

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

In the matter of the application of

THE BANK OF NEW YORK MELLON, in its  
Capacity as Trustee or Indenture Trustee of 530  
Countrywide Residential Mortgage-Backed  
Securitization Trusts,

Petitioner,

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

Index No. 150973/2016

IAS Part 39

**ANSWER OF FEDERAL HOME LOAN MORTGAGE CORPORATION  
TO THE VERIFIED PETITION**

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Dated: New York, New York  
March 4, 2016

The Federal Home Loan Mortgage Corporation (“Freddie Mac”) submits the following Answer, as a holder of Certificates issued by certain Covered Trusts and pursuant to the Order to Show Cause entered by the Court on February 8, 2016, in response to the Verified Petition (“Petition”) filed by The Bank of New York Mellon in its capacity as trustee of those trusts (“Trustee”).

#### PRELIMINARY STATEMENT

The Court should instruct the Trustee to distribute the settlement proceeds in a manner that will prevent “leakage.” This result is expressly mandated by the Governing Agreements. The proposed calculation described in subparagraph (i)(a) of the Trustee’s Prayer for Relief would achieve the correct result (although it would not technically be an “adjustment” but simply the calculation method called for by the Governing Agreements). Each governing Pooling and Servicing Agreement (PSA)<sup>1</sup> requires the Trustee to apply the complete accounting effect of the distribution when it calculates overcollateralization. When overcollateralization is calculated as required, the PSAs’ waterfall provisions will cause the settlement proceeds to flow sequentially in order of priority to the senior classes (and will not permit them to “leak” to other holders under different distribution provisions applicable to Excess Cashflow<sup>2</sup>). There is no reason of law or contract why calculation of trust overcollateralization or distribution of settlement proceeds should vary from how the governing PSAs require them to be performed.

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<sup>1</sup> Although Freddie Mac believes that the position stated in this Answer applies generally to overcollateralization trusts that are part of the settlement, the references to PSAs are to the PSAs in the 21 overcollateralization trusts in which Freddie Mac holds certificates, which are listed in the Appendix hereto. Those 21 trusts constitute 12% of the 175 overcollateralization trusts at issue. Copies of two representative PSAs (for the CWABS 2006-3 and CWALT 2006-OA10 trusts) are submitted herewith for the Court’s convenience; copies of PSAs for all the Covered Trusts were previously submitted to the Court via compact disc when the Petition was filed. (Petn. at 2 n.1.)

<sup>2</sup> All capitalized terms not defined herein are defined in the Petition or the applicable PSAs.

The Petition primarily concerns trusts with an overcollateralization (OC) structure. The purpose of overcollateralization is to provide a cushion of protection in the form of extra assets. The issue here turns on whether, for any affected trust, the OC Target — basically, a specified excess of aggregate loan balance over aggregate certificate balance — is met or exceeded as of the relevant Distribution Date. If the trust is below the OC Target on the relevant date — which is the case here for every affected trust — distributions are required to be made within each loan group sequentially and in order of priority to senior classes (and thereafter sequentially to junior classes). *Only* if the trust is at or above OC Target on the relevant distribution date are collections *not* required to be distributed sequentially and in order of priority to the senior classes.<sup>3</sup>

The 21 trusts at issue in which Freddie Mac is a senior holder — which are included among the OC Trusts referenced in paragraph 22 of the Petition — are not currently at their OC Target levels, and will not be as of (or after) the date that the distributions of settlement proceeds are made. Therefore, any distributions, including the Subsequent Recoveries provided for by the Settlement Agreement, must go to senior holders sequentially in order of priority. There is, in Freddie Mac's respectful view, no genuine basis for dispute on this issue under a correct reading of the applicable PSAs.

It appears from the Trustee's Petition that certain less-senior certificateholders have advocated to the Trustee a different method of calculating overcollateralization — one that would result in a windfall to them. These holders, apparently, want the Trustee to ignore that the trusts will *not* be at their OC Targets on, *or after*, the relevant distribution date, but instead to

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<sup>3</sup> In that scenario, not present here, distributions are made first to senior classes (concurrently (pro rata) as among them) and then to junior classes (sequentially as among them) based on Realized Losses previously applied to each of those classes.

focus on a theoretical point in time *during* the distribution when, they apparently argue, the trusts appear to be at the OC Target.

There are many problems with this approach, including that the fictional moment in time when the trust is at the OC Target is a chimera. The trust will be below the OC Target when the distribution commences *and will be below it again when the distribution is over*. No more collateral will be added to the trust, and no less money will be owed on the securities issued by the trust. That is why the Petition states that any overcollateralization calculation performed as the agitating holders propose leads to “temporary and illusory” overcollateralization, which could lead to wholly unintended “leakage” of settlement funds to persons who are not entitled to them. (Petn. ¶ 26; Prayer for Relief subpar. (i)(b).) The Trustee therefore requests an instruction (*see* Prayer for Relief subpar. (i)(a)) that would allow it to make an “adjustment” that would avoid this (perverse) result.

In fact, no such “temporary and illusory” calculation of overcollateralization is permitted under the governing PSAs. Rather, the Trustee is required to calculate the OC Amount “**after giving effect to**” the distribution “**to be made.**” *See* CWABS 2006-3 PSA § 1.01, Def. of “Overcollateralized Amount.” If overcollateralization is calculated according to that prescribed methodology, the trust is never at the OC Target on the relevant distribution date. The senior certificates that receive the distribution of settlement proceeds are written down to the extent of that distribution; the more junior certificates, previously written down to reflect Realized Losses on non-performing loans, are written up in the (precise) amount of the write down of the seniors; the aggregate certificate balance (money owed by the trust on securities it issued) does not change; the aggregate collateral (loan balance) backing the certificates does not change; the trust’s books remain in perfect balance as they were prior to the distribution; and the trust

remains, for purposes of calculating overcollateralization, exactly where it was before the distribution (below the OC Target). The senior holders get paid as they are supposed to, the junior holders enjoy no windfall by way of leakage or otherwise, and that is the end of the matter.

The Court should order the Trustee to calculate overcollateralization prior to making the distribution of Settlement Proceeds by accounting for both the necessary write down, and the corresponding write up, of the Certificates, which approach is in accordance with subparagraph (i)(a) of the Trustee’s Prayer for Relief and is required by the governing PSAs.<sup>4</sup> (*See* Petn. ¶¶ 29–30.)

#### BACKGROUND AND CONTRACTUAL PROVISIONS

The trusts in question are OC Trusts. An OC Trust is one in which, essentially, the aggregate principal balance of the loans exceeds the aggregate certificate balance of the interest-bearing securities backed by the loans. The trusts, in other words, are overcollateralized in that the trust’s assets (loans) exceed its liabilities (certificates).<sup>5</sup> The governing PSAs require that

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<sup>4</sup> In answer to the statements in the Petition, Freddie Mac takes no position on paragraphs 1–16, 18–24, 31–39, and 41–45. Freddie Mac agrees with the statement in paragraph 28 that leakage to less senior Certificates is inconsistent with an essential purpose of the overcollateralization structure. Freddie Mac disagrees with the statements in paragraph 17 in that Freddie Mac believes the issue concerns the interpretation of the definition of “Overcollateralized Amount” in the PSAs, not the meaning of the write up provisions. Freddie Mac disagrees with the statements in paragraphs 25–27 in that Freddie Mac believes the applicable PSAs do not permit overcollateralization to be calculated in the manner described in those paragraphs and do not permit “leakage.” Concerning the statements in paragraphs 29–30 and 40, Freddie Mac believes the Trustee’s proposed “adjustment” is not an “adjustment” at all — instead, it is already required by the PSAs — and that the PSAs already require the Trustee to “calculat[e] overcollateralization in the OC Trusts in a manner that accounts for the expected write up of previously written down Certificates.”

<sup>5</sup> That is, the amount of the loan balance exceeds the certificate balance for the interest-bearing certificates — the senior and mezzanine classes. On the liability side of the balance sheet, the

collections of principal be distributed to certificateholders sequentially in order of seniority.

PSA § 4.04(b) or § 4.02(b).<sup>6</sup> In other words, senior holders get paid first before mezzanine holders, and the most-senior classes get paid before the less-senior classes. If, however, as of the relevant distribution date, there is an excess of loan balance over certificate balance, and if that excess is above the OC Target, giving rise to “Excess Cashflow,” that excess cash is distributed not sequentially in strict order of seniority of senior classes, but rather concurrently among senior classes according to the amount of Realized Losses attributed to each of the senior classes (and thereafter to junior classes). PSA § 4.04(c) or § 4.02(c).<sup>7</sup> The logic of this scheme is clear: only

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amount of that excess is normally attributed to a “residual” interest, typically retained by the sponsor of the deal, which is roughly equivalent to equity in a capital structure.

<sup>6</sup> As noted, the citations are to PSA section numbers for the 21 OC Trusts in which Freddie Mac is a holder. Under the PSAs for those deals, the settlement proceeds (treated by the Settlement Agreement as Subsequent Recoveries) will be distributed as principal. Principal payments reduce the amount of the Certificate Principal Balance of the certificates to which the proceeds are distributed. The amount of principal paid sequentially to senior classes under the waterfall is the “Principal Distribution Amount.” *Id.* In the OC Trusts in which Freddie Mac holds certificates, the Principal Distribution Amount, in turn, includes the “Principal Remittance Amount” — which consists of repayments of principal, Subsequent Recoveries, and other sources — minus an “Overcollateralization Reduction Amount.” The Overcollateralization Reduction Amount is the difference between the Overcollateralized Amount and the “Overcollateralization Target Amount.” The PSA sets the Overcollateralization Target Amount by formula. Thus, after one works through the contractual terms, the PSA distributes repayments of principal through the waterfall distribution, but it removes from the distribution pool the excess of the Overcollateralized Amount over the target threshold, or Overcollateralization Target Amount.

<sup>7</sup> The provisions in Section 4.04(c) and, in some PSAs, Section 4.02(c) contain substantially similar language. (*See* the PSAs included herewith.) In contrast to the sequential waterfall under Section 4.04(b), this second distribution method is not purely sequential. Instead, it distributes first to the senior classes of Certificates, but among senior classes the distribution is performed concurrently in accordance with the Unpaid Realized Losses applied to the Certificates rather than based on the outstanding Certificate Principal Balances. In many cases, this distribution priority favors the more-junior Certificateholders, including less-senior tranches within the same senior class, because losses are generally realized in *reverse* order of seniority. Thus, only certificates with losses will receive funds earmarked to repay losses, and only to the extent of those losses.

when senior holders are protected to the full extent of the OC Target can “Excess Cashflow” be distributed not to the most-senior class first but concurrently among all senior classes (and then among more-junior classes) by losses.

Where there is no *actual* overcollateralization before or after the distribution — and there will be none here — the only way that distribution pro rata by losses can occur is by application of a calculation methodology that ignores the terms of the PSAs as well as the requirements of trust accounting and the economic reality of the trust. The trust owns loans (assets) and owes payments to certificateholders (liabilities). As borrowers pay on loans and those payments are passed through to certificateholders, the loan balances and the certificate balances are written down in a corresponding amount. As with any balance sheet, assets and liabilities must always be in balance.

But with payments like those under the Settlement Agreement — which are treated as though they are “Subsequent Recoveries” (*see* SA § 3(d)(i); CWABS 2006-3 PSA § 1.01) — the distribution of proceeds has no net effect on either the aggregate loan balances or aggregate certificate balances. The non-performing loans to which such proceeds are attributable have already been marked down to zero, and because those aggregate loan balances do not change, the aggregate certificate balance also does not change.<sup>8</sup> Although the specific certificates receiving

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<sup>8</sup> With performing loans, principal payments made by borrowers each month are subtracted from the Stated Principal Balance as “the principal portion of the Scheduled Payments (x) due with respect to such Mortgage Loan . . . (y) that were received.” CWABS 2006-3 PSA § 1.01, Def. of “Stated Principal Balance”; *see also id.*, Def. of “Scheduled Payments” (defined to include borrowers’ regular payments but not Subsequent Recoveries). And when those payments are distributed to certificateholders, the certificate balance is decreased; the PSA thus defines the Certificate Principal Balance of a certificate as “the Initial Certificate Principal Balance . . . less . . . all amounts distributed . . . in reduction of the Certificate Principal Balance.” *Id.*, Def. of “Certificate Principal Balance.” Both sides of the trust’s balance sheet are “written down” to account for the principal payments to the trust and the distribution of that payment to the certificateholders. By contrast, for loans that have been liquidated (foreclosed upon) and subject

the Subsequent Recoveries are written down, other certificates that have previously been written down to reflect the losses associated with liquidated loans are written up in the same amount. The only thing that changes is the relative certificate balances of different classes of certificates, because some have received proceeds and others have not. The amount of overcollateralization, if any, remains exactly as it was before.

When the calculations and write downs/write ups are properly performed, there is no moment in time at which the calculation of overcollateralization, or of loan or certificate balances, is thrown off in a manner that would allow leakage to occur. The books are balanced before the distribution. The books are balanced after the distribution. Any adjustments to the books are made simultaneously, like every other balance-sheet adjustment. One class of certificate balances goes down, another goes up, and there is no point in time — as a matter of reality or balance-sheet accounting — at which the certificate balances in the aggregate go down by the amount of the distribution, or any portion thereof, such that the trust is, or even appears to be, at the OC Target.

The following example illustrates how the trust accounting should work in the context of receiving settlement proceeds. Suppose the aggregate loan balance backing the certificates is \$1,000,000. The aggregate certificate balance is the same amount, \$1,000,000. Subsequent

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to a determination by the servicer that it has received all amounts it expects to receive in connection with the liquidation of the loan, the principal balance for those loans is reduced to zero for certain relevant accounting purposes; the amount written off is treated as a “realized loss” and is applied to reduce certificate principal balances beginning with the most junior certificates. *See id.* § 4.04(g). When a Subsequent Recovery is received with respect to such loans, there is no reduction in the loan principal balance because the principal loan balance has already been reduced to zero. The corresponding balance sheet effect of the Subsequent Recovery is a write up, in the amount of the recovery, of certificates previously written down by realized losses. *See id.* § 4.04(h).



Recoveries do not decrease the aggregate loan balance by a single dollar. They are instead merely flow-through payments on failed loans — loans that have already been written down to zero. The aggregate value of the loans is still \$1,000,000. The aggregate value of the certificates is also still \$1,000,000. Nothing changes, other than the fact that payments are made to senior holders. Because those payments are made, the certificate balances of holders receiving the payments go down, the certificate balances of holders not receiving the payments simultaneously go up by a corresponding amount — that is the “write up” contemplated by the Settlement Agreement and the PSAs — and the trust ends up exactly where it was before, with \$1,000,000 on each side of the balance sheet, and short of the OC Target. The Settlement Agreement contemplates that, once settlement payments are distributed to any Covered Trust, the Trustee will write the aggregate certificate balance back up by writing up each class to which a Realized Loss has been applied,<sup>9</sup> in reverse order in accordance with the PSAs.<sup>10</sup>

Nonetheless, the position of the more junior certificateholders is, evidently, that in determining overcollateralization the Trustee should give effect to the write down of senior certificateholders resulting from the distribution of the amount of the settlement payments while ignoring the corresponding write up effect for other holders, resulting in the “temporary and illusory” impression referred to in the Petition of a trust at the OC Target when no such thing

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<sup>9</sup> Realized Losses are allocated first to junior classes of certificates: “an Applied Realized Loss Amount will not exist for a single Loan Group with respect to its corresponding Class A Certificates unless the Certificate Principal Balances of the Subordinate Certificates have been reduced to zero.” *See* CWABS 2006-3 PSA § 1.01, Def. of “Applied Realized Loss Amount”.

<sup>10</sup> The Settlement Agreement provides that each Allocable Share of the settlement proceeds will be applied to “Class Certificate Balance” which is defined as the aggregate balance for the class. SA § 3(d)(ii); *see also* CWABS 2006-3 PSA § 4.04(h) (“On each Distribution Date, the Trustee shall allocate the amount of the Subsequent Recoveries . . . to increase the Certificate Principal Balance” of the Certificates sequentially.).

exists. The PSAs prohibit this approach, by requiring the Trustee to calculate the OC Amount “after giving effect to” the distribution “to be made.”

### ARGUMENT

#### **I. The Plain Terms of the PSAs Do Not Permit Recognition of Illusory or Temporary Overcollateralization, So Leakage Is Not Permitted.**

The Settlement Agreement requires the Trustee to distribute the Allocable Share for each loan group in each Covered Trust “in accordance with the distribution provisions of the Governing Agreements . . . as though it was a Subsequent Recovery available for distribution on that distribution date.” SA § 3.01(d)(i). The agreement even emphasizes that “[n]othing” in its relevant subparagraphs “is intended to or shall be construed to amend any Governing Agreements.” *Id.* § 3.01(d)(v). Thus, the terms of the Governing Agreements — the PSAs — control the method of distribution. And those terms provide for a distribution that prevents any “illusory” or “temporary” overcollateralization.

Specifically, for all the Freddie Mac trusts, the PSAs determine whether there is overcollateralization that gives rise to Excess Cashflow to be distributed pro rata by losses among senior classes by comparing the Overcollateralized Amount to the Overcollateralization Target. The PSAs provide that the Trustee shall calculate Overcollateralized Amount by “giving effect to” the distribution “to be made.” CWABS 2006-3 PSA § 1.01, Def. of “Overcollateralized Amount.” The CWABS 2006-3 trust, for example, contains the following definition of Overcollateralized Amount:<sup>11</sup>

Overcollateralized Amount: With respect to any Distribution Date, the amount, if any, by which (x) the sum of the aggregate Stated Principal Balance of the

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<sup>11</sup> The PSA language is substantively the same in other trusts in which Freddie Mac is an investor. Again, the focus of this submission is on deals in which Freddie Mac is a holder. As set forth in the submission of certain institutional investors, there are a few OC Trust PSAs that vary from this formulation.

Mortgage Loans for such Distribution Date and any amount on deposit in the Pre-Funding Account exceeds (y) the aggregate Certificate Principal Balance of the Interest-Bearing Certificates as of such Distribution Date (**after giving effect to distribution** of the Principal Remittance Amounts **to be made** on such Distribution Date and, in the case of the Distribution Date immediately following the end of the Funding Period, any amounts to be released from the Pre-Funding Account).

*Id.* (emphasis added).

There can be no mistaking the import of the unambiguous bolded language. The effect on overcollateralization of the distribution is to be calculated “after giving effect” to the distribution *before* it is made. That is why the provision refers to the distribution “to be made.” The “after giving effect” instruction means that the Trustee measures the Overcollateralized Amount as though the write-up of certificates after distribution of the Subsequent Recovery has already taken place, because the immediate effect of paying out Subsequent Recoveries to senior certificateholders (whose Certificate Principal Balances are correspondingly reduced) is to write back up the Certificate Principal Balances of the holders not receiving the distribution of settlement proceeds. In this simple, straightforward way, the PSA takes care of the issue that now troubles the Trustee.

In interpreting contracts, “[u]nambiguous words and phrases will be construed according to their plain meaning.” *Bank of New York v. Amoco Oil Co.*, 35 F.3d 643, 661 (2d Cir. 1994); *see also Brainard v. New York Central R.R. Co.*, 242 N.Y. 125 (1926) (holding that words and phrases should be given their natural meaning); *cf. Peak Development, LLC v. Constr. Exchange*, 100 A.D. 3d 1394, 1395 (4th Dep’t 2012) (“[I]n interpreting a written contract, we should give effect to the intent of the parties as revealed by the language *and* structure of the contract . . . .”) (emphasis added). It would make little sense to take into account only the payment itself, which reduces the Certificate Principal Balance, and not the corresponding write-up. That would give only partial “effect” to the distribution, and the contractual definition does not support such an

artificially narrow construction. Thus, the most natural reading of “giving effect to” the Subsequent Recovery (the distribution “to be made”) is to give it its complete (net) accounting effect.

Although the Petition does not discuss the “after giving effect to” language, the Trustee proposes to “adjust the Certificate Principal Balances . . . (taking into account the [Subsequent Recovery] write up that will happen after the payment is made) *solely* for the purpose of determining the overcollateralization level of the OC Trust.” Petn. ¶ 30. The “after giving effect to” language in the definition of Overcollateralized Amount requires exactly that. In short, the Trustee’s proposed calculation adjustment is not an “adjustment” at all; it is an application of the calculation methodology the PSAs require.

**II. The Fundamentals of Balance-Sheet Accounting and the Purpose of Overcollateralization Require the Trustee to Consider the Entire Effect of the Distribution.**

The plain terms of the definition of “Overcollateralized Amount” answer the question here. But, should this Court believe the Governing Agreements require further construction, it should construe them “in a manner that accords the words their fair and reasonable meaning, and achieves a practical interpretation of the expressions of the parties. Put otherwise, a contract should not be interpreted to produce a result that is absurd, commercially unreasonable or contrary to the reasonable expectations of the parties.” *Greenwich Capital Fin. Products, Inc. v. Negrin*, 903 N.Y.S.2d 346, 348 (1st Dep’t 2010) (rejecting contract interpretation that “depends on ‘formalistic literalism’ and ignores common sense”) (internal citation omitted). Here, to require or permit the Trustee to distribute settlement proceeds without “giving effect” *in advance* to the distribution for purposes of calculating overcollateralization would defeat the purpose of

trust accounting, subordination and overcollateralization itself, producing a commercially unreasonable result.

As discussed above, trust accounting (like all balance-sheet accounting) is meant to balance assets and liabilities. Subsequent Recoveries reflect unexpected recoveries of principal that was previously written off. Thus, the Certificate Principal Balances are written down to reflect a Subsequent Recovery and then are written back up once the distribution is made. Properly accounted for, Subsequent Recoveries have no effect on the aggregate balance sheet of the trust. Since the Overcollateralized Amount is just the difference between assets and liabilities, the distribution of Subsequent Recoveries therefore has no effect on it, either. In short, the Governing Agreements are written to *prevent* the “temporary, and illusory, overcollateralization” described in the Petition. This Court should not construe those Agreements to frustrate the parties’ intent. *Cf. W.W.W. Assocs., Inc. v. Giancontieri*, 77 N.Y. 2d 157, 162 (1990) (contract must be “read as a whole to determine its purpose and intent”).

The Courts’ “aim is a practical interpretation of the expressions of the parties to the end that there be a realization of their reasonable expectations.” *Duane Reade, Inc. v. Cardtronics, LP*, 54 A.D.3d 137, 140 (1st Dep’t 2008) (quotation marks omitted). The parties expected that, when the trust was in distress, the principal on senior Certificates would be repaid before losses on more junior Certificates would be reimbursed. If there were any doubt about what the plain terms of the Governing Agreements require, this Court should construe them to honor that expectation.

### **III. The Settlement Agreement Is Consistent with the PSAs.**

Because the PSAs already require the calculation method outlined in subparagraph (i)(a) of the Prayer for Relief, the Settlement Agreement does as well. The Settlement Agreement

simply incorporates the PSA distribution provisions: “the Trustee shall distribute [the Allocable Share for each loan group] to Investors in accordance with the distribution provisions of the Governing Agreements . . . as though it was a Subsequent Recovery available for distribution on that distribution date . . . .” SA § 3.01(d)(i). The Settlement Agreement does nothing more than require the Trustee to follow the PSA distribution provisions as described above. The Trustee should therefore be instructed to calculate overcollateralization as required by the PSAs, by giving effect to both the write down and write up of certificate balances in determining the overcollateralized amount, without regard to any claimed “illusory” or “temporary” overcollateralization.

The order of operations in the Settlement Agreement does not change the result. As the Trustee notes, the Settlement Agreement sets out a particular sequence of distribution-related steps. It states, “*after* the distribution of the Allocable Share to Investors pursuant to Subparagraph 3(d)(i), the Trustee will allocate the amount of the Allocable Share . . . to increase the Class Certificate Balance . . . .” *Id.* § 3.01(d)(ii) (emphasis added). The junior holders who have written the Trustee presumably argue that, by accounting for the impending write-up when determining whether the trust is overcollateralized, the Trustee would in effect be executing the write-up before actually making the payment in violation of the Settlement Agreement’s order of operations.

Not so. The Settlement Agreement prohibits formally changing the Certificate Principal Balances by allocating the Subsequent Recovery to write them up, and then applying the payment to *those* new Certificate Principal Balances. For example, as the Trustee points out, in certain Covered Trusts the amount of the distributions “are affected by the relative Certificate Principal Balances of all Certificates.” (Petn. ¶ 35.) Therefore “a distribution based on ‘a write

up first and pay second order of operation in trusts where senior classes incurred losses to date would mean that less senior Certificates increase their Certificate Principal Balance in relation to more senior Certificates, potentially skewing the distribution in favor of less senior Certificates.” *Id.* In other words, if the distribution were calculated against written-up Certificate Principal Balances, the distribution amounts to each tranche of Certificateholders would be different than what they would be absent the write-up. That is what the Settlement Agreement’s order of operations prevents.<sup>12</sup> The PSAs in the OC Trusts, consistent with the Settlement Agreement, still require distributions to be made to the pre-written-up balances.

Finally, the distribution provisions in the PSAs devote several complex, interlocking definitions and paragraphs to calculating principal amounts, overcollateralization levels, and certificate balances. By contrast, the Settlement Agreement says nothing about overcollateralization. The court should not expand an unrelated statement in the Settlement Agreement about the relative order of distributions and write-ups to govern the method of calculating overcollateralization.

### CONCLUSION

For the foregoing reasons, this Court should grant the Petition and issue Judicial Instructions to the Trustee to calculate overcollateralization by accounting for both the expected

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<sup>12</sup> The distribution calculation method the Trustee points to exists only in so-called shifting interest or “SI Trusts.” None of those trusts are OC Trusts, and none of their Governing Agreements use the Overcollateralized Amount concept. For that reason alone, this issue — and the order of operations in the Settlement Agreement that addresses it — has no bearing on the argument advanced here, which turns on the definition of Overcollateralized Amount. The Trustee has also noted that the PSA of one trust specifies that payment should be made after the certificates are written up, but that trust is neither an OC Trust nor an SI Trust and is not relevant.

write down and write up of the Certificates, in accordance with subparagraph (i)(a) of the Prayer for Relief.

Dated: New York, New York  
March 4, 2016

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## **APPENDIX**

### **Covered Overcollateralization Trusts In Which Freddie Mac Is A Certificateholder**

CWABS 2005-9  
CWABS 2005-12  
CWABS 2005-13  
CWABS 2005-14  
CWABS 2005-16  
CWABS 2005-17  
CWABS 2005-AB2  
CWABS 2005-BC5  
CWALT 2005-AR1  
CWABS 2006-2  
CWABS 2006-3  
CWABS 2006-5  
CWABS 2006-7  
CWABS 2006-10  
CWABS 2006-19  
CWABS 2006-26  
CWABS 2006-BC2  
CWABS 2006-BC3  
CWALT 2006-OC8  
CWALT 2006-OC10  
CWALT 2006-OC11

A