

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

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In the matter of the application of

U.S. BANK NATIONAL ASSOCIATION,
WELLS FARGO BANK, NATIONAL
ASSOCIATION, WILMINGTON TRUST,
NATIONAL ASSOCIATION, WILMINGTON
TRUST COMPANY, AND CITIBANK, N.A. (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 Administration and Distribution of a Settlement
Payment,

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Index No. 651625/2018

Hon. Marcy S. Friedman

**OPENING MERITS BRIEF OF
AMBAC ASSURANCE
CORPORATION**

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Cole v. Macklowe,
99 A.D.3d 595 (1st Dep’t 2012)4

I. Introduction

Ambac Assurance Corporation (“Ambac”), the Certificate Insurer for certain classes of certificates (the “Insured Certificates”) issued by four trusts (LXS 2007-6; LXS 2007-10H; LXS 2007-15N; and LXS 2007-14H) (the “Ambac Trusts”)¹ at issue in this proceeding, respectfully submits this opening memorandum of law concerning the distribution of payments under the Settlement Agreement.²

The applicable Trust Agreements give Ambac the right to receive any Subsequent Recoveries that would otherwise be payable to the Insured Certificates, to the extent Ambac made claim payments for write-downs of those certificates. Additionally, the Court should direct the Petitioners not to write up Insured Certificates at all, and to exclude from the write-up of uninsured certificates those sums paid directly to Ambac.³

II. Ambac Is Entitled to Receive Subsequent Recoveries That Would Otherwise Be Payable to the Insured Certificates in the Ambac Trusts

The Trust Agreements for the Ambac Trusts include specific language addressing Ambac’s right to receive Subsequent Recoveries as compensation for its claim payments made due to write-downs of the Insured Certificates, which occur through the application of “Applied Loss Amounts.” This language appears in the definition of “Certificate Principal Amount,” and provides the following: “to the extent that any Applied Loss Amount was reimbursed under the Certificate Insurance Policy, any Subsequent Recovery otherwise payable on the Insured

¹ Ambac also appeared as Certificate Insurer of one additional trust, LXS 2007-17H. LXS 2007-17H is the subject of a severance order currently pending before the Court.

² Capitalized terms not defined herein have the meanings given to such terms in the Petition for judicial instructions under Article 77 (NYSCEF No. 1) or the relevant Governing Agreements.

³ In its initial submission (NYSCEF No. 62), Ambac took the position that the Petitioners should distribute the Settlement Payment within the Ambac Trusts using the Write-Up First method. Ambac does not take a position herein on whether Write-Up First or Pay First is required, but reserves the right to address positions taken by other interested parties.

Certificates shall instead be payable to the Certificate Insurer.” LXS 2007-6 Trust Agreement (Affidavit of Robert Tyrrell (“Tyrrell Aff.”) Ex. 1) § 1.01 (definition of “Certificate Principal Amount”).⁴ The claim payments made by Ambac for Applied Loss Amounts for the Insured Certificates are as follows:⁵

Trust	Insured Certificates	Claim Payments for Applied Loss Amounts
LXS 2007-6⁶	3-A1	\$26,680,125
	3-A2	\$12,219,695
	3-A3-1	\$7,894,625
	3-A3-2	\$8,965,531
	3-A4	\$10,699,585
	3-A5	\$10,606,621
	3-A7	\$53,450,595
LXS 2007-10H	1-A1-2	\$2,874,895
	1-A4-1	\$41,630,678
LXS 2007-14H	A2-2	\$82,203,334
	A4	\$50,949,449
LXS 2007-15N	3-A2	\$136,267,768
	4-A3	\$60,481,970

Ambac is entitled to receive the portion of the Allocable Shares that otherwise would be paid to the Insured Certificates in the Ambac Trusts, up to the amount of its claim payments for Applied Loss Amounts.

The portion of any given Allocable Share that would otherwise be paid to the Insured Certificates (but that is paid to Ambac instead) is determined by treating the Allocable Share as part of the “Principal Remittance Amount” that is paid according to the principal distribution waterfall set forth in each Trust Agreement. While the precise distribution sequence varies from

⁴ See also LXS 2007-10H Trust Agreement (Tyrrell Aff. Ex. 2) § 1.01 (same); LXS 2007-15N Trust Agreement (Tyrrell Aff. Ex. 3) § 1.01 (same); LXS 2007-14H Trust Agreement (Tyrrell Aff. Ex. 4) § 1.01 (same).

⁵ Tyrrell Aff. ¶¶ 3-6.

⁶ In addition to the figures reported for particular certificates in this transaction, Ambac paid \$1,117,825 in claims for Applied Loss Amounts before the tracking of these claim payments at the certificate level. Tyrrell Aff. ¶ 3.

trust to trust, the amount each certificate would receive depends on its Certificate Principal Amount.

III. Write-Ups Are Limited to Uninsured Certificates, and Cannot Include Amounts Paid Directly to Ambac

In connection with the distribution of the Allocable Shares, the Settlement Agreement contemplates a write-up of certain certificate balances.

In connection with the distribution of Plan Payments to Participating Trusts pursuant to Subsection 3.06(a), *to the extent permitted under each Trust's Governing Agreement*, the applicable Accepting Trustee, or the party responsible for calculating certificate balances pursuant to the terms of the Governing Agreements of a given Participating Trust, will apply the amount of the Plan Payment for that Trust to increase the balance of securities within that Trust (other than any class of REMIC residual interests) in the reverse order of previously allocated losses, as though such Plan Payment was a subsequent recovery.)

Settlement Agreement (NYSCEF No. 3) § 3.06(b) (emphasis added). This language makes clear that write-ups occur only to the extent permitted under the Governing Agreements.

In the Ambac Trusts, the amount of any write-up due to Subsequent Recoveries is determined by the definition of "Certificate Principal Amount." That definition provides, in relevant part, that the Certificate Principal Amount is written up by "the lesser of (1) any Deferred Amount for each such Class immediately prior to such Distribution Date and (2) the total amount of any Subsequent Recovery distributed on such Distribution Date to such Certificateholders." LXS 2007-6 Trust Agreement § 1.01.⁷ Thus, the definition of "Certificate Principal Amount" imposes two separate limitations on the write-ups that can occur.

First, by specifying that the write-up cannot exceed the "Deferred Amount," this definition effectively prevents the write-up of Insured Certificates as long as Ambac pays all

⁷ See also LXS 2007-10H Trust Agreement § 1.01; LXS 2007-14H Trust Agreement § 1.01; LXS 2007-15N Trust Agreement § 1.01.

claims for Applied Loss Amounts. That is because the definition of Deferred Amount provides that “any Applied Loss Amount allocated to any Insured Certificates will not be considered a Deferred Amount to the extent such amounts are paid by the Certificate Insurer as part of an Insured Distribution.” *Id.* Because Ambac has paid holders of Insured Certificates for all Applied Loss Amounts, the Deferred Amount for the Insured Certificates should be zero, meaning there can be no write-up of the Insured Certificates.⁸

Second, the Governing Agreements do not permit the write-up of *any certificates* by the Subsequent Recoveries Ambac receives because the Certificate Principal Amount is written up only by the amount “*distributed . . . to such Certificateholders.*” *See* LXS 2007-6 Trust Agreement § 1.01 (emphasis added).⁹ Here, settlement funds distributed to Ambac are not paid to such Certificateholders and are therefore excluded from any write-up.¹⁰ This limitation is sensible because, unlike payments to certificateholders, settlement amounts paid directly to Ambac do not pay down the balance of any class of certificates. Accordingly, there is no need for an offsetting write-up of certificate balances by this sum. If any certificate balances were written up by sums paid to Ambac, it would cause a discrepancy between the certificate balances and the collateral balances in the trust, which would only create further Applied Loss Amounts, requiring additional write-downs. This would be an unintended and absurd result because payment of settlement funds should not trigger further write-downs. *See Cole v. Macklowe*, 99 A.D.3d 595, 595 (1st Dep’t 2012) (“[A] contract should not be interpreted to produce an absurd

⁸ *See* Tyrrell Aff. ¶ 7.

⁹ *See also* LXS 2007-10H Trust Agreement § 1.01; LXS 2007-14H Trust Agreement § 1.01; LXS 2007-15N Trust Agreement § 1.01.

¹⁰ This second restriction on write-ups provides an independent reason why Insured Certificates will not be written up. Here, Ambac’s claim payments for Applied Loss Amounts exceed the settlement payments that the Insured Certificates would otherwise receive as Subsequent Recoveries, so there will be no payments to the holders of Insured Certificates. In the absence of such a payment, the Insured Certificates cannot be written up.

result, one that is commercially unreasonable, or one that is contrary to the intent of the parties.”).

IV. Conclusion

For these reasons, the Court should instruct and authorize the Petitioners to pay to Ambac any distributions of the Allocable Shares that would otherwise be due to the Insured Certificates based on their Certificate Principal Amounts to the extent of Ambac’s claim payments for Applied Loss Amounts thereon, instruct the Petitioners not to write up the balances of the Insured Certificates at all, and to exclude from the write-ups of uninsured certificates any amounts that Ambac receives.

Date: October 19, 2018

By:

/s/ Henry J. Ricardo

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