Commonwealth Advisors, Inc. v Wells Fargo Bank, N.A.
2017 NY Slip Op 30622(U)
March 31, 2017
Supreme Court, New York County
Docket Number: 652112/2015
Judge: Shirley Werner Kornreich
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 54

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COMMONWEALTH ADVISORS, INC.,

Plaintiff,

-against-

WELLS FARGO BANK, NATIONAL ASSOCIATION, and COLLYBUS CDO I, LTD.,

Defendants,

-and-

AG MORTGAGE VALUE PARTNERS MASTER FUND, L.P., AG MVP PLUS SG III, L.P., and AG SECURITIZED ASSET RECOVERY FUND, L.P.,

Intervenor-Defendants.

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Index No.: 652112/2015

DECISION & ORDER

SHIRLEY WERNER KORNREICH, J.:

Motion sequence numbers 002 and 003 are consolidated for disposition.

Intervenor-Defendants AG Mortgage Value Partners Master Fund, L.P., AG MVP Plus SG III, L.P., and AG Securitized Asset Recovery Fund, L.P. (collectively, the Funds)[1] move, pursuant to CPLR 3211, to dismiss the amended complaint (the AC). Seq. 002. Defendant Wells Fargo Bank, National Association (Wells Fargo or the Trustee) separately moves to dismiss the AC on grounds substantially similar to those raised by the Funds. Seq. 003. Plaintiff Commonwealth Advisors, Inc. (Commonwealth) opposes the motions. For the reasons that follow, the motions are granted in part and denied in part.

[1] By order dated November 28, 2016 (Dkt. 48), the court granted the Funds' unopposed motion for leave to intervene, which was supported with a proposed pleading bearing the caption appearing at the top of this decision. *See* Dkt. 11. Below, the Clerk is directed to amend the caption accordingly, and the Funds are directed to serve and file their proposed answer in intervention, which contains cross-claims and counterclaims. *See id.* at 29-32. References to "Dkt." followed by a number refer to documents filed in this action on the New York State Courts Electronic Filing system (NYSCEF).

I. Factual Background & Procedural History

As this is a motion to dismiss, the facts recited are taken from the AC (*see* Dkt. 2) and the documentary evidence submitted by the parties.

Commonwealth is the collateral manager for defendant Collybus CDO I Ltd. (Collybus or the Issuer),[2] a special purpose vehicle incorporated in the Cayman Islands that issued a collateralized debt obligation (the CDO).[3] A Collateral Management Agreement (the CMA) (Dkt. 9) governs Commonwealth's role as collateral manager, and an indenture (the Indenture) (Dkt. 10) governs the rights of the holders of the notes issued by the CDO.[4] Both agreements are dated as of November 9, 2007 and are governed by New York law. Wells Fargo is the indenture

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[2] Collybus has not appeared in this action.

[3] The court assumes familiarity with the structure of CDOs and the role of a CDO collateral manager. Suffice it to say that a collateral manager has contractual and fiduciary duties of care and loyalty to the CDO (subject, here, to certain fiduciary duty waivers [*see* Dkt. 9 at 13-16]) that generally require the collateral manager to put the interests of the CDO ahead of its own. *See, e.g., id.* at 6 ("The Collateral Manager shall cause any purchase or sale of any Collateral Debt Security or Eligible Investment to be conducted on arm's length terms in accordance with reasonable and customary business practices and in compliance with applicable laws and, in the case of any purchase or sale between the Issuer and the Collateral Manager, any Affiliate thereof any accounts managed by the Collateral Manager and/or its Affiliates, such purchases or sales are made on a basis no less favorable, taken as a whole, than would be obtained in a similar transaction with an unaffiliated third party and are otherwise consistent with applicable law and this Agreement."). This is relevant to the reasonable reliance issue since, as explained herein, Commonwealth cannot claim reasonable reliance on Wells Fargo's promises to indemnify legal fees upon a sale of the CDO's collateral because Commonwealth had a duty to sell the collateral if it was in the best interest of the CDO, regardless of whether it was going to receive the requested indemnification. *See* Dkt. 22 at 9 ("there could be no causal connection between the alleged representation and [Commonwealth's] decision to liquidate the [CDO's] assets because, by [Commonwealth's] own admission, its decision to liquidate was dictated by its assessment of the best interests of the [the CDO's] investors, not its own pecuniary interest in recouping expenses.").

[4] It should be noted that section 21 of the CMA provides that if any term of the CMA conflicts with a term of the Indenture, the Indenture controls. *See* Dkt. 9 at 25.

trustee. The Funds are some of the CDO's noteholders (they claim to be "beneficial holders of a significant percentage of Collybus's Class A-2 Notes."). *See* Dkt. 11 at 19.

The Securities and Exchange Commission (the SEC) and others have filed lawsuits against Commonwealth and its principal, non-party Walter A. Morales. *See, e.g.*, Dkt. 37 (complaint in *SEC v Commonwealth Advisors, Inc.*, No. 12-cv-700 (MD La)); *see also Broyles v Cantor Fitzgerald & Co.*, 2013 WL 1681150 (MD La 2013) (civil action against Commonwealth and Moreno by investors in Commonwealth managed funds).[5] The SEC has alleged:

> Since at least 2007, Commonwealth, a Louisiana investment adviser and Morales, its principal, engaged in a scheme to hide losses in certain hedge funds they advised. These losses were realized, in part, from significant investments that the funds held in residential mortgage-backed securities ("RMBS") which had deteriorated in value during the recent downturn in the residential housing market. To hide these losses, Defendants executed improper trades across the funds ("cross-trades") that benefitted certain clients at the expense of other clients. Defendants also made materially false representations to investors about the amount and value of, as well as the process for valuing certain mortgage-backed assets held in the funds and fabricated internal documents to justify the false valuations.
>
> ...
>
> In addition to serving as an investment adviser to individual investors and the hedge funds, Commonwealth became the collateral manager to a [CDO] known as [Collybus] on November 9, 2007. Commonwealth participated in creating Collybus along with an investment bank [] that contributed assets to the CDO and served as the lead structurer, placement agent, and arranger for Collybus. Defendants participated in forming Collybus, in part, by removing failing RMBS from certain Commonwealth funds and selling the impaired securities to Collybus to be included in the CDO portfolio. Investors in Collybus purchased notes that paid a return so long as the assets that comprised the portfolio continued to perform. The return on the Collybus notes was dependent upon the performance

[5] Both actions appear to be ongoing. The most recent opinion in the SEC action was issued on January 11, 2017. *See SEC v Commonwealth Advisors, Inc.*, 2017 WL 107974 (MD La 2017). While the court focuses on the SEC action herein, it should be noted that the *Broyles* action has been the subject of at least 20 judicial opinions, the most recent of which appears to have been issued on September 8, 2016. *See Broyles v Cantor Fitzgerald & Co.*, 2016 WL 4718150, at *1 (MD La 2016).

> of the RMBS and other asset-backed securities that comprised the Collybus portfolio.

See Dkt. 37 at 1, 6. When the RMBS market deteriorated,[6] the SEC claims that:

> Rather than disclose the losses, Commonwealth and Morales engaged in a scheme to hide them from investors. This scheme included removing declining RMBS from Commonwealth-advised accounts and funds ... by selling the impaired securities to Collybus.

See id. at 8. The Funds further explain:

> The actions allege a broad range of misconduct, including defrauding investors in those other funds by concealing losses that those funds had incurred. One of the ways that Commonwealth is alleged to have concealed those losses is through selling deteriorated RMBS to Collybus at backdated prices and then using the proceeds the funds received from those off-market sales to purchase Collybus notes. Through this scheme, Commonwealth is alleged to have masked the existence of losses through replacing direct investments in deteriorated RMBS that needed to be "marked to market" with indirect investments in the same collateral through Collybus notes that could be recorded at higher prices because they were "marked to model."

See Dkt. 20 at 11 (the Funds also contend that "[w]hile Collybus was [] referenced in these litigations, the substance of the claims concerned Commonwealth's duties to its managed funds, not its Collybus-related duties, which are not the source of any of the claims asserted in those actions."). The SEC's complaint alleges a litany of other misconduct, which is not repeated here.[7]

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[6] Familiarity with RMBS, RMBS backed CDOs, and the effect of the financial crisis on such investments is presumed.

[7] The federal district court (deGravelles, J.) explained:

> On November 8, 2012, the [SEC] sued [Commonwealth and Morales] for fraud in connection with their management of several hedge funds. It is alleged that the hedge funds heavily invested in [RMBS] which, when the investments began to falter during the financial crisis of 2007 and 2008, caused Defendants to orchestrate an elaborate, multifaceted, and fraudulent scheme to hide losses and conceal the truth of those losses from investors. In a more recent filing, Plaintiff summarizes the alleged scheme as follows:

In this action, Commonwealth seeks indemnification of the legal fees it incurred (and continues to incur) in these lawsuits. While Morales' misconduct may ultimately prove to be a ground to deny him the legal fees Commonwealth seeks in this action, the parties agree that adjudication of such misconduct is a fact-laden issue that is inappropriate for resolution on this motion to dismiss.[8]

Commonwealth's reimbursement rights are addressed in both the CMA and Indenture. Thus, as discussed herein, the only issue on this motion is interpretation of the applicable waterfall provisions in the Indenture. Section 5 of the CMA, titled "Expenses of the Collateral Manager", sets forth eight categories of expenses for which the CDO must reimburse Commonwealth. *See* Dkt. 9 at 10-11. As applicable here, section 5(iv) provides for "reimbursement of reasonable fees and disbursements of employing outside counsel incurred by

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> Defendants carried out the scheme by (1) transferring distressed RMBS bonds to a hard-to-value [CDO] at inflated prices to conceal declines in the RMBS' market value; (2) transferring massive amounts of the fraudulently overvalued CDO to a Commonwealth-managed fund, despite explicit promises to the largest investor of the fund that Commonwealth would limit the fund's exposure to the CDO to 10% of the fund's portfolio; (3) engaging in widespread cross-trading funds, selling securities from one Commonwealth-managed fund to another at fraudulently low prices in order to artificially create gains to hide the collapsing value of the CDO; and (4) purchasing still more of the troubled CDO and inflating its value to offset losses to the funds on the losing end of the cross-trades.

SEC v Commonwealth Advisors, Inc., 2015 WL 10990241, at *1 (MD La Dec. 16, 2015) (citations omitted).

[8] *See* Dkt. 9 at 20 (CMA § 13(b), excluding indemnification for "bad faith, willful misconduct, gross negligence or reckless disregard of its duties.") It bears mentioning that the AC does not provide any meaningful information about the misconduct allegedly committed by Morales that forms the basis of the lawsuits for which Commonwealth seeks legal fee reimbursement in this action. Such information was provided by the Funds and the Trustee, which the court considers as documentary evidence. The court also takes judicial notice of all relevant filings on PACER and decisions on Westlaw.

the Collateral Manager **in connection with its engagement hereunder**." *See id.* at 11 (emphasis added). The last sentence of section 5 states:

> Any amounts payable pursuant to this Section 5 shall be reimbursed by [Collybus] **to the extent funds are available therefor in accordance with and subject to the limitations, conditions and priority of distribution set forth in the Priority of Payments as set forth in Article 11 of the Indenture and shall constitute Administrative Expenses of the Issuer.**

See id. (emphasis added). This is consistent with section 20 of the CMA, which provides:

> The Collateral Manager **agrees that the payment of all amounts to which it is entitled pursuant to this Agreement shall be paid in the order of priority set forth in, and limited to the extent of funds available pursuant to, Article 11 of the Indenture.** The Collateral Manager agrees to be bound by the provisions of Article 11 of the Indenture as if the Collateral Manager were a party to the Indenture and each of the Collateral Manager and the Issuer hereby consent to the assignment of this Agreement as provided in Article 15 of the Indenture.

See id. at 25 (emphasis added). In other words, Commonwealth's right to reimbursement is not absolute; Administrative Expenses are only recoverable to the extent provided for in Article 11 of the Indenture.

In the Indenture, Commonwealth's fees recoverable under section 5 of the CMA are included in the definition of Administrative Expenses. *See* Dkt. 10 at 11-12. Article 11 of the Indenture, titled "Application of Cash", governs distributions of cash from the CDO's Payment Account (in section 11.1) and Securities Account (in section 11.2).[9] *See* Dkt. 10 at 160-65. Section 11.1 is the provision applicable to this case. It contains a robust waterfall structure governing the priority of payment of principal and interest. Section 11.1(a) begins:

[9] Payment Account "means the Securities Account designated the 'Payment Account' and established in the name of the Trustee pursuant to Section 10.3." Dkt. 10 at 46; *see id.* at 147-48 (section 10.3, defining Payment Account). The Payment Account is distinct from the Principal Collection Account, Interest Collection Account and Custodial Account defined in section 10.2 and the Expense Account and Interest Reserve account defined in section 10.4. *See id.* at 145-47, 148-50.

> Notwithstanding any other provision in this Indenture, but subject to Section 10.2(g) and the other clauses of this Section 11 and Section 13.1, on each Distribution Date, the Trustee, on behalf of the Issuer, shall disburse amounts transferred to the Payment Account from the Collection Accounts pursuant to Section 10.2(f) in accordance with the following priorities (such priorities, but subject to Section 10.2(g) and the other clauses of this Section 11 and Section 13.1, the "Priority of Payments"):

See Dkt. 10 at 160-61. Distribution Date is defined to mean "March 7, June 7, September 7 and December 7 of each year, commencing on December 7, 2007." *See id.* at 29. Distribution "means any payment of principal, interest or fee or any dividend or premium payment made on, or any other distribution in respect of, an obligation, instrument or security." *Id.*

Section 11(a)(i) is a 21-step waterfall for Interest Proceeds (the Interest Proceeds Waterfall). *See id.* at 161 ("On each Distribution Date, Interest Proceeds with respect to the related Due Period will be applied by the Trustee in the order of priority stipulated below:"). The first step is:

> to pay (x) *first*, any taxes, registration and filing fees (including any registered office and government fees) owed by the Issuer and Co-Issuer, (y) *second*, to pay the amount of any due and unpaid fees owing to the Trustee in accordance with the trustee fee schedule, and (z) *third*, subject to the proviso in clause (i)(2) of this Section 11.1(a), to pay the amount of any due and unpaid indemnities and expenses owing to the Trustee.

See id. (italics in original). These amounts must be paid prior to Commonwealth's Administrative Expenses, which are addressed in the second step of the Interest Proceeds Waterfall, which requires payment of:

> all other Administrative Expenses, in the following order: (a) **the amount of any due and unpaid indemnities, fees and expenses owing to the Collateral Administrator**; and then [7 other irrelevant types of expenses omitted] ... **and then** (i) if the balance, after excluding any amounts in the Expense Account reserved for any Hedge Agreement Closing Expenses, of all Eligible Investments in the Expense Account on the related Determination Date is less than U.S.$300,000, for deposit to the Expense Account of **an amount equal to the lesser of (x) the amount by which U.S.$75,000 exceeds the aggregate amount of payments made under sub-clauses (a) [i.e., Commonwealth's**

> **Administrative Expenses] through (h)** of this clause (2) on such Distribution Date and (y) such amount as would have caused the balance, after excluding any amounts in the Expense Account reserved for any Hedge Agreement Closing Expenses, of all Eligible Investments in the Expense Account, immediately after such deposit, to equal U.S.$300,000; **provided that the cumulative amount paid on any Distribution Date (without limiting the right of the Trustee to pay any Administrative Expenses from amounts on deposit in the Expense Account other than on a Distribution Date as provided in the Indenture) under this clause (i)(2) of this Section 11.1(a) and under clause (i)(1)(z) of this Section 11.1(a), may not exceed U.S.$75,000.**

See id. (emphasis added). In other words, while there are myriad subordinated expenses possibly payable under the second step of the Interest Proceeds Waterfall, the total amount payable under this second step on any given Distribution Date is capped at $75,000. This $75,000 cap is the basis for Wells Fargo's refusal to pay more than $75,000 to Commonwealth out of the collateral liquidation distribution discussed further below.

The next 15 steps (i.e., steps 3-17) of the Interest Proceeds Waterfall are not at issue and are not discussed. *See id.* at 161-63. Step 18 provides that after payment is made on the first 17 steps, payment should be made:

> *first*, all amounts owing under clause (1) and clause (2) above **(without giving effect to any caps therein)** to the extent not previously paid in full under clause (1) and clause (2) above, whether as a result of any dollar limitation set forth therein or otherwise (and in the same order of priority as set forth therein) and, *second*, any Subordinate Hedge Termination Payment due at any time prior to the next Distribution Date.

See id. at 163 (italics in original; bold added for emphasis). Hence, under the first part of step 18, if there is more money that could potentially be distributed, steps 1 and 2 of the Interest Proceeds Waterfall are revisited and any amount withheld under those steps by virtue of the

applicable monetary caps is distributed. Thus, under step 18, Commonwealth could receive Administrative Expenses in excess of $75,000 (which it could not receive under step 2).[10]

Section 11(a)(ii) then sets forth a two-step waterfall for Principal Proceeds (the Principal Proceeds Waterfall):

> On each Distribution Date, Principal Proceeds with respect to the related Due Period will be distributed in the order of priority set forth below:
>
> (1) to pay the amounts referred to in **clauses (1) to (8) of Section 11.1(a)(i) above in the same order of priority specified therein**, but only to the extent not paid in full thereunder; and
>
> (2) *first*, to the payment of principal of the Class A-1 Notes until the Class A-1 Notes have been paid in full, *second* to the payment of principal of the Class A-2 Notes until the Class A-2 Notes have been paid in full, ... [the third through eighth steps, regarding other classes of notes, omitted], *ninth*, to the payment of **the amounts specified in clauses (18) and (19) of Section 11.1(a)(i)** hereto, in each case, to the extent not paid thereunder and in the same order of priority specified therein and *tenth*, to the Fiscal Agent for application in accordance with the Fiscal Agency Agreement.

See id. at 163 (italics in original; bold added for emphasis). By virtue of step 1 of the Principal Proceeds Waterfall, payment of principal does not occur until after the payments due under the first 8 steps of the Interest Proceeds Waterfall are made. That includes Commonwealth's Administrative Expenses up to $75,000 (step 2 of the Interest Proceeds Waterfall), but not Commonwealth's Administrative Expenses in excess of $75,000 (step 18 of the Interest Proceeds Waterfall). Under step 2 of the Principal Proceeds Waterfall, payment of the amounts due under step 18 of the Interest Proceeds Waterfall (i.e., Commonwealth's Administrative Expenses in

[10] The finals three steps of the Interest Proceeds Waterfall (i.e., steps 19-21) are irrelevant and are not discussed.

excess of $75,000) is the second-to-last amount payable, ***and is only made after complete repayment of principal to the delineated classes of noteholders.***[11]

It is undisputed that, upon liquidation of the CDO's collateral, there were insufficient funds to make complete repayment of principal (likely due to the crash in the RMBS market). *See* AC ¶ 41 ("Virtually all of the more than $45,000,000 of proceeds of the sale of the last Collateral Debt Securities constitute Principal Proceeds"). According to Wells Fargo, the *ninth* part of step 2 of the Principal Proceeds Waterfall was never reached – ergo, Commonwealth's Administrative Expenses in excess of $75,000 are not recoverable. *See* Dkt. 20 at 6 ("Commonwealth is entitled at most to $75,000 until noteholders' principal is paid in full. Since that principal was not, and will not be, repaid from the sale of Collybus's assets, the payment on Commonwealth's indemnities from that sale is limited to $75,000."). This conclusion is consistent with sections 11.1(c) and (d), which provide:

> If, on any Distribution Date, the amount available in the Payment Account from amounts received in the related Due Period is insufficient to make the full amount of the disbursements required by the statements furnished by the Issuer pursuant to Section 10.7(b), **the Trustee shall make the disbursements called for in the order and according to the priority set forth under Section 11.1(a), subject to Section 13.1 [concerning Hedge Counterparty Subordination, which is not relevant here], to the extent funds are available therefor.**
>
> Except as otherwise expressly provided in this Section 11.1, if on any Distribution Date **the amount available in the Payment Account from amounts received in the related Due Period is insufficient to make the full amount of the disbursements required by any paragraph of Section 11.1(a)(i) or Section 11.1(a)(ii) (and in the order of priority set forth in such paragraph)** to different Persons, the Trustee shall make the disbursements called for by each such paragraph in accordance with the priority set forth in such paragraph, and if

[11] *See* Dkt. 40 at 4 ("This process boils down to three pertinent steps. In step one, Principal Proceeds are used to pay Administrative Expenses to the extent those were left unpaid by Interest Proceeds. Administrative Expenses include Commonwealth's claimed indemnities, and, in step one, their payment is limited to a cap of $75,000. In step two, Principal Proceeds are to be used to repay Noteholders their principal. And, in step three, any remaining Principal Proceeds are applied again to Administrative Expenses, this time without the cap.").

> no such priority is stated therein, then ratably in accordance with the respective amounts of such disbursements then due and payable to the extent funds are available therefor.

See Dkt. 10 at 164 (emphasis added).

It is essential to note that all of the liquidated collateral discussed below was disbursed on a single Distribution Date in accordance with section 12.1(a). *See id.* at 166 ("All Sale Proceeds of [securities] sold by the Issuer in accordance with this Section 12.1 will be deposited in the Interest Collection Account or the Principal Collection Account, as the case may be, in accordance with Sections 10.2(a) and 10.2(b) **and will be applied on the Distribution Date immediately succeeding the end of the Due Period in accordance with the Priority of Payments**.") (emphasis added). This provision, according to Wells Fargo, further supports its positon that no more than $75,000 in Administrative Expenses are recoverable by Commonwealth. That Commonwealth's right to complete reimbursement of Administrative Expenses is not absolute or guaranteed is further reiterated in section 15.4(e). *See id.* at 186-87 ("the Collateral Manager shall continue to serve as Collateral Manager under the Collateral Management Agreement **notwithstanding that the Collateral Manager shall not have received amounts due it under the Collateral Management Agreement because sufficient funds were not then available hereunder to pay such amounts**.") (emphasis added).[12]

In January 2015, Commonwealth began the process of liquidating the CDO's collateral. The sale of such collateral yielded more than $45 million in proceeds, all but $5.5 million of which was disbursed to the noteholders on or about June 8, 2015 (i.e., on a single Distribution Date). The $5.5 million is being held in escrow by Wells Fargo pending resolution of this action,

[12] While not strictly relevant, it bears mentioning that it makes commercial sense to align the incentives of the Collateral Manager with the noteholders by making the amounts recoverable by the Collateral Manager effectively dependent on the performance of the CDO.

which Commonwealth commenced on June 15, 2015. Commonwealth filed the AC on September 21, 2015 to recoup at least approximately $3.4 million of the $5.5 million as Administrative Expenses, and also to force Wells Fargo to set aside the other approximately $2.1 million as a reserve for future Administrative Expenses (the Indenture provides for no such reserve). The AC contains seven causes of action: (1) an injunction prohibiting Wells Fargo from disbursing the $5.5 million to the noteholders; (2) a declaratory judgment regarding Commonwealth's right to Administrative Expenses under the Indenture; (3) anticipatory breach of the CMA and Indenture; (4) breach of the CMA and Indenture; (5) promissory estoppel; (6) negligent misrepresentation; and (7) equitable estoppel. *See* Dkt. 2.

On October 5, 2015, Wells Fargo removed this action to federal court in the Southern District of New York. By order dated June 23, 2016, the federal court (Furman, J.) granted Commonwealth's motion to remand. *See* Dkt. 6. The Funds then immediately moved to intervene and, as noted, the court granted that unopposed motion. *See* Dkt. 48.[13] On July 8, 2016, the Funds and Wells Fargo separately moved to dismiss the AC on substantially identical grounds. They argue that the Indenture, at most, permits Commonwealth to recover $75,000[14] in Administrative Expenses and that all of Commonwealth's other causes of action fail as a matter of law (e.g., promissory estoppel claim not maintainable where, as here, written contracts

[13] Section 14.8 of the Indenture states that "The Collateral Manager, the Surveillance Agent, any Hedge Counterparty, each Subordinate Securityholder shall be a third party beneficiary of each agreement or obligation in this Indenture." *See* Dkt. 10 at 183.

[14] The Funds and Wells Fargo plausibly take the position that this case will not be litigated over $75,000 and that the court's ruling on whether Commonwealth's recovery is capped at this amount is the dispositive issue in this case. Commonwealth does not dispute this. Hence, the need for discovery in this case would only arise if the court held on this motion that Commonwealth has the possibility of recovering more than $75,000. Since the court is indeed holding that Commonwealth's recovery is capped at $75,000, rather than schedule a preliminary conference, the court is scheduling a telephone conference at which the parties shall take a position on whether a stay of discovery pending appeal of this decision is appropriate.

govern). Commonwealth filed an omnibus opposition brief on July 26, 2016 (Dkt. 39), to which the Funds and Well Fargo separately replied on August 5, 2016. The court reserved on the motions after oral argument. *See* Dkt. 49 (12/2/16 Tr.).

II. Discussion

On a motion to dismiss, the court must accept as true the facts alleged in the complaint as well as all reasonable inferences that may be gleaned from those facts. *Amaro v Gani Realty Corp.*, 60 AD3d 491 (1st Dept 2009); *Skillgames, LLC v Brody*, 1 AD3d 247, 250 (1st Dept 2003), citing *McGill v Parker*, 179 AD2d 98, 105 (1st Dept 1992); *see also Cron v Hargro Fabrics, Inc.*, 91 NY2d 362, 366 (1998). The court is not permitted to assess the merits of the complaint or any of its factual allegations, but may only determine if, assuming the truth of the facts alleged and the inferences that can be drawn from them, the complaint states the elements of a legally cognizable cause of action. *Skillgames*, *id.*, citing *Guggenheimer v Ginzburg*, 43 NY2d 268, 275 (1977). Deficiencies in the complaint may be remedied by affidavits submitted by the plaintiff. *Amaro*, 60 NY3d at 491. "However, factual allegations that do not state a viable cause of action, that consist of bare legal conclusions, or that are inherently incredible or clearly contradicted by documentary evidence are not entitled to such consideration." *Skillgames*, 1 AD3d at 250, citing *Caniglia v Chicago Tribune-New York News Syndicate*, 204 AD2d 233 (1st Dept 1994). Further, where the defendant seeks to dismiss the complaint based upon documentary evidence, the motion will succeed if "the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a matter of law." *Goshen v Mutual Life Ins. Co. of N.Y.*, 98 NY2d 314, 326 (2002) (citation omitted); *Leon v Martinez*, 84 NY2d 83, 88 (1994).

"A trust indenture is a contract, and under New York law, interpretation of indenture provisions is a matter of basic contract law." *Quadrant Structured Prods. Co. v Vertin*, 23 NY3d 549, 559 (2014) (citations and quotation marks omitted). It is well settled under New York law that a "contractual provision that is clear on its face must be enforced according to the plain meaning of its terms." *Bank of N.Y. Mellon v WMC Mortg., LLC*, 136 AD3d 1, 6 (1st Dept 2015) (citation omitted). "This rule applies with even greater force in commercial contracts negotiated at arm's length by sophisticated, counseled businesspeople. In addition, courts may not by construction add or excise terms, nor distort the meaning of those used and thereby make a new contract for the parties under the guise of interpreting the writing." *Id.*, accord *Greenfield v Philles Records, Inc.*, 98 NY2d 562, 569-70 (2002) ("if the agreement on its face is reasonably susceptible of only one meaning, a court is not free to alter the contract to reflect its personal notions of fairness and equity."); *W.W.W. Assocs., Inc. v Giancontieri*, 77 NY2d 157, 163 (1990) ("[E]xtrinsic and parol evidence is not admissible to create an ambiguity in a written agreement which is complete and clear and unambiguous upon its face."). When interpreting a contract, it is essential to read the contract as a whole and "avoid an interpretation that would leave contractual clauses meaningless." *TBA Global, LLC v Fidus Partners, LLC*, 132 AD3d 195, 204 (1st Dept 2015), citing *Two Guys from Harrison-N.Y. v S.F.R. Realty Assocs.*, 63 NY2d 396, 403 (1984); *see Kolbe v Tibbetts*, 22 NY3d 344, 354 (2013) (rejecting interpretation that "both conflicts with the most natural reading of the sentence and renders meaningless the [subject contractual] provision"); *see also Beal Sav. Bank v Sommer*, 8 NY3d 318, 324-25 (2007) ("a contract should be 'read as a whole, and every part will be interpreted with reference to the whole; and if possible it will be so interpreted as to give effect to its general purpose.'"), quoting *Westmoreland Coal Co. v Entech, Inc.*, 100 NY2d 352, 358 (2003).

The meaning of the Indenture's waterfalls in section 11 are perfectly clear. As set forth in detail above, when seeking reimbursement of Administrative Expenses out of a Distribution of Principal Proceeds made on a single Distribution Date, Commonwealth is not entitled to Administrative Expenses in excess of $75,000 unless there is complete repayment of principal to all of the noteholders. It is undisputed that the requisite repayment of principal did not occur. Consequently, based on the clear, unambiguous terms of the Principal Proceeds Waterfall, Commonwealth's maximum possible recovery in this action is $75,000.[15]

That being said, Commonwealth claims that it should be entitled to recover more than $75,000 because Wells Fargo supposedly assured it that further reimbursement would be provided if Commonwealth liquidated the CDO's collateral. Commonwealth alleges that it

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[15] Commonwealth's proposed alternative interpretations are unreasonable for reasons best articulated by Wells Fargo:

> [Commonwealth's] theory that step 1 of the Principal Proceeds Waterfall does not limit or cap the amount payable to Commonwealth's in Administrative Expenses, even where (as here) the Noteholders have not been paid, is simply untenable in light of step 2 of the Principal Proceeds Waterfall, which provides that Administrative Expenses are to be paid out without cap after the Noteholders have been paid in full. If, as [Commonwealth] alleges, the Trustee is required to pay Administrative Expenses in full, notwithstanding the $75,000 cap, at step 1 of the Principal Proceeds Waterfall, [sub-step 9] of the Principal [Proceeds] Waterfall, which explicitly requires payment of all remaining Administrative Expenses at step 2 of the waterfall, would be rendered entirely superfluous, because all Administrative Expenses would have been fully paid at step 1.

Dkt. 22 at 18. In other words, Commonwealth's interpretation would render step 2 meaningless. *See In re Viking Pump, Inc.*, 27 NY3d 244, 257 (2016), citing *Westview Assocs. v Guar. Nat'l Ins. Co.*, 95 NY2d 334, 339 (2000) ("surplusage" is "a result to be avoided"). It also should be noted that in light of the express terms of the Indenture clearly refuting Commonwealth's interpretation, Commonwealth cannot escape the meaning of the Indenture by recasting its claim as one for breach of the implied covenant of good faith and fair dealing. *See SNS Bank, N.V. v Citibank, N.A.*, 7 AD3d 352, 355 (1st Dept 2004) (breach of implied covenant "can only be found where the implied term is consistent with other terms in the contract."), citing *Murphy v Am. Home Prods. Corp.*, 58 NY2d 293, 304 (1983); *see also Skillgames*, 1 AD3d at 252 ("A claim for breach of the implied covenant of good faith and fair dealing cannot substitute for an unsustainable breach of contract claim.").

detrimentally relied on this promise and that it would not have liquidated the collateral had it known that its Administrative Expenses reimbursement would be capped at $75,000. For the purposes of this motion, the court assumes the truth of these allegations. Nonetheless, these allegations do not state a claim upon which relief may be granted.

Wells Fargo's alleged assurances are the predicate for Commonwealth's causes of action for promissory estoppel, negligent misrepresentation, and equitable estoppel, none of which are viable because Commonwealth's reliance on Wells Fargo's assurances were not reasonable as a matter of law. *See Castellotti v Free*, 138 AD3d 198, 204 (1st Dept 2016) ("The elements of a promissory estoppel claim are: (i) a sufficiently clear and unambiguous promise; (ii) **reasonable reliance** on the promise; and (iii) injury caused by the reliance.") (emphasis added);[16] *J.A.O. Acquisition Corp. v Stavitsky*, 8 NY3d 144, 148 (2007) ("A claim for negligent misrepresentation requires the plaintiff to demonstrate (1) the existence of a special or privity-like relationship imposing a duty on the defendant to impart correct information to the plaintiff;[17] (2) that the information was incorrect; and (3) **reasonable reliance** on the information.") (emphasis added); *Shondel J. v Mark D.*, 7 NY3d 320, 326 (2006) ("The purpose of equitable estoppel is to preclude a person from asserting a right after having led another to form the **reasonable belief** that the right would not be asserted.") (emphasis added).[18]

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[16] The promissory estoppel claim also fails because the parties' rights are governed by written contracts. *Susman v Commerzbank Capital Markets Corp.*, 95 AD3d 589, 590 (1st Dept 2012) ("to the extent the second cause of action was for promissory estoppel, such a claim cannot stand when there is a contract between the parties.")

[17] The negligent misrepresentation claim also fails because the relationship between the Trustee and Commonwealth was strictly contractual, not fiduciary in nature. *See Basis Pac-Rim Opportunity Fund v TCW Asset Mgmt. Co.*, 124 AD3d 538, 539 (1st Dept 2015).

[18] Even if equitable estoppel was a viable claim in this case, it is not properly pleaded in the AC because equitable estoppel is an affirmative defense. *See Perella Weinberg Partners LLC v*

Under the CMA, and by virtue of its fiduciary duties to the CDO, Commonwealth had the obligation to act in the best interests of the CDO (subject, as previously noted, to inapplicable fiduciary duty waivers). If Commonwealth believed, as it professes, that the liquidation of the CDO's collateral was the right thing to do for the CDO, it had no right to condition such liquidation on Wells Fargo's promise to provide Administrative Expenses reimbursement in excess of that permitted by the Indenture. Indeed, there is no basis to believe that Wells Fargo itself had the right to breach the Indenture's waterfall provisions by remitting Administrative Expenses out of the waterfalls' order or priority or in excess of the applicable caps. Wells Fargo, as indenture trustee, must carry out its "ministerial duties" in accordance with the Indenture. *See Commerce Bank v Bank of N.Y. Mellon*, 141 AD3d 413, 415 (1st Dept 2016), citing *AG Capital Funding Partners, L.P. v State St. Bank & Trust Co.*, 11 NY3d 146, 157 (2008). Therefore, it was unreasonable for Commonwealth to rely on Wells Fargo's assurances because the absence of such assurances cannot have legitimately informed Commonwealth's decision to liquidate the collateral. Simply put, Wells Fargo had no right to violate the Indenture, nor did Commonwealth have the right, as a sophisticated party, to rely on an erroneous interpretation of the Indenture or a promise it should have known would contravene the Indenture. The Indenture serves to protect the rights of the CDO and its noteholders. Commonwealth cannot insist that the Indenture be violated by virtue of the Trustee's or Commonwealth's prior erroneous understanding of its waterfall provisions.

Commonwealth also argues that its receipt of a payment in excess of $75,000 on January 16, 2014 (i.e., not on a Distribution Date) unrelated to the Distribution of Principal Proceeds

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Kramer, 2016 WL 3906073, at *11 (Sup Ct, NY County 2016) ("Equitable estoppel is not an independent, affirmative cause of action; it is a defense to a breach of contract claim based on detrimental reliance.") (collecting cases).

constitutes a course of conduct in contravention of the Indenture that justifies deviating from the Indenture in this instance. That argument is meritless. The Indenture provides for payment of Administrative Expenses between Distribution Dates (e.g., under section 10.4(b) of the Indenture). Since the January 16, 2014 payment was not made under the Indenture's Principal Proceeds waterfall, that payment is not a valid predicate for a course of conduct argument and does not justify deviating from the Principal Proceeds Waterfall, which governs the instant dispute.

In sum, the only claim properly pleaded by Commonwealth is its fourth cause of action for breach of the CMA and Indenture regarding the $75,000 of Administrative Expenses it might be entitled to, subject to the defenses and counterclaims that will be pleaded by the Funds and Wells Fargo.[19] Accordingly, it is

ORDERED that the motions by the Funds and Wells Fargo to dismiss the AC is granted with respect to all claims except the portion of the fourth cause of action for breach of the CMA and Indenture that seeks $75,000 of Administrative Expenses, and all other claims pleaded in the AC are dismissed with prejudice; and it is further

ORDERED that the Funds and Wells Fargo shall answer the complaint within 21 days of the entry of this order on NYSCEF and that this action shall bear the following caption:

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[19] There is no basis in the Indenture to insist on a reserve, but that issue is academic at this juncture. The subject dispute arises from a single Distribution Date, and the $75,000 cap applicable to that Distribution Date is met based on the past expenses already incurred by Commonwealth. There also is no merit in Commonwealth's clam that it gets a multiple of $75,000 based on multiple possible Distribution Dates having transpired since June 8, 2015. That argument has no basis under section 11 of the Indenture, which only permits Administrative Expenses to be paid out of an actual Distribution, of which there was only one. The amount in escrow is from that original Distribution. The court will not speculate about whether Commonwealth has some other basis to seek Administrative Expenses under the Indenture aside from the bases pleaded in the AC and set forth in its brief.

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COMMONWEALTH ADVISORS, INC., Index No.: 652112/2015

Plaintiff,

-against-

WELLS FARGO BANK, NATIONAL ASSOCIATION, and COLLYBUS CDO I, LTD.,

Defendants,

-and-

AG MORTGAGE VALUE PARTNERS MASTER FUND, L.P., AG MVP PLUS SG III, L.P., and AG SECURITIZED ASSET RECOVERY FUND, L.P.,

Intervenor-Defendants.

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And it is further

ORDERED that a preliminary conference will be held on April 27, 2017 at 3:30 pm by telephone conference, and at least one week beforehand, the parties shall e-file and fax to Chambers a joint-letter addressing the question of whether discovery should proceed pending an appeal of this decision.

Dated: March 31, 2017

ENTER:

J.S.C.