then prohibits the retired class from receiving any further distributions under the waterfall. Unlike HBK's interpretation, this reading of the contract gives meaning to both the Retired Class Provision and Section 10.02.

Because the zero-balance certificates at issue have neither been paid off nor formally retired, the Retired Class Provision does not apply.

HBK further argues that zero-balance certificates are not entitled to any write-ups under Section 5.04(b) because such certificates do not have "payment priorities," as is required to receive Subsequent Recoveries under that section. (HBK Br. at 31-32.) HBK reasons that "[s]ince 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.'" (*Id.* at 32.) HBK makes this argument *despite* the certificate payment priorities that are clearly delineated in Section 5.04(a)'s distribution waterfall. HBK's argument is entirely circular; it rests on the faulty premise that HBK's interpretation of the Retired Class Provision is correct and, therefore, that zero-balance certificates are not entitled to write-ups or distributions. However, as explained above, HBK's interpretation of that provision is incorrect. In reality, zero-balance certificates maintain the payment priorities set forth in Section 5.04(a)'s waterfall and are entitled to be written up in accordance with those priorities pursuant to Section 5.04(b). Nothing in the Retired Class Provision purports to override the certificates' payment priorities.[12]

[12] HBK similarly argues that zero-balance certificates have no "Percentage Interest" within the meaning of Section 5.04(b) because they are no longer entitled to receive write-ups or distributions. (HBK Br. at 31-32.) This argument is likewise circular and based on HBK's flawed assumption that its interpretation of the Retired Class Provision is correct.

Finally, HBK argues that the IAS Court "rewrote" the PSAs at issue in order to accomplish the Settlement Agreement's "abstract goals." (HBK Br. at 34.) But the court did no such thing. It merely observed that "[t]he write-up provisions of the Trusts are consistent with the purpose of the Settlement Agreement, as they permit write-ups of the zero balance certificates to the extent of previously allocated realized losses." (R.64.) In other words, both the PSAs and the Settlement Agreement contemplate that zero-balance certificates with outstanding losses may receive Subsequent Recoveries in order to compensate holders for those prior losses. The plain terms of the IAS Court's ruling make clear that the court did not *disregard* the PSAs' text in favor of the Settlement Agreement; rather, it properly interpreted the "write-up provisions" set forth in the PSAs. (*Id.*)

This Court should affirm the IAS Court's ruling that the PSAs unambiguously permit zero-balance certificates to receive write-ups and distributions relating to the settlement payment.

C. If the Court Finds the PSAs to Be Ambiguous, It Should Remand for Consideration of Extrinsic Evidence

To the extent the Court finds that the PSAs are ambiguous as to whether they permit zero-balance certificates to receive write-ups and distributions relating to the Allocable Shares, it should remand this case for consideration of extrinsic evidence by the IAS Court in the first instance. *See Gessin Elec. Contrs., Inc. v. 95 Wall Assoc., LLC*, 74 A.D.3d 516, 518 (1st Dep't 2010). In particular, the IAS

Court would need to consider evidence concerning the parties' course of performance, which this Court has recognized is the "most persuasive evidence of the agreed intention of the parties." *Gulf Ins. Co. v. Transatlantic Reins. Co.*, 69 A.D.3d 71, 85 (1st Dep't 2009) (citation omitted).

In practice, the Petitioner Trustees and Securities Administrators have not interpreted the PSAs to require the formal retirement of certificates whose balances have been written down to zero due to the allocation of Realized Losses. Rather, those certificates have remained in circulation and have been actively traded. (*E.g.*, R.4888.) The parties' course of performance demonstrates that they did not contemplate that certificates would be "retired" merely because their balances had been written down to zero; they understood that certificates should only be retired once they have been paid in full, as provided in Section 10.02. Thus, the evidence concerning the parties' course of performance supports the Olifant Funds' interpretation of the PSAs. At the very least, the PSAs do not unambiguously favor HBK's reading.

II. THE IAS COURT CORRECTLY HELD THAT THE RELEVANT PSAs REQUIRE THE WRITE-UP FIRST METHOD

The IAS Court also correctly held that the Write-Up First order of operations applies to the Write-Up First Trusts, including the Olifant Trusts. As explained more fully in the responsive brief filed by Ambac Assurance Corporation ("Ambac"), the definition of Certificate Principal Balance set forth in the Write-Up

First Trusts' PSAs contains an inherent order of operations that requires the certificate balances to be written up on account of the Allocable Shares *prior* to any distribution of those funds. In order to avoid duplicative briefing, the Olifant Funds respectfully refer the Court to Ambac's briefing on this issue.

CONCLUSION

For the reasons stated above, this Court should affirm the IAS Court's rulings (1) that zero-balance certificates are entitled to receive write-ups and distributions relating to the settlement payment, and (2) that the PSAs for the Write-Up First Trusts require use of the Write-Up First Method.

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Respectfully submitted,

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