Docket #0037 Date Filed: 6/28/2012

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: RESIDENTIAL CAPITAL, LLC, *et al.*, Debtors.	Case No. 12-12020 (MG) Chapter 11 Jointly Administered
RESIDENTIAL CAPTIAL, LLC., *et al.*, Plaintiffs, -against- ALLSTATE INSURANCE CO., *et al*, Defendants.	Case No. 12-ap-01671 (MG) Bankruptcy Case No. 12-12020 (MG) Jointly Administered

OPPOSITION OF THE FEDERAL DEPOSIT INSURANCE CORPORATION AS RECEIVER FOR CITIZENS NATIONAL BANK AND AS RECEIVER FOR STRATEGIC CAPITAL BANK TO DEBTORS' MOTION TO EXTEND THE AUTOMATIC STAY OR FOR INJUNCTIVE RELIEF



TABLE OF CONTENTS

TABLE OF AUTHORITIES ..... ii-iv

STATEMENT OF FACTS 2

ARGUMENT 3

I. The Automatic Stay Should Not Be Extended to the FDIC's Action Against Ally Securities 3

A. The Stay Should Not Be Extended to Claims Against a Non-Debtor When the Non-Debtor Is Independently Liable to the Plaintiff 4

B. None of the Purported Harms to the Estate Justifies Extending the Stay to the FDIC's Claims 7

1. The Debtors Greatly Overstate the Discovery Burden of the FDIC's Suit 7

2. The Possible Future Assertion of Collateral Estoppel by Another Plaintiff Is Not Grounds to Stay the FDIC's Claims 11

3. That Ally Securities Ultimately May Assert a Claim for Indemnification Against ResCap Does Not Warrant a Stay of the FDIC's Claims 12

4. There Is No Coverage for the FDIC's Claim Under the Insurance Policy That Ally Securities Shareswith One or More of the Debtors 13

II. The FDIC's Claims Against Ally Securities Should Not Be Enjoined under Section 105(a) 14

A. The FDIC's Action Poses No Threat of Imminent Harm to the Reorganization 15

B. The Balance of Equities Weighs Against an Injunction 16

C. The Public Interest Weighs Against an Injunction 16

CONCLUSION 1

TABLE OF AUTHORITIES

CASES

A.H. Robins Co., Inc. v. Piccinin, 788 F.2d 944 (4th Cir. 1986) 4, 6

Adelphia Communications Corp. v. Associated Electric & Gas Insurances Servs., Ltd. (In re Adelphia Communications Corp.), 302 B.R. 439 (Bankr. S.D.N.Y. 2003) 11

Alert Holdings, Inc. v. Interstate Protective Services, Inc. (In re Alert Holdings, Inc.), 148 B.R. 194 (Bankr. S.D.N.Y. 1992) 15

Barney's Inc. v. Isetan Co. Ltd. (In re Barney's, Inc.), 200 B.R. 527 (Bankr. S.D.N.Y. 1996) 14

Bidermann Indus. U.S.A., Inc. v. Zelnik (In re Bidermann Indus. U.S.A), 200 B.R. 779 (Bankr. S.D.N.Y. 1996) 13

Calpine Corp. v. Nevada Power Co. (In re Calpine Corp.), 354 B.R. 45 (Bankr. S.D.N.Y. 2006), *aff'd*, 365 B.R. 401 (S.D.N.Y. 2007) 4, 12, 15, 16

Credit Suisse First Boston, LLC v. Intershop Communications AG, 407 F. Supp. 2d 541 (S.D.N.Y. 2006) 13

Eastern Air Lines, Inc. v, Rolleton (In re Ionosphere Clubs), 111 B.R. 423 (Bankr. S.D.N.Y. 1990) 11, 12

Eichenholtz v. Brennan, 52 F.3d 478 (3d Cir. 1995) 12

Escott v. BarChris Constr. Corp., 283 F. Supp. 643 (S.D.N.Y. 1968) 5

GAF Corp. v. Johns-Manville Corp. (In re Johns-Manville Corp.), 26 B.R. 405 (Bankr. S.D.N.Y. 1983) 4

Globus v. Law Research Service, Inc., 418 F.2d 1276 (2d Cir. 1969) 12

Goldin v. Primavera Familienstiftung, TAG Associates, Ltd. (In re Granite Partners), 194 B.R. 318 (Bankr. S.D.N.Y. 1996) 14

Gucci America, Inc. v. Duty Free Apparel, Ltd., 328 F. Supp. 2d 439 (S.D.N.Y. 2004) 4

Hawaii Structural Ironworkers Pension Trust Fund v. Calpine Corporation, Inc. No. 06 Civ. 5358 (PKC), 2006 WL 3755175 (S.D.N.Y. Dec. 20, 2006) 6, 14, 15, 16

In re Worldcom, Inc. Sec. Litig., 346 F. Supp. 2d 628 (S.D.N.Y. 2004) 5

Johns-Manville Corp. v. Asbestos Litig. Group (In re Johns-Manville Corp.), 26 B.R. 420 (Bankr. S.D.N.Y. 1983), *vacated in part on other grounds,* 41 B.R. 926 (S.D.N.Y. 1984) 12

Laventhol, Krekstein, Horwath & Horwath v. Horwitch, 637 F.2d 672 (9th Cir. 1980) 13

Lyondell Chem. Co. v. CenterPoint Energy Gas Servs. Inc. (In re Lyondell Chem. Co.), 402 B.R. 571 (Bankr. S.D.N.Y. 2009) 11, 15

McHale v. Alvarez (In re The 1031 Tax Group, LLC), 397 B.R. 670 (Bankr. S.D.N.Y. 2008) 14, 15

Nevada Power Co. v. Calpine Corp. (In re Calpine Corp.), 365 B.R. 401 (S.D.N.Y. 2007) 14

Phar-Mor, Inc. v. General Electric Capital Corp. (In re Phar-Mor, Inc. Sec. Litig.), 166 B.R. 57 (W.D. Pa. 1994) 6

Queenie Ltd. V. Nygard Int'l, 321 F.3d 282 (2d Cir. 2003) 4, 11

Teachers Ins. and Annuity Ass'n v. Butler, 803 F.2d 61 (2d Cir. 1986) 3

The Chase Manhattan Bank, N.A. v. Third Eighty-Ninth Assocs. (In re Third Eighty-Ninth Assocs.), 138 B.R. 144 (S.D.N.Y. 1992) 14

Trustees of the Sickness and Accident Fund of Local One-L v. Philips Winson, Inc., No. 00 Civ. 9554 (MHD), 2005 WL 273017 (S.D.N.Y. Feb. 3, 2005) 11

Wolf Fin. Group, Inc. v. Hughes Constr. Co. (In re Wolf Fin. Group, Inc.), No. 94B44009 (JLG), 1994 WL 913278 (Bankr. S.D.N.Y. Dec. 15, 1994) 13

STATUTES

11 U.S.C. § 362(a) 3

15 U.S.C.A. § 77k(a)(5) 6

OTHER AUTHORITIES

2 COLLIER ON BANKRUPTCY ¶ 105.02 16

The Debtors ask the Court to stay or enjoin an action by the Federal Deposit Insurance Corporation as Receiver of Citizens National Bank and as Receiver of Strategic Capital Bank (referred to in both capacities as FDIC), in which the FDIC makes claims under the Securities Act of 1933 against 17 issuers and underwriters of mortgage-backed securities that those banks purchased before they failed. One of those 17 defendants is Ally Securities LLC, which the FDIC sued as underwriter of certificates issued in three securitizations by Residential Accredit Loans, Inc. (RALI). RALI, which the FDIC did not sue, is a Debtor. Ally Securities is not a Debtor, but is a distant affiliate of Residential Capital LLC (ResCap), the principal Debtor.

The Debtors assert that the FDIC's claims against Ally Securities will thwart their reorganization and deplete the property of the estate. But every argument that the Debtors make for this proposition is mistaken. In particular:

- Under the 1933 Act, Ally Securities is liable to the FDIC completely independently of whether RALI would be liable to the FDIC. Ally Securities is not sued as a director, officer, or control person, whose liability would depend upon establishing the liability of RALI.

- Discovery on the FDIC's claims against Ally Securities will not be unduly burdensome to any Debtor. Ally Securities itself has many relevant documents; the Debtors have already produced many relevant documents in other cases and can easily produce them again to the FDIC; and, at worst, the Debtors would have to produce documents about fewer than 4,000 mortgage loans.

- RALI will not have to indemnify Ally Securities for its liability to the FDIC because the courts forbid the indemnification of the liabilities of underwriters under the 1933 Act.

- The only insurance policy that Debtors produce that covers both Ally Securities and any Debtors clearly does not cover the FDIC's claims against Ally Securities. That claim will not deplete any coverage that would otherwise have been available to a Debtor.

- The harm to the public interest (which the FDIC protects as Receiver) if the FDIC's action were enjoined would be far greater than any inconvenience to the Debtors from giving discovery in the FDIC's action.

For these reasons, the Court should deny the Debtor's motion to stay or enjoin the FDIC's claims against Ally Securities.

STATEMENT OF FACTS

On May 18, 2012, the FDIC as Receiver for two failed banks, Citizens National Bank and Strategic Capital Bank, brought an action in the United States District Court for the Southern District of New York against 17 defendants for violations of Sections 11 and 15 of the Securities Act of 1933 in connection with the purchase by the failed banks of certificates in 12 securitizations of residential mortgage loans.[1] *See FDIC v. Bear Stearns Asset Backed Securities I LLC*, No. 1:12-cv-04000-LTS (S.D.N.Y filed May 18, 2012). The defendants were sued in their capacities as issuers or underwriters of those certificates or as control persons of those defendants. (FDIC Compl. ¶ 3; Ex. A to Declaration of Kathryn E. Matthews, dated June 28, 2012.)

The FDIC sued none of the Debtors or any of their directors, officers, or control persons. The only affiliate of a Debtor that the FDIC sued is Ally Securities, which it sued as an

[1] The defendants are Bear Stearns Asset Backed Securities I LLC; The Bear Stearns Companies LLC; J.P. Morgan Securities LLC; Citicorp Mortgage Securities, Inc.; CitiMortgage, Inc.; Citigroup Global Markets Inc.; Credit Suisse First Boston Mortgage Securities Corp.; Credit Suisse Management LLC; Credit Suisse Securities (USA) LLC; Merrill Lynch Mortgage Investors, Inc.; Merrill Lynch Mortgage Capital Inc.; Merrill Lynch, Pierce, Fenner & Smith Inc.; Ally Securities, LLC; Deutsche Bank Securities Inc.; HSBC Securities (USA) Inc.; RBS Securities Inc.; and UBS Securities LLC.

underwriter of three securitizations by RALI, one of the Debtors. Those securitizations are RALI 2006-QS6, RALI 2006-QS18, and RALI 2006-QS8. (FDIC Compl. Scheds. 1, 2, 4.) The failed banks bought their certificates in these trusts in the secondary market from dealers other than Ally Securities. (*Id.*) (Two other RALI trusts are also involved in the FDIC's suit, but on those the FDIC has sued only entities that are not affiliated with any Debtor.) (*Id.* Scheds. 5, 9.)

Moreover, according to the offering documents filed with the SEC, Debtors or their affiliates originated only a minority of the loans in the three trusts on which the FDIC has sued Ally Securities. Debtors GMAC Mortgage, LLC and Homecomings Financial, LLC originated 29.1% of the loans in the relevant loan group in RALI 2006-QS6, 41.4% of the loans in the relevant loan groups in RALI 2006-QS18, and 19.6% of the loans in RALI 2006-QS8, a total of approximately 3,817 loans. (*Id.* Scheds. 1, 2, 4 Item 37(a).) Thus, discovery of mortgage loan files, underwriting guidelines, and origination procedures will impose a minimal burden on the Debtors.

On May 14, 2012, Residential Capital, LLC, along with 50 of its subsidiaries, filed for Chapter 11 Bankruptcy protection in this Court. In their motion of May 25, 2012, the Debtors ask the Court to extend the automatic stay to actions against their affiliates that relate to the issuance or sale by the Debtors of mortgage-backed securities, including the action brought by the FDIC.

ARGUMENT

I. The Automatic Stay Should Not Be Extended to the FDIC's Action Against Ally Securities.

By its terms, Section 362(a) applies only to debtors and their property; it does not automatically stay proceedings against non-debtors. *See* 11 U.S.C. § 362(a); *Teachers Ins. and Annuity Ass'n v. Butler*, 803 F.2d 61, 65 (2d Cir. 1986) ("It is well-established that stays

pursuant to § 362(a) are limited to debtors and do not encompass non-bankrupt [entities]."); *GAF Corp. v. Johns-Manville Corp (In re Johns-Manville Corp.)*, 26 B.R. 405, 409 (Bankr. S.D.N.Y. 1983) ("The language of Section 362 clearly refers only to actions against the debtor and does not relate to any other interparty claims."). Although a court may extend the stay to enjoin suits against non-debtors under certain limited circumstances, "[c]ourts caution that such extensions are reserved for 'special circumstances,' . . . and typically apply to those lawsuits which threaten serious risk to a reorganization . . . ." *Gucci America, Inc. v. Duty Free Apparel, Ltd.*, 328 F. Supp. 2d 439, 442 (S.D.N.Y. 2004) (citing *Queenie Ltd. v. Nygard Int'l*, 321 F.3d 282, 287 (2d Cir. 2003)). No such "special circumstances" exist here.

A. The Stay Should Not Be Extended to Claims Against a Non-Debtor When the Non-Debtor Is Independently Liable to the Plaintiff.

The Second Circuit has held that the stay may be extended to a suit against non-debtors only if the suit "will have an immediate adverse economic consequence for the debtor's estate." *Queenie*, 321 F.3d at 287. *See also Calpine Corp. v. Nevada Power Co. (In re Calpine Corp.)*, 354 B.R. 45, 49 (Bankr. S.D.N.Y. 2006), *aff'd*, 365 B.R. 401 (S.D.N.Y. 2007). The Debtors compare this case to one such situation that the Second Circuit recognized in *Queenie*, *i.e.*, "actions where 'there is such identity between the debtor and the third-party defendant that the debtor may be said to be the real party defendant.'" *Queenie*, 321 F.3d at 288 (quoting *A.H. Robins Co., Inc. v. Piccinin*, 788 F.2d 994, 999 (4th Cir. 1986)). That is not true here because Ally Securities is liable to the FDIC completely independently of whether any Debtor would also be liable. Indeed, in *A.H. Robins*, which the Second Circuit quoted in *Queenie*, the Fourth Circuit explained that the "unusual circumstances" test is not satisfied when a third party's liability is independent of any liability of a debtor. *A.H. Robins*, 788 F.2d at 999. Rather, this rationale for extension of the stay applies, if at all, only when there is an identity of interest between the

debtor and the non-debtor defendant, such as a suit in which the non-debtor defendant is alleged to be vicariously liable for liabilities of the debtor and therefore would be entitled to "absolute indemnity" by the debtor for any judgment. *Id.*

Ally Securities has no such identity of interest with any Debtor. The FDIC does not need to prove any liability of any Debtor to win its claims against Ally Securities. To the contrary, under Section 11 of the 1933 Act, Ally Securities, as underwriter of the three offerings in which the failed banks bought certificates, had an independent duty to investigate and verify the statements about those offerings in the prospectus supplements that were filed with the SEC. *See, e.g., In re Worldcom, Inc. Sec. Litig.*, 346 F. Supp. 2d 628, 662 (S.D.N.Y. 2004); *Escott v. BarChris Constr. Corp*., 283 F. Supp. 643, 697 (S.D.N.Y. 1968) ("[U]nderwriters are made responsible for the truth of the prospectus. If they may escape that responsibility by taking at face value representations made to them by the company's management, then the inclusion of underwriters among those liable under Section 11 affords the investors no additional protection."). As the court explained in *Worldcom*,

> [u]nderwriters must "exercise a high degree of care in investigation and independent verification of the company's representations." Overall, "[n]o greater reliance in our self-regulatory system is placed on any single participant in the issuance of securities than upon the underwriter." Underwriters function as "the first line of defense" with respect to material misrepresentations and omissions in [offering documents]. As a consequence, courts must be "particularly scrupulous in examining the[ir] conduct."

346 F. Supp. 2d at 662 (internal citations omitted). Thus Ally Securities is liable to the FDIC independently of any liability of any Debtor for the material untrue or misleading statements about the securities that it underwrote.[2]

[2] The Debtors' assertion that the "Non-Debtor Affiliates," which include Ally Securities, "did not provide any representations or warranties in conjunction with those securities" and "were [not] responsible for preparing or filing the offering documents accompanying the securitizations" is simply untrue. (Debtors' Mot. at 1.) As an underwriter of these offerings, Ally Securities made the statements

When the non-debtor defendant is independently liable to the plaintiff, and the claims against it are not inextricably intertwined with those against the debtor, courts have refused to stay or enjoin claims against the non-debtor. *See, e.g., A.H. Robins*, 788 F.2d at 999 (the Code was not intended to stay actions that assert that a non-debtor is "independently liable as, for example, where the debtor and another are joint tortfeasors or where the nondebtor's liability rests upon his own breach of duty"); *Phar-Mor, Inc. v. General Electric Capital Corp. (In re Phar-Mor, Inc. Sec. Litig.)*, 166 B.R. 57, 62 (W.D. Pa. 1994) (creditor's action against debtor's accounting firm not stayed because accountants owed independent duty running directly to creditor; enjoining action under these circumstances would "abuse the authority provided by §105" and "trample the rights of the Creditor-Defendants to assert their independent and distinct claims against a non-bankrupt third party").

In a case much like this one, *Hawaii Structural Ironworkers Pension Trust Fund v. Calpine Corporation, Inc.,* No. 06 Civ. 5358 (PKC), 2006 WL 3755175 (S.D.N.Y. Dec. 20, 2006), the debtor asked the court to enjoin the prosecution of an action under the 1933 Act against the debtor, five people who were directors of the debtor and signed its registration statements, and the underwriters of its securities. Although the district court affirmed the bankruptcy court's decision to stay the claims against the individual directors because prosecution of those claims threatened to harm the reorganization process, it made clear that the ruling "*does not reach the underwriter defendants and the claims against them may proceed unhindered*." 2006 WL 3755175, at *6 (emphasis added). Just the same is true here. Even if the Court were to stay claims that others have made against the directors and officers or control

---

that appear in the prospectus supplements filed with the SEC for purposes of liability under Section 11 of the 1933 Act. 15 U.S.C.A. § 77k(a)(5).

persons of the Debtors, the FDIC has sued none of those, and its claims against Ally Securities are independent of any liability of any Debtor.

B. None of the Purported Harms to the Estate Justifies Extending the Stay to the FDIC's Claims.

The Debtors make four arguments why all of the MBS actions should be stayed or enjoined: (1) that the actions will impose burdensome discovery obligations on the Debtors; (2) that the Debtors will be exposed to a risk of collateral estoppel, *stare decisis*, and "evidentiary prejudice" if the actions proceed, because the Debtors' alleged conduct is the foundation of the plaintiffs' claims in all of these cases; (3) that the Debtors will face indemnification claims if the MBS actions proceed, because ResCap is obligated to indemnify the non-debtor Corporate Affiliates for losses and expenses that they incur in the MBS actions; and (4) that property of the estate may be depleted by these actions, because the Debtors and the non-debtor Affiliates share insurance coverage for "certain of the MBS Actions." (Debtors' Motion at 2-3.) When the facts of the FDIC's claims are considered independently, as they must be, the Debtors cannot prove any of these arguments.

1. The Debtors Greatly Overstate the Discovery Burden of the FDIC's Suit.

The Debtors make no attempt to quantify – in either hours or dollars – the burden that they expect discovery in the FDIC's suit to impose on them. Although they argue that the discovery of them in the 27 different MBS actions combined will be "Herculean" (Debtors' Mot. at 27), the burden from the FDIC's action, which the Court should consider separately from the other MBS actions, will easily be manageable.

First, the FDIC's suit cannot reasonably be compared to the other investor actions. As against Ally Securities, the FDIC's suit involves only three trusts, all from the same SEC shelf, and spanning only six months (from June to December 2006). In the specific pools that back the

certificates that the failed banks purchased, there are only approximately 3,817 loans that any affiliate of a Debtor originated. There are no individual defendants and no Debtor defendants.

The investor cases that the Debtors cite as "illustrative examples," on the other hand, are much larger. In *Western & Southern Life Ins. Co. v. Residential Funding Co., LLC*, No. A1105042 (Ohio Ct. of Comm. Pleas), for example, the claims are based on seven securitizations, from three different SEC shelves, spanning three years, and including more than 48,000 mortgage loans. (Declaration of Jeffrey A. Lipps, dated May 24, 2012, ¶ 33.) There are seven individual defendants and five Debtor entities named as defendants.[3] (*Id.* ¶ 34.) In *N.J. Carpenters Health Fund v. Residential Capital, LLC*, No. 08-cv-8781-HB (S.D.N.Y.), there are 10 securitizations of more than 28,000 mortgage loans, eight individual defendants, and three Debtor entities named as defendants. (*Id.* ¶¶ 45-46; Memorandum of Law in Support of the RALI Defendants' Motion to Dismiss the Amended Complaint, Ex. A, *N.J. Carpenters Health Fund v. Residential Capital, LLC*, No. 08-cv-8781-HB (S.D.N.Y. July 17, 2009) (Ex. B to Matthews Decl.) The Debtors also are incorrect that each case involves different securitizations so that little, if any, discovery in one suit will be relevant to another. (Debtors' Mot. at 16.) To the contrary, the same three trusts on which the FDIC has sued Ally Securities are involved in one or more of the 26 other actions that are the subject of the Debtors' motion. Two trusts (RALI 2006-QS8 and RALI 2006-QS18) are included in *N.J. Carpenters*; two trusts (RALI 2006-QS6 and RALI 2006-QS18) are included in *Union Cent. Life Ins. Co. v. Credit Suisse First Boston Mortgage Sec. Corp.*, No. 11-cv-2890 (S.D.N.Y.); and one trust (RALI 2006-QS6) is included in *Western & Southern Life*.

[3] There are undoubtedly going to be more depositions taken in a case involving individual defendants, as the knowledge of each is explored in connection with the "due diligence" defense available under the 1933 Act.

Furthermore, according to the Debtors, significant discovery already has taken place in *N.J. Carpenters.* The parties have produced "more than 175,000 pages of documents, including underwriting guidelines, transaction documents, contract files reflecting agreements between debtor RFC and various loan originators, emails for over 20 custodians, and selected loan files." (Lipps Decl.¶ 54.) Given the overlap in securitizations between that case and the FDIC's, there is no reason why these documents (or at least a subset of them) would not be precisely the sort of documents that the FDIC will request. In any event, the Debtors would not need to incur the cost of restoring email backup tapes for the same custodians, or of locating and processing the relevant loan files, underwriting guidelines, and transaction documents.[4] If the FDIC's discovery requests would require some additional searching, sophisticated techniques like predictive coding are available to reduce the cost and burden on the Debtors. The Debtors are wrong that Ally Securities "posses[es] very few documents" so that most of the burden would fall on them. (Debtors' Mot. at 27.) To the contrary, as the Debtors concede, Ally Securities as the underwriter of the securitizations is likely to have documents relating to due diligence and other analysis of the mortgage loans underlying the certificates (*Id.* at 27-28), which is the very subject of the allegedly untrue or misleading statements in the prospectus supplements. Certainly not all discovery will focus on the Debtors.

Most of the documents that the FDIC will request from the Debtors are discrete, easily identifiable documents, such as loan files and underwriting guidelines. Moreover, almost none of such documents will be privileged, so a privilege review need not be time-consuming. Although

[4] According to the Debtors, discovery also has begun in *Western & Southern Life*, and at the time of the Debtors' bankruptcy filing, the defendants were preparing to produce transaction documents and underwriting guidelines relevant to the transactions involved in that case. (Lipps Decl. ¶ 34.) It would impose little additional burden on the Debtors to produce the same documents in this case with respect to the overlapping trust.

the production of email will impose some burden on the Debtors, that burden will be limited significantly by the fact, as explained above, that email from at least some of the relevant custodians apparently has already been restored and produced. Because there are likely to be only a limited number of relevant custodians, there is no reason to think that the Debtors would be required to restore, review, and produce email from a large number of additional custodians. In any event, the parties can negotiate the scope of the searches to take full advantage of the discovery that already has occurred and minimize the burden on the Debtors. It simply is too early in the process for the Debtors to throw up their hands and claim that the FDIC's action will impose too great a burden on the reorganization process and must be stayed.

Finally, the contention of the Debtors that continued litigation against Ally Securities would distract key personnel of the Debtors and negatively affect the reorganization is unfounded. The two witnesses described by the Debtors have knowledge of the activities of Debtor RFC (Debtors' Mot. at 29-31), but Debtors do not refer to any people involved in the reorganization with knowledge of the origination activities of Debtor GMAC Mortgage, which also originated the relevant loans. In any event, the task of locating and producing loan files and accompanying servicing records can be done by clerical or technical personnel and need not distract any key employees involved in restructuring. Similarly, as discussed above, the FDIC anticipates that most of the underwriting guidelines, internal documents, and communications of any Debtors relevant to the FDIC's claims have already been collected and produced in other actions. The re-production of these materials will not detract from the efforts of any key employees in the reorganization. Moreover, most depositions will be of former employees, as the relevant collateral was originated in or around 2006. Debtors admit that there are very few

employees left with personal knowledge of first-lien structured finance operations. (Debtors' Mot. At 29.)

2. The Possible Future Assertion of Collateral Estoppel by Another Plaintiff Is Not Grounds to Stay the FDIC's Claims.

The fact that another plaintiff may attempt to assert collateral estoppel or a related doctrine based on a finding by the court in the FDIC's action is not an appropriate ground on which to enjoin the FDIC's claims. *See Queenie*, 321 F.3d at 288 ("If such apprehension could support application of the stay, there would be vast and unwarranted interference with creditors' enforcement of their rights against non-debtor co-defendants.") Indeed, in *Queenie*, the Second Circuit noted that it had "not located any decision applying the stay to a non-debtor solely because of an apprehended later use against the debtor of offensive collateral estoppel or the precedential effect of an adverse decision." 321 F.3d at 288. *See also Lyondell Chem. Co. v. CenterPoint Energy Gas Servs. Inc. (In re Lyondell Chem. Co.)*, 402 B.R. 571, 591 (Bankr. S.D.N.Y. 2009) (declining to find irreparable injury as a consequence of the potential application of collateral estoppel, res judicata, or *stare decisis*); *Trustees of the Sickness and Accident Fund of Local One-L v. Philips Winson, Inc.*, No. 00 Civ. 9554 (MHD), 2005 WL 273017, at *2 (S.D.N.Y. Feb. 3, 2005) (citing *Queenie* and holding that the "possible precedential effect on the debtor's case . . . is not an adequate basis for extending the automatic stay to a non-debtor"). The Debtors cite *Queenie* elsewhere in their motion, but omit this dispositive language that completely undermines their argument on this point.[5]

[5] The cases on which the Debtors rely (while disregarding the dispositive holding in *Queenie*) are factually distinguishable. In *Adelphia Communications Corp. v. Associated Electric & Gas Insurances Servs., Ltd.*(*In re Adelphia Communications Corp.)*, 302 B.R. 439, 450 (Bankr. S.D.N.Y. 2003), the court determined that the outcome of an insurer's action to rescind insurance policies against individual directors and officers may have a preclusive effect on the insurance policies of the Debtor companies. *Eastern Air Lines, Inc. v. Rolleton (In re Ionosphere Clubs)*, 111 B.R. 423, 435 (Bankr. S.D.N.Y. 1990) involved RICO claims, such that a finding of conspiracy liability of a co-defendant foreclosed any

3. That Ally Securities Ultimately May Assert a Claim for Indemnification Against ResCap Does Not Warrant a Stay of the FDIC's Claims.

The Debtors assert that ResCap is obligated to indemnify the non-debtor Corporate Affiliates – including Ally Securities – for losses and expenses incurred in the MBS actions. They argue that, because those anticipated indemnification claims will have adverse consequences on the Debtors' estate, the claims against these entities should be stayed or enjoined. (Debtors' Mot. at 3.) The Court should reject this argument because Ally Securities is not entitled to indemnification for liability under the 1933 Act.

Debtors rely on the indemnification provision in the Amended and Restated Operating Agreement between ResCap, General Motors Corporation, and GMAC LLC, dated November 27, 2006, and governed by New York law, under which ResCap agreed to indemnify GMAC Affiliates "to the fullest extent permitted by law." (*See* Debtors' Mot. at 17; Ex. B to Declaration of James Whitlinger, dated May 25, 2012.) But indemnification of a securities underwriter, such as Ally Securities, for liability under federal securities laws violates public policy and is not enforceable. *See Globus v. Law Research Service, Inc.*, 418 F.2d 1276, 1288 (2d Cir. 1969) ("to tolerate indemnity under these circumstances would encourage flouting the policy of the common law and the Securities Act."); *Eichenholtz v. Brennan*, 52 F.3d 478, 484-85 (3d Cir. 1995) ("If the court enforced an underwriter indemnification provision, it would effectively

---

effective defense by the Debtor to a RICO claim. *Ionosphere* also involved claims against a high-ranking official of Debtor, resulting in likely adverse findings under the doctrine of respondeat superior. Similarly, *Johns-Manville* concerned actions against key officers and employees whose liability was necessarily derivative of debtor's liability. *Johns-Manville Corp. v. Asbestos Litig. Group (In re Johns-Manville Corp.)*, 26 B.R. 420, 428-429 (Bankr. S.D.N.Y. 1983), *vacated in part on other grounds,* 41 B.R. 926 (S.D.N.Y. 1984) ("injunction appropriate where the "true object [of suit against non-debtor] is the debtor itself" and where suit was "nothing more than an effort to circumvent Section 362 by suing [debtor's] officers and directors when the real party in interest" was the debtor). *See also In re Calpine*, 354 B.R. at 50 (finding "significant risk of collateral estoppel" where non-debtor's liability was directly contingent on Debtor's liability). No such concerns are present here, where the FDIC is seeking to establish the *independent* liability of Ally Securities as an underwriter under the 1933 Act.

eliminate the underwriter's incentive to fulfill its investigative obligation."); *Laventhol, Krekstein, Horwath & Horwath v. Horwitch*, 637 F.2d 672, 676 (9th Cir. 1980) ("permitting indemnity would undermine the statutory purpose of assuring diligent performance of duty and deterring negligence"); *Credit Suisse First Boston, LLC v. Intershop Communications AG*, 407 F. Supp. 2d 541, 547 (S.D.N.Y. 2006) (indemnification precluded in securities cases involving negligent misrepresentations). Because Ally Securities cannot enforce the indemnification agreement as to its liability to the FDIC under the 1933 Act, indemnification is not a basis to stay the action against the non-debtor Ally Securities.[6]

4. There Is No Coverage for the FDIC's Claim Under the Insurance Policy That Ally Securities Shares with One or More of the Debtors.

The Debtors argue that an errors-and-omissions policy obtained by Ally Financial provides coverage to the non-debtor Affiliates, and that payments on behalf of non-debtor Affiliates like Ally Securities will deplete the coverage limits available to the Debtors. (Debtors' Mot. at 17.) But the policy that the Debtors attach to their motion (Ex. C. to Whitlinger Decl.) does not cover Ally Securities for liability under Section 11 of the 1933 Act. The policy covers liabilities incurred in connection with Broker-Dealer Services rendered to a Broker-Dealer Customer. (Ex. C to Whitlinger Decl. at 38, 40.) Neither of the failed banks was a Broker-Dealer Customer of Ally Securities. Both purchased the RALI certificates in the secondary market from

[6] Ally Securities may be indemnified for the fees and costs it incurs in defending the FDIC's action, but only if Ally Securities prevails in the action. *See Intershop*, 407 F. Supp. 2d at 548 ("one who is not at fault may enforce a contractual agreement for the indemnification of expenses incurred in the *successful* defense of securities laws claims") (emphasis in original). Thus, the right of Ally Securities to indemnification is conditioned on its successful defense of the action. Because Ally Financial's right to indemnification from the Debtors is not absolute or unconditional, extension of the stay is not warranted. *See Bidermann Indus. U.S.A., Inc. v. Zelnik (In re Bidermann Indus. U.S.A., Inc.)*, 200 B.R. 779, 784-85 (Bankr. S.D.N.Y. 1996) (the fact that chairman of debtor would need to demonstrate his entitlement to indemnity under criteria set forth in statute and corporation's by-laws weighed against staying tort action against him); *Wolf Fin. Group, Inc. v. Hughes Constr. Co. (In re Wolf Fin. Group, Inc.)*, No. 94B44009 (JLG), 1994 WL 913278, at *4 (Bankr. S.D.N.Y. Dec. 15, 1994) (denying stay where non-debtors failed to show "an unconditional right to indemnification").

other dealers. Moreover, the policy covers a claim only if either (i) the claim was made during the policy period (which ended on December 31, 2008) or the extended reporting period (which ended on December 31, 2009), or (ii) during the policy period, the insured gave the insurer notice of the circumstances that could give rise, and later did give rise, to the claim. The first condition is not satisfied because the FDIC made its claim against Ally Securities in May 2012. And the Debtors make no allegation that Ally Securities gave the required notice of claim before December 31, 2008, and thereby satisfied the second condition.

II. The FDIC's Claims Against Ally Securities Should Not Be Enjoined under Section *105(a).*

The Debtors also have failed to make a showing that would justify an injunction under Section 105(a). Because the practical effect of such an injunction is to broaden the scope of the automatic stay, it is a power that must be used "sparingly." *See Barney's, Inc. v. Isetan Co. Ltd. (In re Barney's, Inc.)*, 200 B.R. 527, 531 (Bankr. S.D.N.Y. 1996); *The Chase Manhattan Bank, N.A. v. Third Eighty-Ninth Assocs. (In re Third Eighty-Ninth Assocs.)*, 138 B.R. 144, 146 (S.D.N.Y. 1992) ("[The debtor bears the burden of proof in obtaining the 'extraordinary and drastic remedy' of an injunction.") (internal citation omitted). To enjoin claims against non-debtors under Section 105(a), the Court "must find that the claims 'threaten to thwart or frustrate the debtor's reorganization efforts,' and that the injunction is 'important' for effective reorganization." *McHale v. Alvarez (In re The 1031 Tax Group, LLC)*, 397 B.R. 670, 684 (Bankr. S.D.N.Y. 2008) (Glenn, J.) (quoting *Goldin v. Primavera Familienstiftung, TAG Associates, Ltd. (In re Granite Partners)*, 194 B.R. 318, 337 (Bankr. S.D.N.Y. 1996)). The threat to the reorganization process must be "imminent, substantial and irreparable." *Nevada Power Co. v. Calpine Corp. (In re Calpine Corp.)*, 365 B.R. 401, 410 (S.D.N.Y. 2007) (quoting *Hawaii Structural*, 2006 WL 3755175, at *4).

"A request by a debtor for an injunction under Section 105(a) pending confirmation of the debtor's plans for reorganization is regarded as a request for a preliminary injunction." *Hawaii Structural*, 2006 WL 3755175, at *4. In considering such a request, courts in this district have applied the "'traditional preliminary injunction standard as modified to fit the bankruptcy context.'" *In re Calpine,* 365 B.R. at 409 (internal citation omitted). That approach considers: (1) whether there is a reasonable likelihood of successful reorganization; (2) whether there is imminent irreparable harm to the estate in the absence of an injunction;[7] (3) whether the balance of harms tips in favor of the moving party; and (4) whether the public interest weighs in favor of an injunction. *See, e.g., In re Lyondell*, 402 B.R. at 588-89; *In re Calpine*, 365 B.R. at 409; *Hawaii Structural*, 2006 WL 3755175, at *4. Under these factors, an injunction is not warranted.

A. The FDIC's Action Poses No Threat of Imminent Harm to the Reorganization.

As discussed in detail above, the FDIC's action poses no imminent threat to the restructuring process. That action will not impose burdensome discovery obligations on the Debtors; the risk that an adverse finding in the FDIC's action against a non-debtor could be used against the Debtors in another action is minute; Ally Financial will not be able to enforce the indemnification agreement against the Debtors; and the errors-and-omissions policy does not cover the FDIC's claims.

[7] Not all courts require a showing of irreparable harm. *See, e.g., In re The 1031 Tax Group*, 397 B.R. at 684 ("because 105(a) injunctions are authorized by statute, they do not need to comply with the traditional requirements of Fed. R. Civ. P. 65"). In particular, many have recognized a "narrow exception" to the irreparable harm requirement, under which courts may issue a preliminary injunction where the action to be enjoined is one that threatens the reorganization process or which would impair the court's jurisdiction with respect to the case before it. *See In re Calpine,* 365 B.R. at 409-10*; In re Lyondell*, 402 B.R. at 590; *In re The 1031 Tax Group*, 397 B.R. at 684; *Alert Holdings, Inc. v. Interstate Protective Services, Inc. (In re Alert Holdings, Inc.)*, 148 B.R. 194, 200 (Bankr. S.D.N.Y. 1992) (concluding that, where the movant shows "that the action sought to be enjoined would embarrass, burden, delay or otherwise impede the reorganization proceedings or if the stay is necessary to preserve or protect the debtor's estate or reorganization prospects, the Bankruptcy Court may issue injunctive relief").

B. The Balance of Equities Weighs Against an Injunction.

Under this factor, the Court must balance the comparative harm to the Debtors and their reorganization if an injunction is not granted against the harm to the FDIC if it is. *See Hawaii Structural*, 2006 WL 3755175, at *4. For all of the reasons explained above, the FDIC's suit does not pose a risk of significant harm to the Debtors' reorganization. On the other hand, if the Court enjoins the FDIC's claims, it will have to wait many months or years before it can pursue them, and will then have to pursue them separately from its claims against the other underwriters of the same securities. The three securitizations underwritten by Ally Securities were also underwritten by RBS Securities Inc., Deutsche Bank Securities Inc., and HSBC Securities (USA) Inc., which the FDIC has also sued. Pursuing its identical claims against those underwriters now and against Ally Securities later would be a waste of the money of the receiverships.

C. The Public Interest Weighs Against an Injunction.

The public interest factor "'requires a balancing of the public interest in successful bankruptcy reorganizations with other competing societal interests.'" *In re Calpine*, 365 B.R. at 413 (quoting 2 COLLIER ON BANKRUPTCY ¶ 105.02). Whatever public interest there is in avoiding the minor inconvenience to the Debtors of producing documents on the loans they originated is far outweighed by the public interest, which the FDIC represents in its capacity as Receiver for these failed banks, in promptly recovering all funds to which the receiverships are entitled and paying those funds to the creditors of the failed banks.

CONCLUSION

For all of the foregoing reasons, the Court should deny the Debtors' motion to stay or enjoin the FDIC's claims against Ally Securities under Sections 362(a) or 105(a) of the Bankruptcy Code.

GRAIS & ELLSWORTH LLP

By: /s/ Mark B. Holton

David J. Grais (DG 7118)
Mark B. Holton (MH 4939)
Kathryn E. Matthews (KN 0932)
Leanne M. Wilson (LW 1225)
Maria Heifetz (MH 1104)

1211 Avenue of the Americas
New York, New York 10036
Phone: 212-755-0100

Attorneys for Federal Deposit Insurance Corporation as Receiver for Citizens National Bank and as Receiver for Strategic Capital Bank