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	Index No. 150973/2016
	Assigned to: Scarpulla, J.
Petitioner,	**BRIEF OF CERTAIN INSTITUTIONAL INVESTORS CONCERNING THE REMAINING DISPUTED TRUSTS**
For Judicial Instructions under CPLR Article 77 On the Distribution of a Settlement Payment.	

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The undersigned investors submit this brief concerning the 17 Remaining Trusts that are the subject of the objections lodged by Tilden Park Capital Management LP ("Tilden Park") and Prosiris Capital Management LP ("Prosiris") (collectively, the "Disputed Trusts"). The undersigned investors hold one or more of the super-senior certificates issued by each of the 17 Disputed Trusts except CWALT 2006-OA7 and submit this brief with respect to each Disputed Trust they hold.

STANDARD OF REVIEW

Article 77 Proceedings are summary in nature. In an Article 77 proceeding, the Court must examine the Trustee's Verified Petition (as well as any other evidence filed), after which it "shall make a summary determination upon the pleadings, papers and admissions to the extent that no triable issues of fact are raised."[1]

SUMMARY OF ARGUMENT

For the Disputed Trusts, the Trustee seeks judicial instruction from this Court as to whether it should distribute the Settlement Payment in a manner that leads to what the Trustee calls "leakage," in which settlement proceeds will be siphoned away from the super-senior certificates to deeply discounted junior certificates like those held by Tilden Park and Prosiris. The Pooling and Servicing Agreements ("PSAs") and Prospectus Supplements (collectively, the "Governing Agreements") require the Trustee to distribute the Settlement Payment in a manner that *avoids* leakage to those junior certificates. That result is not only required by the text of the Governing Agreements, it is also consistent with the basic intent of the subordination and overcollateralization structures and provisions in the Disputed Trusts: to allocate losses from the bottom of the waterfall up, with the senior-most certificates incurring losses only in the event

[1] N.Y.C.P.L.R. 409.

that junior certificates are unable to absorb such losses. Distributing the Settlement Payment as Tilden Park and Prosiris propose does violence to those structures, exposing the senior-most certificates to a risk of loss they were never intended to incur. The Governing Agreements therefore cannot be interpreted, consistent with their purpose, in a manner that perversely *flips* the structure of the Trusts by allowing tens of millions of dollars to leak to deeply discounted junior certificates, while dramatically increasing the risk of loss to the senior-most certificates in the months and years following the distribution of the Settlement Payment.

I. THE GOVERNING AGREEMENTS REQUIRE THE TRUSTEE TO DISTRIBUTE THE SETTLEMENT PAYMENT IN A MANNER THAT AVOIDS LEAKAGE TO JUNIOR CERTIFICATES.

A. The Court Should Read the PSAs Together with the Prospectus Supplements, Which Together Form the Contract Among the Parties.

Under New York law, which governs each of the Disputed Trusts, all writings forming part of a single transaction must be read together. *See, e.g.*, *This Is Me, Inc. v. Taylor*, 157 F.3d 139, 143 (2d Cir. 1998); *PETRA CRE 2007-1 CDO, Ltd. v. Morgans Grp. LLC*, 84 A.D.3d 614, 615 (1st Dep't 2011) ("Agreements executed at substantially the same time and related to the same subject matter are regarded as contemporaneous writings and must be read together as one."). A prospectus supplement is one of the "instruments disclosing all material terms and conditions" of a security like those issued by the Disputed Trusts. *In re Trusteeship Created by Am. Home Mortg. Inv. Trust 2005-2*, 14-cv-2494, 2014 WL 3858506, at *20 (S.D.N.Y. July 24, 2014). As such, the prospectus supplement reflects the "reasonable understanding of all potential investors." *Id.* at *21. New York courts have therefore held that agreements like PSAs must be read in conjunction with prospectus supplements to ascertain the actual intent of the parties. *See id.*; *see also Wells Fargo Bank, N.A. v. Fin. Sec. Assur. Inc.*, 504 Fed. App'x 38, 40

(2d Cir. 2012); *Bank of N.Y. Mellon v. WMC Mortg., LLC*, 12-cv-7096, 2015 WL 4597540, at *8 (S.D.N.Y. July 30, 2015).

This is especially true where the PSAs "explicitly reference[] and incorporate[] the Prospectus." *In re Trusteeship*, 2014 WL 3858506, at *20. The PSAs at issue here did just that. For example, Section 10.01 of the CWALT 2006-OA14 PSA states that the PSA can be amended *without the consent of certificateholders* "to conform [the PSA] to the Prospectus and Prospectus Supplement provided to investors in connection with the initial offering of the Certificates."[2] It is thus both appropriate and necessary for the Court to consider the Prospectus Supplements for the Disputed Trusts to ascertain the agreement among, and reasonable expectations of, the parties. The PSAs, together with the Prospectus Supplements, are therefore referred to below as the "Governing Agreements."[3]

B. The Text and Intent of the Governing Agreements Require That the Settlement Payment Be Distributed in a Manner That Avoids Leakage.

The Governing Agreements should be interpreted in a manner that is consistent with the intent of the parties. *See, e.g., Novak & Co., Inc. v. N.Y. Convention Center Dev. Corp.*, 202 A.D.2d 205, 206 (1st Dep't 1994) ("in a matter where parties seek enforcement of a contract, the court has the responsibility of effectuating the true intent of the parties" (quoting *Furgang v. Epstein*, 106 A.D.2d 609 (2d Dep't 1984))). The Governing Agreements cannot be read in a manner that "would defeat and contravene the purpose of the agreement[s]." *Reape v. N.Y. News, Inc.*, 122 A.D.2d 29, 30 (2d Dep't 1986). "Single clauses cannot be construed by taking them out of their context and giving them an interpretation apart from the contract of which they

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[2] The PSA for CWALT 2006-OA14 is attached as Exhibit B to the Affidavit of David M. Sheeren, filed herewith (the "Sheeren Aff.").

[3] A compilation of the key provisions of the Prospectus Supplements is included as Exhibit A to the Sheeren Affidavit. The full Prospectus Supplements and Pooling and Servicing Agreements for the Disputed Trusts, which are voluminous, are being delivered to the Court on a portable storage device.

are a part." *Richard Feiner & Co. v. Paramount Pictures Corp.*, 95 A.D.3d 232, 239 (1st Dep't 2012) (internal quotations omitted). "The ultimate aim" of these interpretive rules, of course, "is to realize the parties' reasonable expectations through a practical interpretation of the contract language." *Gessin Elec. Contractors, Inc. v. 95 Wall Assocs., LLC*, 74 A.D.3d 516, 518 (1st Dep't 2010); *see also Frye v. Brown*, 189 A.D.2d 1031, 1033 (3d Dep't 1993) ("Undoubtedly, the ultimate goal in contract interpretation is realization and effectuation of the parties' intent.").

1. Overcollateralization Exists to Protect Senior Certificates from Losses.

The basic purpose of overcollateralization is to insulate the senior certificates from the risk of loss. In the Trustee's words,

> An OC Trust is designed to create credit enhancement, or protection, for more senior Certificateholders through a concept called overcollateralization. An OC Trust is overcollateralized when the principal balance of the underlying mortgage loans (the trust's assets) exceeds the Certificates Principal Balances of the Certificates issued by the OC Trust (the trust's liabilities). In a given month, principal distributions to Certificates below specified seniority levels (generally, "junior" or "subordinated" Certificates) are ***not*** permitted unless the trust as a whole has sufficient "overcollateralization"—that is, unless the balance of the underlying mortgage loans (the trust's assets) exceeds the Certificate Principal Balances (the trust's liabilities) by an amount specified in the Governing Agreements. If the overcollateralization falls short of the required "Overcollateralization Target Amount"—hereinafter referred to as the OC Target—then principal distributions cannot flow to "junior" or "subordinated" holders.

Verified Pet. ¶ 23 (emphasis added). The Prospectus Supplements describe how overcollateralization protects the senior-most certificates as follows:

> On any distribution date, the amount of overcollateralization (if any) will be available to absorb the losses from liquidated mortgage loans if those losses are not otherwise covered by excess cashflow (if any) from the mortgage loans. The required level of overcollateralization may change over time.

Prospectus Supp. for CWALT 2006-OA10, S-19 (emphasis added).[4]

2. Subordination Exists to Protect Senior Certificates from Suffering Losses.

Even if the overcollateralization of a Trust is depleted, the senior-most certificates benefit from a second level of protection through subordination, a related type of "credit enhancement" described in the Prospectus Supplements. As set out in the Prospectus Supplements, subordination protects the senior-most certificates through the issuance of *junior* certificates, which are designed to absorb losses so they are not suffered by the senior-most certificates. In the Trustee's words, "[t]his senior-subordinate structure means that, as a general matter, subordinated Certificates are riskier than senior Certificates . . . ." Verified Pet. ¶ 28. This basic tradeoff of risk and return can be seen throughout the Governing Agreements, including in the Prospectus Supplements, which describe the purpose of subordination as follows:

> The issuance of senior certificates and subordinated certificates by the issuing entity is designed to increase the likelihood that senior certificateholders will receive regular distributions of interest and principal.
>
> . . . .
>
> Subordination is designed to provide the holders of certificates having a higher distribution priority with protection against losses realized when the remaining unpaid principal balance of a mortgage loan exceeds the proceeds recovered upon the liquidation of that mortgage loan. In general, this loss protection is accomplished by allocating the realized losses on the mortgage loans first, among the subordinated certificates, beginning with the subordinated certificates with the lowest distribution priority, and second to the senior certificates in accordance with the priorities set forth above under " – Allocation of Losses."

Prospectus Supp. for CWALT 2006-OA10, S-19 (emphasis added).[5]

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[4] Similar provisions appear in each of the Prospectus Supplements for the Disputed Trusts and are set out in Exhibit A to the Sheeren Affidavit.

[5] *Id.*

Consistent with the basic purpose of subordination, the Prospectus Supplements confirm that once the Trusts' overcollateralization is depleted, realized losses must be allocated *first* to the most junior class of certificates then outstanding, until its certificate balance is written down to zero, at which point realized losses are then allocated to the *next* most junior class of certificates, and so on, as follows:

> After the credit enhancement provided by excess cashflow and overcollateralization (if any) has been exhausted, collections otherwise payable to the subordinated classes will comprise the sole source of funds from which credit enhancement is provided to the senior certificates. Realized losses will be allocated in the following order of priority:
>
> - to the subordinated certificates, beginning with the class of subordinated certificates with the lowest distribution priority, until the class certificate balance of that subordinated class has been reduced to zero, and
> - concurrently, to the senior certificates (other than the notional amount certificates), pro rata, based on the aggregate class certificate balances of the group 1 senior certificates, the group 2 senior certificates, the group 3 senior certificates and the group 4 senior certificates as follows: (a) with respect to the group 1 senior certificates, sequentially, to the Class 1-A-3, Class 1-A-2 and Class 1-A-1 Certificates, in that order, until their respective class certificate balances are reduced to zero; . . . .

Id. at S-18 (emphasis added).[6] As this language shows, holders of the Class 1A1 Certificates—the super-senior certificates—are only supposed to suffer realized losses *after* realized losses have entirely depleted the more junior certificates, including the Class 1A2 Certificates like those held by Tilden Park and Prosiris. *Id.*

In plain terms, overcollateralization and subordination together form an asset cushion that provides protection to the senior-most certificates against the risk of loss. The first level of protection for the senior-most certificates is overcollateralization. Once the Trusts' overcollateralization is depleted, however, the Trusts' subordination structure continues to

[6] *Id.*

protect the senior-most certificates from suffering losses. The junior certificates bear a greater risk of loss and are compensated for that greater risk with a higher coupon rate than the rate paid to the safer, senior-most certificates. This basic structure is set out plainly in the Governing Agreements and is one to which all Certificateholders bound themselves when they purchased their certificates.

3. Tilden Park's Misinterpretation of a Single, Isolated Provision of the Governing Agreements Ignores Other Provisions of the Governing Agreements and Their Essential Purpose and Would Lead to Absurd Results.

Properly interpreted, the Governing Agreements require that the Settlement Payment be distributed in a manner that effectuates their essential purpose by protecting the senior-most certificates from the risk of loss. Because allowing part of the Settlement Payment to leak to junior certificates would perversely *increase* the risk of loss to the senior-most certificates, the Settlement Payment should be distributed in a way that prevents leakage. In arguing for leakage to their junior certificates, Tilden Park and Prosiris violate several basic rules of contract construction by misinterpreting a single, isolated provision of the Governing Agreements and ignoring contrary provisions of the Governing Agreements and the essential purpose of the Trusts' overcollateralization and subordination structures.

The Settlement Agreement requires the Trustee to distribute the Settlement Payment "as though it was a Subsequent Recovery available for distribution on that distribution date." Settlement Agr. § 3(d)(i). In each of the Disputed Trusts, Subsequent Recoveries are included in the "Principal Remittance Amount."[7] As the Trustee has explained, Subsequent Recoveries have historically been "modest" and are "typically limited to funds such as proceeds of the sale of real estate owned properties and adjustments to payments on private mortgage insurance claims."

[7] *See* PSA for CWALT 2006-OA14 § 1.01 (Definitions) (attached as Ex. B to the Sheeren Aff.).

Verified Pet. ¶ 15. Therefore, Subsequent Recoveries have historically been included in full in the "Principal Distribution Amount," which is generally distributed to senior certificates based on their respective certificate balances.[8] Indeed, with respect to the 512 Trusts that have already received their share of the $8.5 billion Settlement Payment, 100% of each Trust's Allocable Share was treated as a Subsequent Recovery and distributed as part of the Principal Distribution Amount to the senior certificates based on their respective certificate balances.

Tilden Park argues, however, that with respect to the 17 Disputed Trusts, only *part* of the Allocable Shares can be included in the "Principal Distribution Amount" because, by its definition, the Principal Distribution Amount is "cap[ped]" by the sum of (i) regular monthly principal payments received from borrowers; (ii) regular monthly proceeds from the liquidation of mortgage loans; and (iii) the Overcollateralization Target Amount (which is defined as a fixed, dollar amount).[9] Based on this single, isolated provision of the Governing Agreements, Tilden Park and Prosiris argue that only the portion of the Allocable Share *up to* the Overcollateralization Target Amount can be paid as part of the Principal Distribution Amount.

Tilden Park and Prosiris then argue that the portion of the Allocable Share that *exceeds* the Overcollateralization Target Amount must be distributed pursuant to a later provision of the PSAs that reimburses certificates for their past realized losses.[10] As their argument goes, because the vast majority of past realized losses have been suffered by deeply discounted (and often entirely written off) *junior* certificates like those held by Tilden Park and Prosiris, the

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[8] *See, e.g.*, *id.* § 1.01 (definition of "Principal Distribution Amount") & § 4.02(a)(5)(A)(1) (distribution method for "Principal Distribution Amount").

[9] *See* Tilden Park's Mem. of Law in Support of Respondent's Verified Answer to the Verified Pet. (Docket No. 32) at 9-10, 14-15.

[10] *Id.* An example of this provision for the reimbursement of losses is Section 4.02(a)(6)-(7) of the PSA for CWALT 2006-OA14 (attached as Ex. B to the Sheeren Aff.).

junior certificates should receive most (and sometimes all) of the amount by which the Allocable Share exceeds the Overcollateralization Target Amount.[11]

In the Trustee's own words, however, diverting the bulk of the Settlement Payment "to less senior, subordinated Certificateholders at the expense of more senior Certificateholders could be viewed as ***contrary to an essential purpose of the overcollateralization structure—protecting more senior Certificateholders from risk of loss***." Verified Pet. ¶ 28 (emphasis added). New York courts do not endorse a reading of contract language if it "would defeat and contravene the purpose of the agreement." *Reape*, 122 A.D.2d at 30; *see also Frye*, 189 A.D.2d at 1033 ("Undoubtedly, the ultimate goal in contract interpretation is realization and effectuation of the parties' intent."). But that is just the sort of reading that Tilden Park and Prosiris invite the Court to embrace. The Court should reject the invitation.

In advocating for the bulk of the Allocable Shares to be paid to their deeply discounted junior certificates, Tilden Park and Prosiris have taken a single clause out of the context of the overall contract and given it an interpretation at odds with the contract of which it is a part, violating one of the basic rules of contract interpretation under New York law. *See, e.g.*, *Richard Feiner & Co.*, 95 A.D.3d at 239. Tilden Park and Prosiris's interpretation that the "Principal Distribution Amount" should be capped at the Overcollateralization Target Amount cannot be reconciled with either the text of the Governing Agreements as a whole or the basic purpose of the Trusts' subordination and overcollateralization structures: to insulate the senior-most certificates from the risk of loss.

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[11] *See* Tilden Park's Mem. of Law in Support of Respondent's Verified Answer to the Verified Pet. (Docket No. 32) at 9-10, 14-15.

Tilden Park and Prosiris's reading is particularly problematic because, once the Allocable Shares are diverted to the junior certificates, they will *never return* to the Trusts through the creation of increased overcollateralization or subordination.[12] As a result, when underlying mortgages default and lead to realized losses in the future, the senior-most certificates will be *far* more likely to bear those realized losses under Tilden Park and Prosiris's (mis)reading of the Governing Agreements. In this way, their reading would *eviscerate* the Trusts' subordination and overcollateralization structures and force the senior-most certificates to bear losses *before* they are borne by junior certificates. This result is plainly "in tension with the descriptions" in the Prospectus Supplements and fails to "give independent force and effect to each provision of the . . . critical documents responsible for placing the loans into the RMBS trust." *Bank of N.Y. Mellon*, 2015 WL 4597540, at *8 (adopting a "more holistic reading" of a PSA to account for the language in the prospectus).

In any event, under Tilden Park and Prosiris's reading, the *only* reason their junior certificates would receive a windfall is that the Allocable Shares exceed the Overcollateralization Target Amounts for their Trusts because of the "unprecedented amount of Subsequent Recoveries" flowing into the Trusts. Verified Pet. ¶ 26. Like many of the OC Trusts, however, any overcollateralization in the Disputed Trusts has already been *depleted*, and as the Trustee indicated in the Petition, "it is likely that the OC Trusts will never meet their OC Target again."

[12] In many instances, the distribution of the Settlement Payment according to Tilden Park and Prosiris's preferred method would cause the Trusts to become *under*collateralized as a result of the Settlement Payment. Under Tilden Park and Prosiris's preferred distribution method, whenever the portion of the Allocable Share to be distributed to the junior certificates as reimbursement of losses exceeds those certificates' outstanding principal balances—as is often the case, given that many of the junior certificates have already been written down to zero or are deeply discounted—the post-distribution "write-up" mandated by Section 3(d)(ii) of the Settlement Agreement will cause the trusts' outstanding certificate balances to exceed the Trusts' outstanding collateral balances, leading to the creation of *under*collateralization as a result of the Settlement Payment. That outcome makes no sense under the contracts and would leave the Trusts structurally unsound.

Id. ¶ 24. As the Trustee further explained in the Verified Petition, any purported overcollateralization created by the Settlement Payment itself is "illusory," "temporar[y]," and "artificial[]." *Id.* ¶¶ 26, 29. Even under Tilden Park and Prosiris's reading of the contracts, the Settlement Payment itself cannot create *real* overcollateralization—such that the Trusts' outstanding collateral balances exceed the Trusts' outstanding certificate balances. Despite this, their *entire argument* hinges on the "illusory," "temporar[y]," and "artificial[]" achievement of the Overcollateralization Target Amount *during* the distribution of the Allocable Shares—simply because the Subsequent Recoveries are large. There is no "reasonable" or "practical" rationale, *see Gessin Elec. Contractors, Inc.*, 74 A.D.3d at 518, for diverting the bulk of the Settlement Payment to deeply discounted junior certificates based on the *illusion* that the Disputed Trusts' Overcollateralization Target Amounts are met. Therefore, the Court should not permit it.

The absurd and commercially unreasonable results of Tilden Park and Prosiris's interpretation can be shown in an example for one of the Disputed Trusts: CWALT 2006-OA14. The Allocable Share for that Trust is $38,887,771.[13] The Overcollateralization Target Amount for that Trust is equal to the "OC Floor," which is now fixed at $4,771,950.[14] The outstanding certificate balances and realized losses below are drawn from the Trust's most recent remittance report[15]:

[13] The Allocable Shares for each Trust and Loan Group are available on the Trustee's settlement website (http://cwrmbssettlement.com/notice.php). As shown there, the Settlement Payment is split among each of the three groups in this Trust as follows: Group 1 ($13,864,960); Group 2 ($12,744,897); and Group 3 ($12,277,914).

[14] The OC Floor is calculated as 0.5% of the Trust's Cut-off Date Pool Principal Balance of $954,390,021.53.

[15] *See* Ex. C to the Sheeren Aff. Certificates not at issue here are not shown in the table.

Class	Certificate Balance	Cumulative Realized Losses	*Held by Tilden Park or Prosiris?*
1A1	$74,489,454	$1,005,245	
1A2	$0	$47,683,715	*Yes*
1A3	$0	$17,968,331	
2A1	$54,630,919	$701,107	
2A2	$0	$40,545,147	*Yes*
2A3	$0	$16,586,201	
3A1	$67,048,052	$30,589,865	
3A2	$0	$34,212,851	

As the above table shows, the senior-most certificates (1A1, 2A1, 3A1) have already begun suffering realized losses, and the junior certificates held by Tilden Park and Prosiris (1A2, 2A2) have already been completely written off (i.e., they now have a certificate balance of zero dollars), and they have suffered realized losses of over $47 million and $40 million, respectively. Under Tilden Park and Prosiris's reading of the Governing Agreements, the Principal Distribution Amount would be "capped" by the Overcollateralization Target Amount of $4,771,950, which would leave $34,115,821 to distribute under the later provision of the PSA that generally reimburses certificates for past realized losses[16]:

Total Allocable Share for CWALT 2006-OA14	$38,887,771
Less Overcollateralization Target Amount Paid to Senior-Most Certificates	($4,771,950)
Remaining Allocable Share to Be Distributed As Reimbursement of Losses	$34,115,821

Next, under Tilden Park and Prosiris's (mis)interpretation, the senior-most certificates would be reimbursed for their past realized losses, but because the 1A1 and 2A1 Certificates have only recently begun suffering realized losses, those amounts would not be significant for

[16] *See supra* notes 7-10 for examples of these provisions.

the 1A1 and 2A1 Certificates.[17] In total, Intex's modeling shows that under Tilden Park and Prosiris's reading of the Governing Agreements—reflected in Intex's "After Distribution" Method—approximately $19 million of the total $38.9 million settlement payment would "leak" to the junior certificates held by Tilden Park and Prosiris and would never return to the Trusts in the form of increased overcollateralization or subordination for the benefit of the senior-most certificates.[18] This outcome cannot be reconciled with the text or intent of the Governing Agreements. It serves no rational economic purpose and provides the junior certificates a massive windfall for which they did not bargain, and therefore could not and should not have expected, given the requirements of the contracts and the central purpose of the subordination and overcollateralization provisions they contain.

Furthermore, because Tilden Park and Prosiris's interpretation would divert the bulk of the Allocable Shares to deeply discounted junior certificates, and would not build an asset cushion in the form of subordination or overcollateralization, the senior-most certificates' risk of loss would perversely *increase* in the future. For example, Intex's modeling shows that under the "After Distribution" Method preferred by Tilden Park and Prosiris, the super-senior 1A1 certificate would suffer realized losses almost six years earlier than it would under Intex's "Standard" Method, and the 2A1 certificate would suffer realized losses over eight years earlier than it would under Intex's "Standard" Method, assuming the Allocable Share was paid in September 2016[19]:

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[17] The reimbursement of losses for the 3A1 certificate, however, would be significant, but Tilden Park and Prosiris do not hold that certificate or the 3A2 certificate which is more junior to it.

[18] *See* Sheeren Aff. ¶ 5.

[19] *See id.* ¶ 6.

Super Senior Certificate	**Date on Which Super Senior Certificate Will Resume Suffering Realized Losses**		**Acceleration of Realized Losses Suffered by Senior-Most Certificates Under Tilden Park / Prosiris Distribution Method**
	Tilden Park / Prosiris Distribution Method (i.e., Intex's "After Distribution" Method)	**Intex's "Standard" Method**	
1A1	December 2016	August 2022	5 years, 8 months
2A1	September 2017	November 2025	8 years, 2 months

Permitting $19 million of the Allocable Share to "leak" out to *entirely written off* junior certificates just *months before* the senior-most certificates would begin incurring significant realized losses is an absurd, commercially unreasonable result. It turns the overcollateralization and subordination structures in this Trust upside down by allocating the risk of losses to the senior-most certificates instead of to the junior certificates.

Finally, another hypothetical demonstrates the absurdity of Tilden Park and Prosiris's argument: If the Allocable Share of $38,887,771 for CWALT 2006-OA14 was distributed in eight monthly installments equal to the OC Target of $4,771,950 and a ninth installment of $712,171, then even under Tilden Park and Prosiris's reading of the Governing Agreements, the senior-most certificates would receive 100% of the Allocable Share because the OC Target—the alleged "cap" on the Principal Distribution Amount—would never be exceeded in any given month. It makes no sense under the Governing Agreements for the senior-most certificates to be made substantially *worse off* if the Allocable Share was paid *sooner* rather than *later*, but that perverse result is required under Tilden Park and Prosiris's reading of the contract.

II. INDUSTRY PARTICIPANTS UNDERSTOOD AND EXPECTED THAT THE SETTLEMENT PAYMENT WOULD BE DISTRIBUTED IN A MANNER THAT AVOIDS LEAKAGE TO JUNIOR CERTIFICATES.

Because Tilden Park and Prosiris's interpretation of the Governing Agreements is so contrary to their meaning and intent, industry participants have long expected that the Settlement Payment would be made to the senior-most certificates in a manner that avoids leakage to junior certificates. These market expectations have manifested in several ways.

A. Intex's "Standard Method" Does Not Provide for Leakage to Junior Certificates Like Those Held by Tilden Park and Prosiris.

First, as the Trustee itself noted in the Verified Petition, Intex, "a leading provider of cash flow models that are used and relied upon by investors throughout the structure fixed income industry," has modeled the distribution of the Settlement Payment in the Disputed Trusts.[20] Intex's "Standard" Method, which serves as the *default* distribution method for each of the Disputed Trusts, *see* Aff. of Intex Solutions, Inc. ¶ 5, App. A.,[21] does not provide for leakage of the Settlement Payment to junior certificates like those held by Tilden Park and Prosiris.

Intex has testified that it began modeling how the Settlement Payment would flow under Tilden Park and Prosiris's preferred method only at the request of certain unnamed investors. *See id.* ¶ 6. The earliest date on which Intex appears to have added a so-called "toggle" to allow investors to see the impact of distributing the Allocable Shares under Tilden Park's theory was September 5, 2014 for CWALT 2007-OA3—over ***three years after*** the Settlement Agreement was posted on the Trustee's website in July 2011 and approximately ***10 months after*** the first Article 77 trial ended in November 2013. *Id.* Both Tilden Park and Prosiris hold the 1A2 and

[20] Verified Pet. ¶ 42.

[21] *See* Exhibit E to the Sheeren Aff.

2A2 junior certificates in that Trust. Intex has not disclosed the identity of the investors who requested that Intex add the "toggle."

B. The Settlement Agreement Itself and Trial Testimony in the Prior Article 77 Proceeding Confirm That the Settlement Payment Was Not Intended to Leak to Junior Certificates.

Finally, both the Settlement Agreement itself and trial testimony in the first Article 77 confirm that it was never intended that significant amounts of the Settlement Payment would be diverted to deeply discounted junior certificates like those held by Tilden Park and Prosiris, to the detriment of the senior-most certificates.

By requiring a "write up" of certificate balances in Section 3(d)(ii) of the Settlement Agreement in an amount that would completely *offset* the amount by which the Allocable Shares would otherwise "pay down" the certificate balances under Section 3(d)(i), the Settlement Agreement makes clear that the Settlement Payment was not intended to *alter* the level of collateralization in the Trusts:

> (ii) In addition, 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 for that Covered Trust in the reverse order of previously allocated Realized Losses, to increase the Class Certificate Balance, Component Balance, Component Principal Balance, or Note Principal Balance, as applicable, of each class of Certificates or Notes (or Components thereof) (other than any class of REMIC residual interests) to which Realized Losses have been previously allocated, but in each case by not more than the amount of Realized Losses previously allocated to that class of Certificates or Notes (or Components thereof) pursuant to the Governing Agreements . . . . For the avoidance of doubt, this Subparagraph 3(d)(ii) is intended only to increase Class Certificate Balances . . . as provided for herein, and shall not affect the distribution of the Settlement Payment provided for in Subparagraph 3(d)(i).

(Emphasis added.) However, under Tilden Park and Prosiris's interpretation, the *entirely written off* junior certificates they hold would both (i) receive the bulk of the Settlement Payment as reimbursement of their past realized losses and (ii) receive a "write up" in the full amount of the

Settlement Payment they receive.[22] In that case, however, the "write up" of their certificate balances under Section 3(d)(ii) would necessarily *exceed* the amount by which their certificate balances are "paid down" under Section 3(d)(i) – because it is impossible to "pay down" a certificate balance *below* zero. As a result, under Tilden Park and Prosiris's (mis)interpretation, the Settlement Payment would cause the Trusts' outstanding certificate balances to exceed the Trusts' outstanding collateral balances, which is the very definition of *under*collateralization. That outcome cannot be reconciled with the plain intent of the Settlement Agreement not to alter the level of collateralization in the Trusts.

Testimony in the original Article 77 proceeding also confirms that it was never intended that the Settlement Payment would be distributed to holders of deeply discounted junior certificates; to the contrary, the testimony confirms that the intention was that the Settlement Payment would be distributed consistently with the text and intent of the Trusts' overcollateralization and subordination structures, so that the senior-most certificates would be insulated from the risk of loss and the existing overcollateralization of the Trusts (whatever it was) would be unaltered by the settlement. As Jason Kravitt, the lead negotiator for BNY Mellon, testified on cross-examination:

> The way we wrote the Settlement Agreement is that it's the tranches who are most senior who suffered losses who get the cash first, therefore, the people who are holding subordinated and most subordinated tranches, likely, will not get any cash out of the settlement if the losses in the settlement went to any of the senior level tranches. So, if you made a bet on a subordinated tranche, this wouldn't necessarily get you any cash distributed out of the settlement. The way the cash is distributed would restore the face amount of some of this—or the face amount or the partial portion of the face amount of any lower seniority tranche, it might get some interest in a future period it might not otherwise get. ***But the recovery goes***

[22] The same logic applies not only to entirely written off junior certificates, but also to deeply discounted junior certificates like the ones Tilden Park and Prosiris hold. *See supra* note 12.

> ***first in line to the senior holders and then the next level and so on down to the bottom***.[23]

The testimony continued as follows:

> Q: You are aware of the waterfall that is being proposed?
>
> A: The waterfall is the distribution that is set out within the trust documents themselves. All we did is characterize how the payments would be—is characterize the payments within the various defined terms in the agreement and then the agreement tells you how to use those, and ***we also set in some rules to make sure that subordinate tranches didn't get money before senior tranches***.
>
> Q: That is my next point. You are aware that in all likelihood many tranches of investors, certificate holders in the lower tranches, will get nothing?
>
> A: Correct. Well, I wouldn't say "likelihood." I'm aware of the reasonable possibility that that will happen.[24]

This testimony only further confirms that the settlement distribution method advocated by Tilden Park and Prosiris is not only inconsistent with the text and intent of the Governing Agreements and the purpose of the overcollateralization and subordination structures, it is also inconsistent with the intent of the Settlement Agreement. The Court should reject it.

CONCLUSION

For the reasons set forth above, the undersigned investors respectfully request that the Court direct the Trustee to distribute the Allocable Shares to the Disputed Trusts by employing Intex's "Standard" Method, whereby the Trustee should calculate the Principal Distribution Amount in the Disputed Trusts based upon the "written-up" certificate principal balances, but

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[23] *See* Trial Transcript for July 12, 2013 at 1878:2-16, attached as Ex. D to Sheeren Aff. (emphasis added).

[24] *Id.* at 1879:5-18 (emphasis added).

distribute each Trust's Allocable Share among particular tranches based upon the pre-distribution certificate principal balances.[25]

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[25] The undersigned investors also join in the Trustee's and AIG's arguments opposing the creation of an artificial "Record Date" for the distribution as of February 2016.