APL-2020-00126
New York County Clerk's Index No. 651854/2014

Court of Appeals

of the

State of New York

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006,

Plaintiff-Appellant,

— against —

DB STRUCTURED PRODUCTS, INC.,

Defendant-Respondent.

BRIEF FOR *AMICI CURIAE* THE NATIONAL CREDIT UNION ADMINISTRATION BOARD AND FREEDOM TRUST 2011-2 IN SUPPORT OF PLAINTIFF-APPELLANT

John A. Libra
Korein Tillery LLC
205 North Michigan Avenue
Suite 1950
Chicago, Illinois 60601
Tel.: (312) 641-9750
Fax: (312) 641-9751

Attorneys for the National Credit Union Administration Board as Liquidating Agent

Peter W. Tomlinson
David S. Kleban
Jeffrey F. Kinkle
Patterson Belknap Webb & Tyler LLP
1133 Avenue of the Americas
New York, New York 10036-6710
Tel.: (212) 336-2400
Fax: (212) 336-2000

Attorneys for Freedom Trust 2011-2

March 4, 2022

CORPORATE DISCLOSURE STATEMENT
PURSUANT TO RULE 500.1(f)

Amicus Freedom Trust 2011-2 is a Delaware statutory trust. It does not have any parents, subsidiaries, or affiliates.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

STATEMENT OF INTEREST OF AMICI CURIAE 1

PRELIMINARY STATEMENT 4

BACKGROUND 5

A. Features of RMBS Trust Governance Pertaining to Repurchase Actions 5

B. Practical Obstacles to Trustee Repurchase Suits 7

C. No-Action Clauses and Certificateholder Derivative Standing 9

ARGUMENT 12

I. The Question Presented in This Appeal Is Not Answered by Reliance 12

II. No Policy Is Served by the Holding Below 13

CONCLUSION 16

TABLE OF AUTHORITIES

Page(s)

Cases

ACE Sec. Corp. v. DB Structured Prods., Inc., 112 A.D.3d 522 (1st Dep't 2013), *aff'd on other grounds*, 25 N.Y.3d 581 (2015) 10, 11

Campbell v. Hudson & M. R. Co., 277 A.D. 731 (1st Dep't 1951), *aff'd*, 302 N.Y. 902 (1951) 11

Deutsche Bank Nat'l Tr. Co. v. Barclays Bank PLC, 34 N.Y.3d 327 (2019) 6

Gaines v. City of New York, 215 N.Y. 533 (1915) 15

Malay v. City of Syracuse, 25 N.Y.3d 323 (2015) 14

Phoenix Light SF Ltd. v. Deutsche Bank Nat'l Trust Co., No. 14-cv-10103-JGK (S.D.N.Y. Aug. 14, 2015) 6, 13

Rapid Transit Subway Constr. Co. v. City of New York, 259 N.Y. 472 (1932) 12

Reliance Ins. Co. v. PolyVision Corp., 9 N.Y.3d 52 (2007) 12, 13

Royal Park Invs. SA/NV v. Deutsche Bank Nat'l Tr. Co., No. 14-cv-4394, 2017 WL 1331288 (S.D.N.Y. Apr. 4, 2017) 6

U.S. Bank Nat'l Ass'n v. DLJ Mortg. Capital, Inc., 33 N.Y.3d 72 (2019) 13

United States v. Bestfoods, 524 U.S. 51 (1998) 12

Statutes

12 U.S.C. § 1752a(a) 1

12 U.S.C. § 1754 ... 1

12 U.S.C. § 1766 ... 2

12 U.S.C. § 1781 ... 1

12 U.S.C. § 1783 ... 1

12 U.S.C. § 1784 ... 1

12 U.S.C. § 1786(h) ... 2

12 U.S.C. § 1787 ... 2

Other Authorities

CPLR 205(a) ... *passim*

CPLR 305(b) ... 14

CPLR 306(b) ... 14

The National Credit Union Administration Board as Liquidating Agent ("NCUA") and Freedom Trust 2011-2 ("Freedom Trust" and, together with NCUA, the "Investor Amici") respectfully submit this brief in support of Plaintiff-Appellant ACE Securities Corp. Home Equity Loan Trust, Series 2006-SL2, by HSBC Bank USA, National Association, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006 (the "Trustee"). As discussed below, the Investor Amici urge the Court to reverse the Order of the Appellate Division, First Judicial Department, dated November 19, 2019, which affirmed dismissal of Plaintiff-Appellant's claims against Defendant-Appellee DB Structured Products, Inc. ("DBSP").

STATEMENT OF INTEREST OF AMICI CURIAE

The National Credit Union Administration is an independent federal agency responsible for chartering and regulating federal credit unions, regulating federally insured state credit unions, and administering the National Credit Union Share Insurance Fund (the "Fund"). *See* 12 U.S.C. §§ 1752a(a), 1754, 1781, 1783-1784. The Fund protects the deposits of nearly 92 million account holders. They are financed by insured credit unions and backed by the full faith and credit of the United States. *See id.*; *id.* § 1782(c). When an insured credit union is in danger of failing, the NCUA Board may step in as conservator—and, if necessary, liquidating agent—to preserve and conserve the credit union's assets, and thereby minimize losses and risks to the Fund and to other claimants against the credit union. *See id*. §§ 1766, 1786(h), 1787.

NCUA's[1] interest in litigation over residential mortgage-backed securities ("RMBS") stems from its role as liquidating agent for four large corporate credit unions that failed in 2010. The Credit Unions were major financial institutions that offered short-term liquidity and a variety of financial services to other credit unions. They failed in part because of losses sustained by purchasing RMBS—purchases that had been represented as extremely safe investment-grade, triple-A-rated RMBS, but that, by the time NCUA became conservator of the Credit Unions, had suffered enormous losses.

To offset the Credit Unions' losses, and to make the Fund as a claimant whole for amounts it had been required to pay to protect the Credit Unions' depositors, NCUA sponsored a series of resecuritization transactions that issued NCUA Guaranteed Notes ("NGNs").[2] NCUA transferred into the NGNs hundreds of securities similar to the ones at issue in this case, although it has no ownership interest in the ACE Securities Corp. Home Equity Loan Trust, Series

[1] For convenience, from this point forward, this brief uses the abbreviation "NCUA" to refer solely to the agency's Board in its capacity as conservator or liquidating agent (distinct from the agency's capacity as regulator) unless the context indicates otherwise. As relevant to this case, NCUA is liquidating agent for U.S. Central Federal Credit Union, Western Corporate Federal Credit Union, Members United Corporate Federal Credit Union, and Southwest Corporate Federal Credit Union (collectively, the "Credit Unions").

[2] Timely repayment of principal and interest to the investors in NGNs is guaranteed by the NCUA, in its agency capacity, and is backed by the full faith and credit of the United States.

2006-SL2 (the "Trust") addressed here. The resecuritization transactions have now matured, and NCUA is the holder of many certificates whose value may be materially affected by the outcome of this case and the ability of RMBS trustees, in general, to pursue claims against RMBS originators and sponsors.

Freedom Trust is a Delaware statutory trust. Freedom Trust's holdings include RMBS similar to those at issue in this appeal. Freedom Trust does not own any certificates issued by the Trust at issue here, but owns other RMBS certificates that could be affected by the Court's resolution of the legal question presented in this appeal.

The Investor Amici submit this brief to draw to the Court's attention certain considerations that are not addressed by the parties, but which are necessary to understand the context of this appeal.[3] For example, DBSP argues that the Court should affirm because the First Department's ruling serves the interests of New York public policy by denying the benefit of CPLR 205(a) to insufficiently "diligent" plaintiffs. Def.-Respondent Br. at 50. As set forth below, this argument mischaracterizes the situation and ignores important dynamics affecting the prosecution of claims on behalf of RMBS trusts. The Investor Amici—parties with diverse interests in RMBS that have at times taken active roles in the management

[3] The Court previously accepted a brief by the Investor Amici in support of the Plaintiff-Appellant's motion for leave to appeal. Court of Appeals Decision List, Sept. 1, 2020, Mo. No. 2020-336.

of repurchase litigation—are in a position to illuminate those dynamics, which often operate outside of the Court's view.

PRELIMINARY STATEMENT

There is no legitimate dispute that the Trust at issue was saddled with thousands of mortgage loans as to which DBSP breached its contractual representations and warranties. The massive scale of misconduct by entities like DBSP has been well documented and need not be recounted here. Nor is there any dispute that, prior to the expiration of the statutory limitation period, DBSP was given notice of an action on the Trust's behalf to enforce DBSP's repurchase obligations.

The question is whether DBSP will escape liability thanks to the First Department's unduly narrow construction of CPLR 205(a), which withheld the statute's benefit from the Trustee in this revival action. However, it is not the Trustee, but the investors—the beneficiaries of the Trust named in the case caption—who will be harmed if that construction is not corrected.

The Investor Amici agree with the doctrinal arguments presented by the Trustee, but write separately to offer important context regarding structural dynamics that sometimes lead to derivative suits being filed within the limitations period by RMBS trust beneficiaries instead of by the trustees themselves. With these dynamics in mind, it is clear that DBSP's accusations of insufficient "diligence" are unwarranted and that no policy of the State is served by the holding in the court below.

BACKGROUND

A. Features of RMBS Trust Governance Pertaining to Repurchase Actions

As the Court is aware, RMBS certificates were frequently issued to investors by New York common law trusts. These certificates entitle the investors (or "certificateholders") to distributions of income the trust receives as homeowners make payments on the underlying mortgage loans. RMBS investors are diverse and include credit unions, life insurance companies, pension funds, and large institutional investors managing assets for clients such as universities.

Most RMBS trusts (including the Trust at issue here) are governed by pooling and servicing agreements. Among other things, these instruments describe the duties and powers of the trustee, which administers the trust. A trustee, although it has no economic interest in the trust assets, holds legal title to the underlying mortgage loans "for the benefit of the Certificateholders." *E.g.* R.131 (PSA § 2.01).

Typically, the trustee is empowered to enforce the loan repurchase obligations of the securitization sponsor and/or mortgage loan originators who made representations and warranties—a crucial backstop to the represented quality of the loans. But trustees assert that (except in situations involving an "event of default") they have no fiduciary obligations to the certificateholders and are not required to prosecute litigation claims on behalf of a trust unless they are (i) directed to do so by investors with a threshold percentage (typically 25% or more) of the "voting rights" in the trust and (ii) indemnified against the expenses and liabilities the trustee could incur in following that direction. Consistent with that position, trustees almost always decline to take enforcement actions unless these conditions are met.[4]

"Voting rights" are usually allocated pro rata based on the outstanding balances of the certificates. It is uncommon for a single investor to control 25% or more of the voting rights in an RMBS trust (which would typically require hundreds of millions of dollars in holdings) and there is no trust mechanism by which certificateholders can identify one another to join forces. *Cf. Deutsche Bank Nat'l Tr. Co. v. Barclays Bank PLC*, 34 N.Y.3d 327, 338 (2019) (recognizing the consensus that certificateholders are "geographically scattered" and that their residences do not provide a "workable basis" for determining place of economic injury); *Royal Park Invs. SA/NV v. Deutsche Bank Nat'l Tr. Co.*, No. 14-cv-4394, 2017 WL 1331288, at *6 (S.D.N.Y. Apr. 4, 2017) (denying certification of proposed class of RMBS certificateholders because, inter alia, certificates are "traded over-the-counter among entities located in more than ten different

---

[4] *See*, *e.g.*, Br. i.s.o. Mot. to Dismiss Second Am. Compl. at 7-8., Dkt. 36, *Phoenix Light SF Ltd. v. Deutsche Bank Nat'l Trust Co.*, No. 14-cv-10103-JGK (S.D.N.Y. Aug. 14, 2015).

countries through geographically dispersed broker-dealers located in various parts of the world" and the nature of "ownership recordation presents hurdles even to identifying *current* Certificate holders").

B. Practical Obstacles to Trustee Repurchase Suits

The factors described above create substantial obstacles to the investigation of breaches and the initiation of repurchase suits on behalf of RMBS trusts. Providing the trustee with a direction and indemnity (a "D&I") as described above is onerous: it creates a contractual entanglement that can last the entire litigation (which in these matters is lengthy and complex) and imposes a significant financial undertaking. At the same time, there is a mismatch between these burdens, which directing holders bear alone, and the benefits of successful repurchase litigation, which are diffused among investors in a given trust.

The impediments to D&I agreements between investors and their representative trustees are exacerbated by coordination problems. RMBS certificates are traded in largely anonymous, over-the-counter markets where trades are often matched by brokers. While coalitions are sometimes formed to achieve the "voting rights" threshold, such a process takes time and significant effort and expense. Often, the opacity of investors' holdings makes collective action to meet the threshold impracticable or even impossible. Furthermore, some institutional investors are not able to enter D&I agreements at all due to their own governance structures.

Meanwhile, negotiations between investors and trustees regarding the terms of a direction and indemnity are frequently challenging and protracted. RMBS trustees have no stake in the performance of the certificates and no economic incentive to prosecute the actions—and, as noted above, typically view themselves as having no obligation to investigate potential breaches or file suit. They therefore negotiate aggressively for D&I agreements that are maximally protective to themselves.

Making matters worse, certificateholders cannot easily obtain copies of documentation associated with the origination of the mortgage loans, which is necessary to perform a complete forensic investigation into breaches of loan-level representations and warranties. Unlike the trustees (*e.g.* R.131 (PSA § 2.01)), certificateholders have no direct contractual right to the loan files. The process of requesting and gaining access to those loan files is yet another obstacle to the prosecution of repurchase claims.

Representation and warranty obligors, like DBSP, have fully exploited these many obstacles to enforcement of claims on behalf of RMBS trusts to avoid being accountable for liabilities on thousands of trusts and hundreds of billions of dollars.

The practical result of these various impediments is that a D&I agreement is sometimes not fully executed before the statute of limitations on the repurchase claim expires. In certain of those cases, certificateholders have filed suit derivatively for the benefit of all investors before the end of the limitation period. (In many more cases, the trusts' claims simply expired.) These derivative actions put the defendants on notice of the repurchase claims prior to the expiration of the statute of limitations. But some of them have been found procedurally defective due to the certificateholder's failure to satisfy a "no-action" clause in the governing documents, as discussed further below.

C. No-Action Clauses and Certificateholder Derivative Standing

RMBS trust instruments often contain provisions called "no-action" clauses that restrict certificateholders' entitlement to file lawsuits related to the trust. There are weighty issues—not yet addressed by this Court and not raised in this appeal—concerning the application of these no-action provisions in specific cases. The circumstances under which an RMBS certificateholder may sue derivatively on behalf of the securitization trust have been the subject of litigation, including between the parties to this appeal. Here, the applicable no-action clause provides:

> No Certificateholder shall have any right by virtue of any provision of this Agreement to institute any suit, action or proceeding in equity or at law upon or under or with respect to this Agreement, unless such Holder previously

> shall have given to the Trustee *a written notice of default and of the continuance thereof*, as hereinbefore provided, and unless also the Holders of Certificates entitled to at least 25% of the Voting Rights shall have made written request upon the Trustee to institute such action . . . .

R.225 (PSA § 12.03) (emphasis added). In the action that preceded this "revival" suit, the parties disputed whether the DBSP's breaches of its representations and warranties about the mortgage loans constituted the kind of "default" that could satisfy the no-action clause and entitle a certificateholder to sue derivatively. The First Department answered in the negative, holding that only a "default" pertaining to "failures of performance by the servicer or master servicer" would have sufficed. *ACE Sec. Corp. v. DB Structured Prods., Inc.*, 112 A.D.3d 522, 523 (1st Dep't 2013) ("*ACE I*"), *aff'd on other grounds*, 25 N.Y.3d 581 (2015). In reaching that holding (which was not reviewed by this Court), the Appellate Division appears to have conflated the uncapitalized term "default" in the no-action clause with defined terms elsewhere in the agreement; it is the *latter* that pertains expressly to the servicer's and master servicer's conduct.[5]

Whether or not it correctly construed the no-action clause at issue here, *ACE I* illustrates that the effect of a no-action clause in any particular case will depend on the factual circumstances and contract language. And in any event,

---

[5] *Compare* R.225 (PSA § 12.03) (no-action clause referring to "default[s]") *with* R.205-208 (PSA §§ 8.01(a) and 8.01(b)) (defining "Servicer Event of Default" and "Master Servicer Event of Default," respectively).

the Appellate Division accurately recognized that a no-action clause is not a wholesale bar on derivative suits by certificateholders; rather, it imposes "a condition precedent to such an action." *ACE I*, 112 A.D.3d at 523. Furthermore, First Department caselaw has long established that a no-action clause will not be enforced where the indenture trustee, by "abdicating its function with respect to the point in question, declines to act at all." *Campbell v. Hudson & M. R. Co.*, 277 A.D. 731, 734-35 (1st Dep't 1951), *aff'd*, 302 N.Y. 902 (1951). In such a case, "bondholders for themselves and others similarly situated may bring a derivative action in the right of the trustee, rather than in their own individual rights as bondholders." *Id.*

Thus, while RMBS trust documents frequently impose *conditions* on a investors' capacity to sue, they do not by any means render the certificateholder a "stranger" to the litigation interests of the securitization trust.

Here, it has been found that the certificateholders that first asserted the claims at issue in this case failed to satisfy the applicable conditions precedent to commencing a derivative suit. Now the trustee—unencumbered by the restrictions imposed by the "no action" clause—seeks to revive the same claims, for the benefit of the same entities (the trust and its certificateholders), in a suit pursuant to CPLR 205(a).

ARGUMENT

I. The Question Presented in This Appeal Is Not Answered by *Reliance*

It is worth repeating: the claims asserted in the initial derivative suit and in the Trustee's revival suit are the same. Both actions are brought in the name and for the benefit of the same entity—the Trust. And, had the initial suit not been found defective, any recovery would have benefitted the Trust and the certificateholders in the same exact way as a recovery in the revival suit.

Whether, under these circumstances, CPLR 205(a) is available in the revival suit was not answered by this Court's decision in *Reliance*. There, the benefit of CPLR 205(a) was withheld from a corporation seeking to revive a claim for breach of contract originally asserted by its subsidiary, which was not a party to the contract at issue. *Reliance Ins. Co. v. PolyVision Corp.*, 9 N.Y.3d 52 (2007). That holding was consistent with the longstanding judicial recognition of legal separation between affiliated corporations. *See*, *e.g.*, *Rapid Transit Subway Constr. Co. v. City of New York*, 259 N.Y. 472, 487-88 (1932); *United States v. Bestfoods*, 524 U.S. 51, 61 (1998) ("It is a general principle of corporate law deeply ingrained in our economic and legal systems that a parent corporation . . . is not liable for the acts of its subsidiaries.") (citations and internal quotation marks omitted). Just as corporate affiliates are ordinarily not liable for one another's wrongdoing, neither can they assert one another's claims.

The problem with the original action in *Reliance* was therefore not a procedural or technical defect in the plaintiff's "standing" (for that term was never used in the opinion), but that the suit was brought in the name of an entity with no substantive interest in the contract. *See* 9 N.Y.3d at 56 (previous action was "dismissed for naming the wrong plaintiff"). Here, the Trust *was* named in the original action, just as it is named in the revival action. Only the representative suing on its behalf has changed. The certificateholder's derivative suit was dismissed for failure to satisfy the no-action clause—a *procedural* condition to suit. The failure of such a condition in the original suit does not foreclose the later use of CPLR 205(a) under this Court's precedents. *See U.S. Bank Nat'l Ass'n v. DLJ Mortg. Capital, Inc.*, 33 N.Y.3d 72, 80-82 (2019).

II. No Policy Is Served by the Holding Below

DBSP frames the First Department's decision as just desserts for a purported lack of "diligence," and as serving the policy objectives of CPLR 205(a). *See* Def.-Appellee Br. at 50. Not so. The discussion above should illustrate the significant impediments to trustee repurchase suits not present in traditional litigation. The Court must not infer an "unwillingness" (*id.*) by the parties in interest to prosecute claims simply because the initial suit was filed by investors and not the Trustee. The *Trust* timely asserted its claims, but did so in a faulty procedural vehicle where a condition precedent to suit had not been met. That condition has nothing to do with the merits of the claims, and is imposed in a governing trust document, the PSA, to which DBSP is not even a party. This Court has consistently construed the "broad, remedial" policy of CPLR 205(a) to embrace circumstances just like these.

Nor does denying the Trustee the benefit of CPLR 205(a) provide it any incentive for haste. As noted above, RMBS trustees' fortunes are not tied to the performance of the trust or its litigation recoveries. The First Department's decision adversely affects only the investors injured by DBSP's failure to repurchase defective loans, for whose benefit both lawsuits were commenced.

Lawsuits by certificateholders in these circumstances, even when ultimately found defective, serve the aims of the statute of limitations and of CPLR 205(a) by "putting defendants on notice of the claims" within the limitation period. *Malay v. City of Syracuse*, 25 N.Y.3d 323, 329 (2015).[6] They also present the only meaningful avenue for recovery for most investors. Suits against the *trustees* for failure to commence timely actions may themselves be time-barred (absent some form of tolling agreement), and in any event would be met with a defense that the trustee was under no obligation to sue. Meanwhile, federal securities laws provide

[6] New York has a long tradition of allowing plaintiffs to start a lawsuit purely for the purpose of preventing claims from becoming time-barred, so long as the defendant is given notice of their general nature. A plaintiff may commence an action for purposes of the statute of limitations by filing a summons accompanied only by a short "notice," *see* CPLR 305(b), and may serve those papers as many as 120 days later, *id.* 306-b, (Alexander, McKinney Practice Commentary, C306:1).

inadequate recourse. The reason for the ubiquity in RMBS transactions of representations and warranties, and of the corresponding repurchase remedy, is that they provide a specified recovery for the collective benefit of the trust. The securities laws do not allow investors to leverage that centralized mechanism, instead requiring costly litigation about the circumstances of each individual investor.

It is particularly audacious for DBSP to invoke the "policies" of this State in attempting to secure for itself the windfall of not having to answer for its prolific misconduct. Let us not forget why we are here: DBSP agreed to a repurchase mechanism designed to be the primary remedy for breaches of representations and warranties. When the pervasive nature of their breaches was revealed, DBSP and other sponsors abandoned that commitment, refused to comply with the contractual remedy, and forced investors to engage in onerous, protracted, and expensive litigation. The investors had no choice but to investigate the trusts' claims on their own and to try to negotiate D&Is with their representative trustees. For the reasons described above, those negotiations were not finalized before the end of the six-year limitation period.

Judge Cardozo's warning against an unduly "narrow construction" of CPLR 205(a), *Gaines v. City of New York*, 215 N.Y. 533, 539 (1915), is particularly poignant in these circumstances, where the effect of such a construction would be to absolve the architects of the worst man-made financial crisis in a generation from adhering to their agreements. Such a result is not commanded by any precedent and would not serve any policy.

CONCLUSION

For the foregoing reasons, the Investor Amici join with Plaintiff-Appellant in respectfully requesting that the Court reverse the Appellate Division's decision.

Dated: March 4, 2022
New York, New York

PATTERSON BELKNAP WEBB & TYLER LLP

Peter W. Tomlinson
David S. Kleban
Jeffrey F. Kinkle
1133 Avenue of the Americas
New York, New York 10036
(212) 336-2000
pwtomlinson@pbwt.com
dkleban@pbwt.com
jkinkle@pbwt.com

Attorneys for Freedom Trust 2011-2

KOREIN TILLERY LLC

John A. Libra
205 North Michigan Avenue
Suite 1950
Chicago, Illinois 60601
(312) 641-9750
jlibra@koreintillery.com

Attorneys for the National Credit Union Administration Board as Liquidating Agent

CERTIFICATION

Pursuant to 22 N.Y.C.R.R. §500.13(c)(1), I certify that the total word count for all printed text in the body of this brief, exclusive of any statement of the status of related litigation, corporate disclosure statement, table of contents, table of cases and authorities, statement of questions presented required by subsection (a) of this section, and any addendum containing material required by subsection 500.1(h), is 3,614 words.

Dated: April 21, 2022
New York, New York

PATTERSON BELKNAP WEBB &
TYLER LLP

____

Peter W. Tomlinson
1133 Avenue of the Americas
New York, New York 10036
(212) 336-2000
pwtomlinson@pbwt.com

Attorney for Freedom Trust 2011-2