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

In the matter of the application of

THE BANK OF NEW YORK MELLON (as Trustee under various Pooling and Servicing Agreements and Indenture Trustee under various Indentures), *et al.*

Petitioners,

for an order, pursuant to C.P.L.R. § 7701, seeking judicial instructions and approval of a proposed settlement.

Index No. 651786/2011

Assigned to: Kapnick, J.

RESPONDENTS' JOINT BRIEF IN OPPOSITION TO APPROVAL OF PROPOSED SETTLEMENT AND ENTRY OF PROPOSED FINAL ORDER AND JUDGMENT

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Respondents respectfully submit this joint brief in opposition to approval of the proposed settlement and entry of the Proposed Final Order and Judgment ("PFOJ"), and in response to Petitioners' October 11, 2013 brief (Doc. No. 942).[1]

PRELIMINARY STATEMENT

This Court has been presented with an extraordinary and unprecedented request by Petitioners to approve a collusive and inadequate settlement that would extinguish claims of thousands of absent RMBS investors for mere pennies on the dollar, where the evidence is that losses exceed $100 billion, through an obscure Article 77 proceeding that has never been utilized for this purpose over the many decades it has been on the books. Giving a whole new meaning to the word "chutzpah," the Petitioners also request that the Court, among other things, bar any investor from opting out of the settlement if it does not like the deal and completely immunize Petitioners from any liability to investors for their conduct in negotiating the accord. For two principal reasons, the Court should decline Petitioners' requests:

First, the process leading to this settlement was plagued by conflict and collusion at every turn. The Trustee, Bank of New York Mellon ("BNYM"), was admittedly looking to protect only its own self-interest rather than the interests of the thousands of investors (or "certificateholders") it was bound to protect. BNYM's counsel, Mayer Brown, too was conflicted because it regularly represents Bank of America ("BofA") and indeed promised not to file suit against BofA on behalf of BNYM—in other words, to fight with both hands tied behind its back. Nor could the Institutional Investors effectively represent the absent certificateholders' interests, as these institutions had strong ties to BofA, admitted acting solely in their own personal interests, and held less than a 25% voting interest in 305 of the 530 RMBS trusts

[1] Respondents reserve the right to supplement this brief following the close of evidence.

covered by the settlement. Their counsel (Gibbs & Bruns), who admittedly did not represent absent certificateholders, was also completely co-opted by BofA, which agreed to pay it an $85 million fee to support the Settlement Agreement. These conflicted parties negotiated among themselves and deliberately excluded other certificateholders. And when certificateholder AIG pleaded for some information, the BNYM/BofA/Institutional Investors insisted on a wholly illegitimate condition: that AIG promise not to share the information with its counsel, Quinn Emanuel Urquhart & Sullivan, LLP. This is because they knew that Quinn Emanuel had seen Countrywide's loan files in a separate litigation and thus was aware that the breach rate was over 90%, more than double the 36% rate that was the predicate for the proposed settlement here.

Second, even if this conflicted, back-room, closed-door process had not occurred, its *outcome* cannot be endorsed without running roughshod over the absent certificateholders' interests that this Court has a duty to protect. The settlement amount, $8.5 billion, is a fraction of the $50 billion that even the conflicted Institutional Investors had initially demanded, and an even smaller fraction of the more than $100 billion in total losses the Institutional Investors estimated these Trusts will ultimately suffer. And the 36% breach rate that serves as the predicate for the $8.5 billion figure not only lacks support in any analysis of actual loan files (which analysis is absolutely industry-standard in every RMBS case), but was borrowed from BofA's past experience in the wholly inapposite Government Sponsored Entities ("GSE") context, which Freddie Mac's General Counsel deemed an "apples to oranges" comparison. The settlement also assumes away the possibility of recovery against BofA as successor to Countrywide, even though substantial evidence supports the theory and a New York jury recently found BofA liable for Countrywide's "Hustle" loan origination program.

While this Article 77 proceeding is the first case of its kind, it will not be the last. More are waiting in the wings. Recent public reports confirm that the same institutional investor group and its counsel have other global RMBS settlements like this one lined up for judicial approval. This Court has both the opportunity and the duty to create a precedent that teaches trustees and trust settlement proponents that they must act reasonably, responsibly, free from conflicts that compromise their judgment, and always in a manner that is in the best interests of the thousands of absent certificateholders whose rights will be affected. This settlement—which resulted from a process that reeks of collusion and is infected with countless disabling conflicts—should not become the hallmark of conduct for which future trustees strive, but rather the beacon for what should be avoided. Much is at stake for investors and this Court.

* * * * *

Although Respondents will discuss the relevant record evidence in more detail in the "Summary of Evidence" section below, an overview may be helpful to the Court. By the late summer of 2010, BNYM was under increasing pressure from investors for its do-nothing approach to massive losses suffered in Countrywide-issued RMBS for which it purportedly served as trustee and found itself in the crosshairs of Kathy Patrick and a group of high-powered, well-connected financial institutions. Ms. Patrick made it clear to BNYM that it had breached its duty to protect investors from massive losses caused by Countrywide's securitization of junk loans and BofA's bad servicing of those loans. BNYM called in its risk officers, who recognized the Trustee's significant downside risk. BNYM also called in its long time counsel, Mayer Brown, and tasked it with protecting BNYM, not certificateholders. As Respondents have shown (but only through hard-fought discovery and withering cross-examination), BNYM's first and enduring priority was to eliminate its own risk. At every turn, BNYM worked to avoid the heightened duties an Event of Default would have triggered, to secure indemnity and payment of all expenses from BofA, and to get released for as much of its past misfeasance as possible.

Likewise, RMBS investors were targeting BofA for Countrywide's now-infamous mortgage fraud debacle. The two banks needed each other: BNYM controlled the claims and BofA controlled the cash. To get what it needed, BNYM quickly sold out to BofA. Together, they hatched a back-room deal to co-opt Ms. Patrick and her investor group, to negotiate a secret low-ball settlement without investigating or valuing any of the claims, and to force it upon tens of thousands of investors who were deliberately excluded from the settlement negotiations.

The price of co-opting Ms. Patrick and the investor group was to pay Ms. Patrick's firm an $85 million fee, releasing the investors from their fee agreement with Ms. Patrick's firm; ensure hundreds of millions of dollars of recovery for the investor group, without regard to the actual prices they paid for their RMBS certificates; cover BNYM's expenses for which the investors became obligated to pay after sending "binding instructions" to BNYM in August 2010; and get the investor group and its lawyers a release from suits by certificateholders aggrieved by their role in this collusive and deceptive settlement. In exchange, the investors quickly dropped their $50 billion settlement demand and bid against themselves until reaching a number even lower than what BofA was willing to pay. If it was a negotiation, they caved; if it was a Kabuki, as one of the lead negotiators called it, they danced.

Having used its checkbook to gain control of BNYM and the investor group, BofA now had to ensure that no other certificateholders could meddle as the Settlement Proponents cooked up a low-ball deal. The most urgent problem was the impending Event of Default instigated by Ms. Patrick in order to get BNYM's and BofA's attention. If the 60-day cure clock ran, the Trustee would have heightened duties and would have to give notice to all certificateholders.

This would have invited "wildmen into the fray"— meaning other certificateholders who (unlike the investor group) were not conflicted and thus had the proper motivation and incentive to maximize a recovery from BofA. To avoid a situation where non-conflicted certificateholders might seek to become involved (and possibly scuttle their sweetheart deal), the Settlement Proponents did something unprecedented—they conspired to toll the 60-day cure period through a Forbearance Agreement, which tolling is nowhere authorized by the governing agreements. Recognizing the risk in deviating from its express duties, BNYM conditioned its agreement on receiving indemnity from BofA for failing to give notice of the Forbearance Agreement to certificateholders. Thereafter, BNYM knew that it could walk hand-in-hand with BofA with impunity. And it did.

The "triangular merger" of BofA, BNYM, and the investor group was negotiated by BNYM's outside counsel at Mayer Brown, a law firm for whom BofA was a "good client" and that also represented 10-12 of the Institutional Investors at the time. Mayer Brown claimed to resolve its obvious and ultimately debilitating conflict by obtaining a waiver from BofA, but the waiver prohibited Mayer Brown from suing BofA. Obviously, conflicted counsel was never going to create real leverage against its own client. BNYM would be negotiating with both hands tied behind its back and, as the record shows, jumped at the first opportunity to settle. Indeed, Mayer Brown described its role early on as "transactional" counsel.

BNYM's conflict and BofA's control manifested themselves at every turn. BofA paid for every one of BNYM's lawyers, advisors, and litigation experts and continues to do so to this day. It is no surprise, therefore, that they all would tell the Court that the settlement is reasonable, while having no facts to back up their BofA-serving conclusions.

But BNYM did far more than simply use experts to rubber-stamp the settlement. Rather, the record shows that BNYM and its conflicted counsel were the architects of the very opinions they rely on to support the settlement. The Settlement Proponents' argument that Countrywide's insolvency justifies the settlement amount is a perfect example of the charade that only the discovery process unveiled. BofA hired—through BNYM—a valuation firm to determine the net worth of Countrywide, but BNYM failed to task the firm with any real investigation and instead instructed the firm to assume away facts critical not only to determining Countrywide's real value but also to a meaningful analysis of BofA's liability as a successor to Countrywide. Then, BNYM hired a law professor to opine on the successor liability question, but—having no facts to which this heavily fact-dependent doctrine could be applied—he gave BNYM a meaningless opinion that it now uses as a reasonable basis for its collectability concern. Besides, the successor liability defense was all make-believe from the beginning. BofA continually pays Countrywide's repurchase claims, and expressly makes capital contributions to keep Countrywide solvent because a Countrywide bankruptcy would have "negative downsides and impacts to Bank of America." Even more telling is the fact that BofA's lead negotiator told a national television audience *during the negotiations* that BofA would honor valid repurchase claims. Notwithstanding these facts, BNYM's purported belief in the bankruptcy bluff demonstrates its willful blindness; its effort to sell it to the Court demonstrates its commitment to BofA.

BNYM's and the investor group's allegiance to BofA is also apparent from their abandonment of any investigation into the loan files and servicing records that are the key to unlocking tens of billions of dollars in repurchase, servicing, and document-related liability. They were the detectives who never showed up at the crime scene. Although both repeatedly emphasized the critical need for a loan file investigation from the outset, they quickly changed their tune once BofA indicated a willingness to settle and dangled the carrot in the form of an offer to pay all of their bills. Consequently, rather than investigate the loans in the actual trusts that they are trying to settle, BNYM and the investor group accepted BofA's concocted "GSE repurchase experience" as a proxy despite knowing that the "GSE repurchase experience" was wrong on many levels. Indeed, to quote one of those GSE's (Freddie Mac's) then General Counsel, using the GSE experience as a proxy was like comparing "apples and oranges," "totally irrelevant," and "not even worthy of discussion." On top of that, BofA built in an array of assumptions, selective adjustments, "judgmental quantifications," and unsupported discounts that any reasonable Trustee would have immediately recognized as a sham.

Nothing about this proposed settlement or the process by which it was reached merits the judicial approval and protection that the Trustee, BofA, and the Institutional Investors seek. The undersigned Respondents respectfully request the Court not approve the proposed settlement, and decline to enter the requested PFOJ findings.

SUMMARY OF THE EVIDENCE[2]

Events Leading Up to the Notice of Non-Performance Left BNYM Concerned About Its Own Liability Exposure

1. In summer 2010, BNYM knew that the Covered Trusts were suffering massive losses, Tr. (Lundberg) 4581:2-8, and that certificateholders wanted action to be taken to investigate, and ultimately to remedy, those losses. Tr. (Stanley) 3149:8-3150:6, 3151:15-3153:8; R-4073; R-4075. Rather than act, however, BNYM pointed to technical deficiencies in certificateholder demands to sit silent. R-4074; R-4076; R-146.

[2] For the full record, Respondents respectfully refer the Court to the trial record and to the objections and related briefs filed on May 3, 13, & 20, 2013. (Doc. Nos. 588, 771, 814). Triaxx also filed a Motion for Judgment During Trial pursuant to CPLR § 4401. (Doc. Nos. 945-949).

2. Although BNYM initially reacted to Gibbs & Bruns's June 17 and August 20, 2010 letters on behalf of the Institutional Investors in much the same do-nothing fashion, *see* R-146, BNYM clearly understood that the Institutional Investors believed the Trustee was contractually obligated to investigate the losses being suffered by certificateholders. Tr. (Bailey) 2262:4-2265:6; R-15; R-16. Douglas Chapman, chief risk officer for BNYM Corporate Trust, admitted that the August 2010 letter created potentially significant downside risk for BNYM. R-4151 at 12:9-19, 169:8-170:6, 172:6-9, 176:7-20, 237:10-25 (Chapman Dep.). In short, BNYM was well aware that it faced potential liability for its past inaction.

The October 18, 2010 Notice of Non-Performance, and BNYM's Prompt Retention of the Fatally Conflicted Mayer Brown

3. On October 18, 2010, Gibbs & Bruns sent BofA and BNYM a Notice of Non-Performance letter ("October 18 Notice") detailing the ways in which the BofA Master Servicer was in default of its obligations. R-17. The purpose of the Notice was to put pressure on both the Master Servicer and BNYM. Tr. (Kravitt) 1602:15-21, 1610:6-8.

4. In the first of many self-protective moves, BNYM quickly hired Jason Kravitt of Mayer Brown to represent it with respect to the October 18 Notice. Tr. (Kravitt) 1318:11-1319:6, 1563:2-1564:10. Mayer Brown was hired to represent BNYM as Trustee "full stop," not to represent the interests of the certificateholders. *Id.* at 1655:17-19; Tr. (Bailey) 2465:10-15. Any certificateholders not represented by Gibbs & Bruns were thus unrepresented during the ensuing settlement negotiations. Tr. (Kravitt) 1655:20-1656:5.

5. Mr. Kravitt understood his and Mayer Brown's job to include protecting BNYM from any liability for its actions, including lawsuits by the Institutional Investors or other certificateholders, and obtaining an indemnity for BNYM so that all its actions would be immune from liability. Tr. (Kravitt) 1654:3-15, 1675:26-1676:14, 1676:26-1677:4, 1680:18-24.

6. Acknowledging the inherent conflict created by tasking counsel with protecting BNYM from liability for its past inaction while at the same time pursuing relief (on behalf of certificateholders) that BNYM should have pursued earlier, Mr. Kravitt conceded that what is good for BNYM may not necessarily be the same thing as what is good for the interests of the trusts. Tr. (Kravitt) 1675:14-17. Yet he did not recommend that BNYM retain independent counsel or other counsel to protect the interests of the certificateholders. *Id.* at 1675:19-25.

7. Consistent with its mandate to represent and protect BNYM, Mayer Brown repeatedly sought a broad release for BNYM's conduct in connection with its administration of the Covered Trusts. See Tr. (Kravitt) 1885:13-23, 1887:4-10, 1888:5-1889:8; R-118 at 003 ¶ d; R-119 at 008 ¶ q; R-235. Even Gibbs & Bruns acknowledged that the Trustee's language regarding a broad release "creates a conflict for the Trustee . . . ." R-210 at 007.

8. At the time Mayer Brown was hired, it separately represented BofA and 10-12 of the Institutional Investors, and could not represent BNYM without obtaining conflict waivers. Tr. (Kravitt) 1561:8-1562:5, 1575:2-24; R-724; R-725; R-1072.

9. In a February, 2011 e-mail to a representative of Goldman Sachs (one of the Institutional Investors) seeking Goldman Sachs' conflict waiver, Mr. Kravitt described BofA as his firm's "good client." R-1240; Tr. (Kravitt) 1689:25-1690:10. As its conduct ultimately demonstrated, Mayer Brown would do nothing to ruffle the feathers of its "good client."

10. Mr. Kravitt conceded that the conflict waiver letter executed by BofA did not allow Mayer Brown to represent BNYM in a lawsuit against BofA. Tr. (Kravitt) 1573:19-1574:26. In a phone call between Mr. Kravitt and Jana Litsey of BofA, Ms. Litsey made clear that the waiver did not extend to Mayer Brown representing BNYM to pursue litigation against BofA. *Id.* at 1582:19-1583:25. BNYM did not even know if Mayer Brown could represent

BNYM in replacing the Master Servicer, a BofA entity. *Id.* at 1597:18-1598:21. In other words, BofA knew that it was dealing with a firm, Mayer Brown, that was powerless to take any action adverse to it and that had no real negotiating leverage. Indeed, Mr. Kravitt approached the matter not as potential litigation to enforce Trust rights but as a "transaction" or "work-out." R-44; Tr. (Kravitt) 1490:19-23, 1513:22-1514:22.

11. Just as remarkably, BNYM proceeded to retain Mayer Brown without notifying certificateholders of the conflicts. Tr. (Kravitt) 1578:12-1579:5, 1593:19-1594:14. This failure is in stark contrast to its September 3, 2010 response to Gibbs & Bruns's August 20 letter, in which BNYM stated that, before hiring contingency counsel, it "would want, at a minimum, to notice all certificateholders of the proposed engagement to enable them to express any concerns that they might have." R-146 at 003.

BNYM and Mayer Brown Immediately Focused On a Settlement

12. On November 3, 2010, Mr. Kravitt flew to Houston, Texas to meet with Kathy Patrick for the first time. Tr. (Kravitt) 1321:22-1322:21. BNYM's former in-house counsel admitted that BNYM sent Mr. Kravitt to Houston to see if there could be a negotiated settlement of the claims against BofA and Countrywide. Tr. (Bailey) 2299:2-17.

13. During that meeting, Mr. Kravitt and Ms. Patrick agreed that the best strategy would not be to "wage war," but rather to "play by the book" by engaging in a "well constructed and planned investigation." R-1451 at 002. The "investigation" he was referring to was a loan file review. Tr. (Kravitt) 1691:17-1692:14. It turned out, however, that the critical loan file review was quickly abandoned without a single loan ever reviewed, and the so-called "investigation" was nothing more than a half-hearted process that BNYM hoped would provide just enough cover for a much lower than justified settlement.

14. The first meeting between representatives of BNYM, the Institutional Investors, and BofA/Countrywide (collectively, "Settlement Proponents") occurred on November 18, 2010. Tr. (Kravitt) 1343:13-1344:11, 1628:13-16. Right out of the gate, Mr. Kravitt raised the possibility of settlement. *Id.* at 1345:12-14. BofA was all too happy to go along and even expressed its interest in having the settlement extend beyond just the trusts in which the Institutional Investors held 25% of the voting rights. *Id.* at 1354:22-1355:22, 1470:17-1471:10. BNYM and Ms. Patrick were quite interested in a larger, broader settlement, especially since for BNYM it provided the Trustee with greater protection from claims against it, and for Ms. Patrick it offered a much bigger pay day.

15. Remarkably, within two days following the Settlement Proponents' first meeting, Mr. Kravitt e-mailed BofA's counsel to solicit input on how BofA wanted the much larger settlement constructed and how to make it "bullet proof." R-44 at 001; Tr. (Kravitt) 1628:13-1632:17, 1636:24-1637:21. BNYM was willing to discuss a settlement involving as many trusts as BofA wanted, even though BNYM had not received a certificateholder direction for those trusts. Tr. (Kravitt) at 1634:5-8, 1634:18-1635:6.

16. In addition to making sure the settlement would accomplish BofA's goals, and consistent with his objective of protecting BNYM, Mr. Kravitt e-mailed BofA's counsel to ask whether the settlement would resolve allegations over BNYM's failures to comply with its document certification duties and to what extent the proposed settlement would protect BNYM from future claims by investors and borrowers. R-58 at 003; Tr. (Kravitt) 1894:25-1895:21.

17. Following the November 18, 2010 meeting, BofA lead negotiator Terry Laughlin initiated private meetings with three leaders of the investor group, PIMCO, WAMCO, and

BlackRock. Mr. Laughlin did not invite counsel for the Trustee or the Gibbs & Bruns firm, and was the lone attendee for BofA. Tr. (Laughlin) 697:15-699:7, 736:8-739:7.

18. By December 2010, Mr. Kravitt knew there was a "good chance" of a settlement. Tr. (Kravitt) 1720:18-1721:3.

BNYM Acted in its Own Self-Interest By Entering the Forbearance Agreement and Attempting to Avoid the Event of Default

19. BNYM knew that the October 18 Notice identified "events that, if true and absent a cure, will become Events of Default." R-1458 at 020. BNYM operated as though the October 18 Notice triggered the 60-day cure period in PSA § 7.01(ii). Tr. (McCarthy) 4991:26-4992:8.

20. On cross-examination, Mr. Kravitt conceded that, *if* the Trustee had been "looking for leverage" against BofA, then BNYM may have wanted an Event of Default to occur. Tr. (Kravitt) 1505:2-11. However, the Trustee was not looking for leverage: it was looking to "AVOID" an Event of Default, because having one outstanding was not in BNYM's "self interest." R-1444 at 001; R-1445 at 001.

21. If an Event of Default occurred, the Trustee (1) would be subject to a prudent person standard, Tr. (Kravitt) 1504:4-7; (2) would have to consider replacing the Master Servicer, which it viewed as a very difficult decision, *id.* at 1335:17-1336:15; and (3) would be required to provide notice to certificateholders of an Event of Default. *Id.* at 1683:3-10; Tr. (Lundberg) 4609:10-14.

22. An Event of Default is a "very big deal" and a "serious issue for" the Trustee. Tr. (Bailey) 2325:24-26; Tr. (Lundberg) 4577:14-22. An Event of Default "would have entailed an enormous amount of work and decision-making" by the Trustee. Tr. (Kravitt) 1335:17-1336:15. The Trustee was concerned about what it would have to do, what the Institutional Investors

might do, and what other certificateholders might do if an Event of Default occurred. Tr. (McCarthy) 4988:22-4989:12.

23. Certificateholders, in contrast, benefit from an Event of Default because they then have a Trustee subject to a prudent person standard managing the trust assets, receive notice of the Event of Default, and have the right to demand that the Trustee take action to remedy the Master Servicer's defaults. If the Trustee fails to do so, certificateholders have the right to take direct action against the Master Servicer. R-13 §§ 7.03(b), 8.01, 10.08. Despite the benefits of an Event of Default for certificateholders, BNYM "act[ed] quickly" and "work[ed] hard" to avoid one. Tr. (Kravitt) 1569:3-26, 1733:14-26; Tr. (McCarthy) 4988:13-15, 5014:25-5015:16.

24. BofA and BNYM's interests were aligned, but contrary to the certificateholders' interests, in wanting to avoid an Event of Default. Tr. (Kravitt) 1504:18-1505:3.

25. BNYM's efforts to avoid an Event of Default eventually resulted in the Forbearance Agreement. R-46. The Forbearance Agreement, signed by counsel for BNYM, BofA, and the Institutional Investors on December 9, 2010, purports to toll the 60-day cure period triggered by the October 18 Notice. *Id.*

26. This Forbearance Agreement had no basis in the governing contracts, which do not contemplate that BNYM can change the 60-day cure period. Tr. (Kravitt) 1570:2-11; R-13. BNYM thus was brazenly acting without contractual authority or certificateholder consent when it agreed to the Forbearance Agreement.

27. In the early negotiations of the Forbearance Agreement, the Trustee and BofA had a different view than the Institutional Investors of what the Forbearance Agreement should accomplish. Ms. Patrick explained in a December 2, 2010 e-mail that her clients were "not *lengthening* the 60 day cure period" started by the October 18 Notice. Rather, the Institutional

Investors were agreeing not "to send a second notice demanding that the Trustee take action to remedy the Event of Default." R-50 (emphasis in original); Tr. (Kravitt) 1361:20-1362:3.

28. Mr. Kravitt e-mailed both BofA's counsel and his client to express concern about Ms. Patrick's position, writing "Oy. . . . The [Forbearance Agreement] should prevent an EOD from occurring for a period of time; not tie one group of [certificateholders'] hands with regard to an EOD that is claimed to be outstanding." R-50.

29. Mr. Kravitt similarly e-mailed BNYM's Deputy General Counsel, Kevin McCarthy, describing Ms. Patrick's position as follows: "This may be disturbing. This means there IS, in [Ms. Patrick's] opinion, an [Event of Default], and this specific group of [certificateholders] is forbearing from exercising their rights with regard to it. What if another group chooses to do so? It would not be precluded from doing so. Further, if there is an [Event of Default], then the Trustee's standard of care changes to a prudent man standard." R-1445.

30. Mr. Kravitt went on in his e-mail to Mr. McCarthy: "I don't think it is in Kathy's interest to actually have an [Event of Default] outstanding. For one reason, it allows other 'wildmen' to jump into the fray, and it starts BONYM on a track to figure out on its own if it should replace the [Master Servicer.]" R-1445 at 001.

31. "Wildmen" was a pejorative reference to other certificateholders not in the Gibbs & Bruns group. Tr. (McCarthy) 5019:10-5020:7. Mr. Kravitt believed that such certificateholders, who were not conflicted or beholden to BofA and would push for loan files and a maximum recovery for all injured investors, could destabilize the negotiations between BofA and the Institutional Investors and somehow "jump into the fray." Tr. (Kravitt) 1748:9-14. But an easy, stable negotiation was only in BNYM's and BofA's interest—it was not in the interest of the certificateholders who had suffered massive losses due to Countrywide's breaches.

32. Certificateholders who attempted to get in on the negotiations were kept out. In one of the most telling and egregious examples of keeping unconflicted investors out of the fray, AIG, in March 2011, asked BofA for information regarding the status of BofA's discussions with the Institutional Investors. BofA responded that it would consider allowing AIG a "window" into the discussions, but only on two conditions: (1) that AIG not involve in any way its long-time RMBS counsel Quinn Emanuel in the process, and (2) that AIG promise not to share any information with Quinn Emanuel that it learned during the process. R-4159. At the time, BofA imposed these ridiculous conditions on AIG, BofA was well aware of Quinn Emanuel's deep involvement in the MBIA versus Countrywide litigation, in which Quinn Emanuel had actually examined Countrywide's loan files in MBIA's case against Countrywide and knew of the incredibly high incidence of breaches of representations and warranties. Thus, BofA—which already had secured agreements from BNYM and the Institutional Investors not to seek a loan file review and use the "GSE experience" as a proxy—desperately wanted to keep Quinn Emanuel out of the process and eliminate the risk that Quinn Emanuel, with its superior knowledge of the true Countrywide breach rates, would derail the sweetheart settlement that was effectively a done deal at that juncture. AIG explained that it could not agree to the conditions and was never afforded a "window" into the discussions or provided any information until the settlement was publicly announced.[3]

33. Similarly, when Walnut Place sought authorization from BNYM to pursue a separate lawsuit against Countrywide on just one of the Covered Trusts, counsel for the Institutional Investors stated to BNYM that their clients were "concerned that efforts by others

[3] During opening statements, Ms. Patrick represented to the Court that AIG had been invited into the settlement discussions and declined. Tr. 165:3-5. This was a grossly misleading statement by Ms. Patrick in light of the undisputed facts, as set forth herein, that BofA imposed unreasonable and unacceptable conditions on AIG.

could interfere with or derail the ongoing settlement discussions[.]" R-19 at 002. BNYM never did authorize a separate lawsuit apart from the global settlement discussions.

34. Mr. McCarthy responded to Mr. Kravitt's concern about Ms. Patrick's view of the Forbearance Agreement: "Jason-I think you need to speak with Kathy [Patrick] directly to clear this up before it goes sideways. If she is under the belief that there is an [Event of Default] outstanding . . . then we have a real problem because that is not the assumption that we have been operating under—we have [been] working hard to AVOID a formal declaration of an [Event of Default]." R-1445 at 001 (emphasis in original).

35. The Institutional Investors ultimately agreed to the Trustee's and BofA's approach to the Forbearance Agreement, and purportedly tolled the 60-day cure period. R-46. As part of the Institutional Investors' "consideration" for the Forbearance Agreement, BofA and BNYM agreed that the Institutional Investors would not have to pay the Trustee's legal fees, or otherwise indemnify BNYM, under PSA § 8.05. R-46 at 002; Tr. (Kravitt) 1510:26-1512:4.

BNYM Benefited from Its Indemnity Agreements with BofA

36. Recognizing that it lacked a legal basis to alter the 60-day cure period, BNYM negotiated a separate Indemnity Agreement with BofA on December 10, 2010, one day after execution of the Forbearance Agreement. R-52. Under the terms of the Indemnity Agreement, the BofA Master Servicer agreed to "pay the reasonable legal fees and expenses that the Trustee incurs (or has incurred) in connection with its counsel's participation in, and planning with regard to, ongoing discussions regarding the October 18 Letter[.]" *Id.* at 001. This included indemnifying BNYM for "liabilities of any kind . . . that may be imposed upon, incurred by or asserted against the Trustee that arise solely out of its entry into the Forbearance Agreement." *Id.*

37. Receiving the indemnity was important to BNYM. Tr. (McCarthy) 5008:17-23, 5009:14-16. Indeed, when Ms. Patrick first proposed a draft of the Forbearance Agreement with BofA providing an indemnity, Mr. Kravitt responded by saying, "Thanks for the indemnity. I appreciate it." R-1220 at 001. BNYM needed an indemnity because without one it did not have the assurance that BofA would pay for its settlement activities. Tr. (Kravitt) 1637:5-21. In a December 9, 2010 e-mail, Mr. Kravitt told counsel for BofA that "BNYM won't release me to sign [the Forbearance Agreement] until they get a signed indemnity." R-62 at 001; Tr. (Kravitt) 1772:16-24. Unlike with the indemnity provided in the PSAs, BNYM now knew that its multi-million dollar legal fees as well as its potential liability to other certificateholders for its failure to provide notice would be covered and that there would not be a dispute about who is paying the bills. It would be BofA. The Indemnity Agreement thus provided a comfort and a benefit to BNYM. Tr. (Kravitt) 1776:7-19.

38. BNYM was not content with just the December indemnity, however. In June 2011, when BNYM and BofA executed the proposed Settlement Agreement, they also entered a "Side Letter" agreement in which BofA agreed to indemnify BNYM for *all* of its settlement conduct, as well as BNYM's advocacy for and performance of the proposed Settlement Agreement. That indemnification continues through today. Tr. (Kravitt) 1774:7-19.

39. The Side Letter also contains an additional guaranty found nowhere in the PSA and which was, therefore, an added benefit to the Trustee. Under the Governing Agreements, only the Master Servicer entity—BACHLS—has to indemnify the Trustee. Under the Side Letter, Bank of America Corporation, the corporate parent of BACHLS, guarantees the Trustee's indemnification. R-5 at 004.

40. BNYM knows that, when a trustee seeks an indemnity, it may not be in the best interests of certificateholders because the very purpose of the indemnity is to protect the trustee from liability to the certificateholders. Tr. (Kravitt) 1654:16-24. That is clearly the case here, as the Side Letter and December 2010 Indemnity Agreement—from the putative defendant—protect BNYM for its decision not to give notice to certificateholders in December 2010, the decision to enter the Forbearance Agreement, the decision to stop the Event of Default clock, the decision to allow Ms. Patrick to negotiate the settlement for all of the trusts (including the many in which the Institutional Investors held less than 25% of the voting rights), and the failure to investigate the claims being settled. *Id.* at 1495:6-1496:19, 1510:14-25.

41. Under the terms of the indemnity agreements, BofA has paid and continues to pay all of BNYM's attorneys' fees in connection with the Article 77 proceeding. BofA also has paid all of BNYM's advisors and litigation experts. Tr. (Kravitt) 1517:9-1518:14.

BNYM's Decision to Forego Certificateholder Notice Was Self-Interested

42. In December 2010, BNYM considered giving notice to certificateholders about the ongoing settlement discussions. Tr. (Kravitt) 1685:7-1687:16. But BofA strongly opposed the giving of notice, instead wishing to negotiate without interference from "wildmen" and then to present the settlement as a *fait accompli*. *Id.* at 1766:17-21. BNYM informed BofA that it would factor any indemnity BofA agreed to provide into BNYM's decision whether to give notice. *Id.* at 1764:20-1765:9. In a December 1, 2010 e-mail to BofA's lawyers at Wachtell Lipton, Mr. Kravitt wrote that he and BNYM "agreed that you made some very good points on the notice to [certificateholders]. It would help us considerably in our decision making process to put aside such notice if indeed we received the very narrow liability indemnity that we discussed with you this afternoon." R-53. Thus, again, BofA bought BNYM's cooperation.

43. As a result of receiving the December indemnity, BNYM made the conscious decision not to provide any notice of the settlement negotiations or the Forbearance Agreement to certificateholders until after it had signed the proposed Settlement Agreement, even though it was capable of doing so. Tr. (Bailey) 2194:16-20; R-4152 at 151:4-152:24 (Crosson Dep.). BNYM knew that press releases did not constitute notice under the PSAs. Tr. (Bailey) 2392:3-8. Having secured BNYM's agreement not to give notice, the parties were able to continue their discussions in secret and without any outside scrutiny. Consequently, absent certificateholders, including substantial holders like AIG, were completely unaware that the settlement being negotiated was one that would be binding on all certificateholders, and would release all of their potential putback claims.

BNYM Did Not Actively Participate in the Settlement Amount Negotiations, Even as the Institutional Investors Bid Against Themselves

44. In a stunning dereliction of duty, BNYM allowed the Institutional Investors to negotiate the settlement, including for RMBS trusts in which they lacked 25% voting rights. Tr. (Kravitt) 1496:13-19. BNYM representatives thus "were more observers than participators" during negotiations. R-4142 at 17:14-18:5, 260:17-23 (Bostrom Dep.).

45. On April 11, 2011 the Institutional Investors presented their analysis of BofA/Countrywide's repurchase exposure for 543 Countrywide trusts. PTX 604; Tr. (Smith) 386:19-22, 391:21-392:4. The Institutional Investors' estimated range of the repurchase exposure was $27 billion to $52.6 billion. Tr. (Smith) 629:9-18; PTX 604. Of the scenarios presented by the Institutional Investors in PTX 604, $32 billion was their best estimate of the repurchase exposure. Tr. (Smith) 404:19-405:8. However, at the end of the meeting, they inexplicably demanded only $12 billion. *Id.* at 393:5-9.

46. On April 18, 2011, the Institutional Investors and BofA met again. Tr. (Smith) 393:10-13. During that meeting, Terry Laughlin, on BofA's behalf, said that any demand would have to be below $10 billion for BofA's board to consider it. *Id.* at 398:9-14.

47. In response to Mr. Laughlin's comment, the Institutional Investors lowered their demand to $9.8 billion. Tr. (Smith) 398:15-16. The Institutional Investors then "pretty immediately withdrew" that demand and demanded $8.5 billion. *Id.* at 398:17-20. Thus, in the course of a few hours, the Institutional Investors dropped their demand from the already low-ball figure of $12 billion to the ridiculously low level of $8.5 billion—and did so without even consulting the Trustee or its counsel.

48. Before the April 18 session, Mr. Kravitt emailed Ms. Patrick and Mr. Koplow (who represented BofA) to say the Trustee was "fine with the 'lawyers talking with lawyers' process, provided [Mr. Ingber] and/or I can sit in as well." Mr. Kravitt went on to say "Again, we'd like to be able to say that we 'watched' the whole thing and it was clearly hard fought arms length." Tr. (Kravitt) 1848:15-1851:19; R-90.

49. Nonetheless, Mr. Kravitt failed to perform even this bystander's role. He was not present at the final negotiating session where BofA and the Institutional Investors agreed to the $8.5 billion, nor was any other BNYM representative. Tr. (Kravitt) 1471:11-20, 1850:4-1852:4.

50. The absent BNYM did not approve any of the Institutional Investors' settlement offers—or downward moves—before they were sent to BofA. Tr. (Bailey) 2250:12-26. Incredibly, BNYM never made any settlement offers. *Id.* at 2254:13-20. Thus, rather than using the rights and leverage it had to maximize the Trusts' recovery, BNYM was a potted plant.

51. Perhaps BNYM did not want an active negotiating role because BofA was one of its largest clients and accounted for over half of BNYM's MBS business. Tr. (Stanley) 3135:15-

3136:18, 3144:7-13, 3146:19-26. Even during settlement talks, BNYM was attempting to generate additional revenue from BofA, including through a meeting of high-level BNYM and BofA personnel. *Id.* at 3138:16-25, 3145:3-3146:2. Whatever the reason for its decision to be absent from the settlement discussions, the Trustee provided no dollar limits to the Institutional Investors and effectively abdicated full responsibility to their counsel (Kathy Patrick) to arrive at a final number. Aside from the patently obvious and admitted fact that those financial institutions were acting solely in their own self-interest, and not for the interest of absent certificateholders, their lawyer had been completely co-opted by BofA, which agreed to pay her a staggering $85 million fee if the settlement were accepted and approved—regardless of the amount of time she and her law firm expended.

<u>The "Threat" to Put Countrywide into Bankruptcy and the Claimed Successor Liability Defense Were Inconsistent with BofA's Actions</u>

52. During a February 2011 meeting, BofA's chief negotiator Terry Laughlin supposedly threatened that BofA would put Countrywide into bankruptcy if the repurchase liability got too high. Tr. (Laughlin) 717:19-718:8.

53. In fact, abundant publicly-available evidence, which BNYM ignored, showed that, far from bankrupting Countrywide, BofA was paying Countrywide's debts. Moreover, during the settlement negotiations, Mr. Laughlin stated on national television that BofA would honor valid repurchase claims. R-341; Tr. (Laughlin) 790:23-791:21, 794:7-24. And there is no evidence in the record that BofA has ever stated in any of its corporate filings that it was considering putting Countrywide into bankruptcy. Mr. Laughlin further admitted on cross-examination that there would be "negative downsides and impacts to Bank of America" and its shareholders if BofA tried to bankrupt Countrywide. Tr. (Laughlin) 734:23-735:12.

54. BofA makes capital infusions into Countrywide to "maintain the capitalization of the company," including to pay repurchase claims for private-label deals like the Covered Trusts. Tr. (Laughlin) at 796:11-797:6; Tr. (Scrivener) 1187:6-18. BofA has already paid billions of dollars for settlements related to Countrywide loans. Tr. (Laughlin) 730:24-731:7.

55. In her opening statement, Ms. Patrick represented to the Court that BofA's Terry Laughlin had advised the Institutional Investors and BNYM that BofA had already sought and received approval from the Office of the Comptroller of the Currency ("OCC") to put Countrywide into bankruptcy. Tr. 177:12-17. But the truth was just the opposite and showed Ms. Patrick's representation to the Court to be a complete falsehood: Mr. Laughlin testified that he advised the Institutional Investors and BNYM that BofA had *not* sought any such approvals. Tr. (Laughlin) 782:8-783:19.

BNYM Did Not Conduct a Factual Investigation of the Loans in the Covered Trusts

56. Mr. Laughlin admitted that a "sampling of the loan files" could be used to "size a claim." Tr. (Laughlin) 747:24-748:5.

57. A loan file review is the norm in RMBS litigation. Tr. (Burnaman) 2890:7-15, 2977:8-12; Tr. (Cowan) 4103:3-23. In fact, from the outset of their discussions, the Institutional Investors and BNYM agreed that a loan file review was critical to their pursuit of a recovery from BofA. SOE ¶ 13, *supra.*

58. BNYM has the contractual right to access "all records and documentation regarding the Mortgage Loans," without charge. R-13 § 3.07. BNYM knew it had a contractual right to loan files. Tr. (Kravitt) 1466:6-13. BNYM's counsel even concluded that demanding loan files would put pressure on BofA and that BNYM would be successful in a lawsuit against BofA to obtain loan files. Tr. (Kravitt) 1466:14-1467:6. Yet in another example of BNYM giving away its leverage over BofA, BNYM never requested any loan files. *Id.* at 1468:7-24.

BNYM's decision not to get loan files was made in part because BofA did not want to provide them. *Id.* at 1466:2-5; Tr. (Laughlin) 743:5-10. Thus, rather than press for loan files—or even a sampling of loan files, as New York courts have accepted—BNYM and the Institutional Investors agreed not to ask for loan files and to use the inapposite GSE experience as a proxy. *See* SOE ¶¶ 60-70, *infra*.

59. In addition, even though the December Indemnity Agreement was supposed to protect BNYM from liability for its conduct in the settlement negotiations, BNYM did not know whether BofA would agree that the indemnity covered a loan file review if BNYM or the Institutional Investors had ever requested one. Tr. (Kravitt) 1811:9-1813:3.

BNYM's Settlement Amount Advisor Relied on Unverified Assumptions Provided by Bank of America to Determine a Purportedly Reasonable Settlement Range

60. As a consequence of BNYM failing to obtain loan files, BNYM's settlement amount advisor, Brian Lin, did not look at any loan files in purporting to calculate a reasonable settlement range. PTX 444 at 109. This omission was remarkable, since Mr. Lin had never before calculated a breach rate without looking at loan files. Tr. (Lin) 3978:9-16.

61. Rather than using loan files to determine a purportedly reasonable settlement range, Mr. Lin blindly accepted BofA's data without verification, including BofA's 14% defect rate. Tr. (Lin) 3871:21-3872:20. The 14% defect rate equals a 36% breach rate multiplied by a 40% success rate, *id.* at 3873:9-22, and includes the false assumption that the repurchase remedy evaporates after two years. R-4143 at 229:6-230:6 (Robertson Dep.). Mr. Lin adopted the 36% breach rate and 40% success rate in whole, and applied them across all collateral types. PTX 444 at 110.

62. When he accepted BofA's estimates, Mr. Lin knew that BofA had an interest in the outcome of the dispute and that BofA was the entity that would pay the settlement amount.

Tr. (Lin) 3885:22-3886:22, 3940:14-16, 3941:9-12. Mr. Lin also knew that there was no historical information that could be used to confirm BofA's estimates. *Id.* at 3934:22-3935:9, 3935:12-3936:13. Mr. Lin does not know the margin of error of the 36% assumed breach rate. *Id.* at 3937:6-22, 3938:7-18. In short, Mr. Lin's so-called investigation was a sham.

The BofA Assumptions Were Accepted Wholesale by BNYM Even Though Premised on an Irrelevant, Inapplicable, and Incomplete GSE Repurchase Experience

63. BofA's analysis of its repurchase exposure in the Covered Trusts was based on its claimed GSE repurchase experience. Tr. (Scrivener) 1033:17-1034:7; Tr. (Lin) 3919:18-23. That repurchase experience is completely inapplicable to the Covered Trusts, which are private-label deals. Robert Bostrom, who participated in the settlement negotiations as Freddie Mac's General Counsel and in the GSE repurchase experience, testified that the Institutional Investors' response to BofA's GSE repurchase experience proxy was "a clear dismissal that [it was] not relevant, they were different loans, they reflected different quality of loans, different repurchase history, different origination channels, they were not the traditional Freddie/Fannie conforming loan mix, it was a totally different thing and, therefore irrelevant." R-4142 at 99:16-100:3 (Bostrom Dep.). According to Mr. Bostrom, "[t]he belief was that [BofA] [was] picking a lowball number based upon loans that had no bearing or relevance to the quality and underlying pools of loans in the PLS portfolios." *Id.* at 97:8-13. Mr. Bostrom recalled the Institutional Investor group calling the comparison, "apples to oranges," *id.* at 261:19-262:16, and "just so totally out of line as to not even be worthy of discussion." *Id.* at 263:2-16.

64. Even BNYM's advisors recognized the incomparability of the GSE repurchase experience to private-label securitizations such as the Covered Trusts. PTX 444 at 106-07; R-363 at 97-98. Yet BNYM just went along with whatever BofA said, no matter how preposterous.

65. BofA claimed to make certain adjustments to the GSE repurchase data to account for collateral type differences between GSE loans and the loans in the Covered Trusts. Tr. (Scrivener) 1102:15-1103:26. But those minor adjustments were based on assumptions and "judgmental quantifications," *id.* at 1103:2-26, 1116:5-24, and thus failed to solve the apples-to-oranges problem.

66. There are also loan-level differences between the GSE loans and the loans in the Covered Trusts, including loan size, credit quality, loan-to-value ratio, and documentation type. Tr. (Burnaman) 2865:11-2871:18. These credit risk attributes are relevant to the likelihood of breaches of representations and warranties. Tr. (Lin) 4021:10-16, 4024:8-4027:12. Nonetheless, BNYM's Mr. Lin undertook no effort to quantify the correlation between the credit risk factors and the likelihood of breaches. *Id.* at 4027:13-25.

67. Mr. Lin accepted data from the GSE repurchase experience despite having zero personal knowledge of the GSE repurchase experience, data, process, or considerations. Tr. (Lin) 3937:6-22, 3938:7-18, 3998:4-12.

68. The GSEs themselves recognized that using their repurchase experience as a proxy for private-label loans is misleading because their repurchase decisions were based in part on business considerations. In a November 15, 2010 letter to the SEC, the General Counsels to Fannie Mae and Freddie Mac reported that the GSEs' "decision whether to pursue a remedy with respect to the seller of the loan and, if so, which remedy to pursue, is based on a number of internal business and policy considerations." R-566 at 005; R-4142 at 82:11-84:3 (Bostrom Dep.).

69. In September 2011, FHFA's Office of Inspector General reported that (1) Freddie Mac's methodology for identifying defective loans failed to capture all loans subject to

repurchase, and (2) Freddie Mac's business relationships with loan sellers like BofA "was a factor weighing against implementing more expansive loan review and repurchase policies." R-201 at 027.

70. BNYM knew the GSE repurchase experience was not even complete when it accepted it as a proxy and even after it was complete, BNYM neither conducted nor demanded a recalculation of the estimated settlement range. Tr. (Scrivener) 1158:19-24; Tr. (Lin) 4014:15-17; Tr. (Burnaman) 2842:13-2845:21.

Mr. Lin's Estimated Settlement Range Suffered From Other Material Flaws

71. Mr. Lin's analysis only captured losses that are the result of loan-level default. Tr. (Lin) 4018:18-20. Investors are materially and adversely affected, however, by events other than and in addition to default. Tr. (Waterstredt) 917:6-12.

72. The Covered Trusts are private-label securitizations, but Mr. Lin did not have any information regarding BofA's repurchase experience with private-label securitization trustees. Tr. (Lin) 3922:18-24. BofA maintains a claims database that tracks repurchase information for private-label transactions, Tr. (Scrivener) 1084:5-23, 1085:8-13, 1087:24-1088:18, and that can be used to identify loans with an increased likelihood of being defective. *Id.* at 1149:15-1150:19. But, by burying their heads in the sand and willfully blinding themselves to reality, neither Mr. Lin nor any of the Settlement Proponents ever asked for this data.

BNYM Summarily Rejected Data That Would Have Supported A Higher Settlement Amount

73. The Institutional Investors, despite being conflicted themselves, presented an alternate damages analysis to BofA's presentation. PTX 604. The Institutional Investors' analysis was based on a forensic re-underwriting of 250,000 private label loans, similar to those in the Covered Trusts. Tr. (Lin) 3944:2-17.

74. The Institutional Investors estimated losses to the Covered Trusts of more than $100 billion, and supported their estimates with back-up information. R-22; R-150-153. The Institutional Investors also estimated breach rates between 50% and 65%, and success rates between 60% and 75%. PTX 604.

75. Mr. Lin reported to BNYM that the Institutional Investors' analysis had more advantages and less disadvantages than BofA's analysis. PTX 444 at 103, 106. BNYM's litigation expert found the Institutional Investors' approach to be reasonable. Tr. (Burnaman) 2822:13-2823:11.

76. Nonetheless, and in yet another obvious example of his head-buried-in-the-sand approach, Mr. Lin used a loss estimate of $61.3 billion to $76.8 billion, $25-40 billion lower than the Institutional Investors' loss estimate.[4] PTX 444 at 110. Mr. Lin also accepted the 36% breach rate and 40% success rate derived from BofA's 14% defect rate, assuming them to be correct without verification. Tr. (Lin) 3872:22-3873:22, 3935:12-3936:13.

<u>BNYM's Use of Advisors Was Unreasonably Narrow and Limited</u>

77. With the exception of Mr. Lin (who was hired in February 2011), all of BNYM's pre-settlement advisors were hired and performed their work in late April 2011 or later, *after* the parties had already agreed on the $8.5 billion Settlement Amount. Tr. (Kravitt) 1857:14-1858:3; Tr. (Bingham) 4478:26-4479:3. Their analysis was thus entirely a *post hoc* justification for a settlement already reached. And their analysis was equally if not more deficient than Mr. Lin's.

Professor Robert Daines

78. The Trustee hired Professor Daines to consider two fact-intensive legal theories (veil piercing and successor liability) which BNYM could have used to seek recovery directly

[4] Mr. Lin acknowledged that total loss is one of the most important calculations in estimating BofA's repurchase liability. Tr. (Lin) 3964:22-3965:9. Yet BNYM never questioned that his loss estimate was as much as *$40 billion* lower than the Institutional Investors' estimate. Tr. (Stanley) 3176:7-16.

from BofA. PTX 444 at 18. Incredibly, the Trustee did not ask Professor Daines to look into any facts relevant to the legal theories, Tr. (Daines) 3305:6-21, and he did not independently verify any facts. *Id.* at 3316:13-17, 3351:15-20.

80. While the Trustee asked Professor Daines to give his general and factually uninformed views on successor liability, there is no evidence the Trustee investigated or evaluated the viability of fraudulent conveyance claims or fiduciary duty claims brought in connection with the Countrywide acquisition. The Trustee also never investigated the strength of either the patently obvious contractual successor liability claims available under PSA §§ 6.04 and 6.02, or a direct liability claim against BofA. Tr. (Coates) 4822:24-4828:14, 4794:6-23.

81. BNYM did not ask Professor Daines to help the Trustee develop the best possible successor liability case against BofA. Tr. (Daines) 3306:18-23, 3308:8-23, 3314:19-3315:2, 3316:24-3317:4.

Capstone Valuation Services

82. The Trustee hired Capstone Valuation Services to "opine on the maximum economic value that BNYM could recover from Countrywide . . . assuming a hypothetical judgment . . . for certain claims." PTX 444 at 5.

83. The Trustee artificially limited the scope of Capstone's work by instructing it to assume: (1) there was no basis on which a court could pierce the corporate veil to reach BofA, (2) Countrywide was solvent at the time of the transactions, and (3) BofA paid reasonably equivalent value for Countrywide's assets. Tr. (Bingham) 4484:8-25, 4513:10-17, 4524:17-23. In other words, Capstone was to assume that BofA had no successor liability, not to undertake any analysis of that key issue.

84. Although Capstone was capable of valuing an asset-stripping claim against BofA, the Trustee did not hire it to do so. Tr. (Bingham) 4510:17-24. Capstone was also capable of,

but was not hired to, value potential litigation claims and claims that could be brought against BofA in a potential bankruptcy of Countrywide. *Id.* at 4477:23-4478:21, 4515:10-15.

Professor Barry Adler

85. The Trustee hired Barry Adler to opine on the meaning of the phrase "material and adverse" as used in PSA § 2.03(c). PTX 444 at 76.

86. Professor Adler is not an expert on PSAs, Tr. (Adler) 4387:3-20, and he informed the Trustee that he had limited experience in RMBS and no knowledge of relevant events or customary practice. *Id.* at 4422:2-4423:11.

87. On April 22, 2011, Mr. Kravitt e-mailed Professor Adler and Professor Marcel Kahan, whom Mr. Kravitt originally asked to write the opinion ultimately written by Professor Daines. In that e-mail, Mr. Kravitt dictated the conclusions of these supposedly independent experts: "In fact, the opinion would not have to conclude as to which party was right or wrong with regard to the legal issues at hand, but merely that if the Defendants made such arguments, there was a substantial (or perhaps, 'reasonable') chance that they would win on such arguments." R-138 at 003. This is the approach of a lawyer who wants to justify an already-reached deal, not to advocate on behalf of those his client (BNYM) is duty-bound to represent.

88. Mr. Kravitt not surprisingly got the opinions he asked for. Professor Adler gave the Trustee his "general views on the . . . language from 2.03(c)," PTX 444 at 78, but the Trustee never asked him to develop the best legal arguments to defeat BofA's interpretation of 2.03(c). Tr. (Adler) 4419:12-15.

89. The Trustee also did not inform Professor Adler that approximately 100 of the PSAs contain "material and adverse" clauses that deem certain breaches of representations and warranties to be material and adverse. *E.g.*, R-13 § 2.03(c); Tr. (Adler) 4426:22-24, 4427:9-16.

Given that the Trustee had long been bought and paid for by BofA, this omission by the Trustee is less than surprising.

Brian Lin's Servicing Opinion

90. BNYM also hired Mr. Lin (who, as explained above, failed in evaluating repurchase exposure) to evaluate the Settlement Agreement's servicing provisions. PTX 14. Yet Mr. Lin has never authored any peer-reviewed articles in the area of servicing, worked at a servicers' desk or supervised a servicing department, worked for a company that engages in the servicing of high-risk loans, or been qualified as an expert on the valuation of servicing improvements. Tr. (Lin) 3801:6-8, 3803:23-3804:13, 3805:21-3806:12, 3807:7-15.

91. Mr. Lin opined in his servicing report that the settlement's servicing provisions would be an "improvement," but he never evaluated BofA's existing servicing practices to establish a baseline. Tr. (Lin) 3820:4-12; 3828:17-22.

BNYM Did Not Investigate or Try to Put A Dollar Figure on Any of the Servicing Claims or Document Exception Claims

92. Apparently believing that it could settle claims without evaluating them, BNYM never investigated the October 18 Notice's allegations of Master Servicer misconduct. Tr. (Bailey) 2354:15-2355:6. BNYM did not value BofA's liability for past servicing failures, Tr. (Kravitt) 1831:4-14, and did not hire an expert for that purpose despite having the time and money to do so. *Id.* at 1830:2-18. The same methodology that BNYM's litigation expert used to quantify the purported "servicing improvements" could have been used to quantify losses caused by servicing failures, but BNYM never asked him to do so. Tr. (Burnaman) 2986:19-2987:25.

93. BNYM did not even try to recover damages for past servicing violations and similarly never valued liability for documentation failures. Pet. Br. at 39, 40. Yet if approved, the settlement would release all claims "arising out of or relating to . . . the servicing of the

Mortgage Loans held by the Covered Trusts. . . ." and all claims "arising out of or relating to . . . the documentation of the Mortgage Loans held by the Covered Trusts . . . ." R-1 § 9(a).

<u>The Trust Committee Served as a Rubber Stamp</u>

95. BNYM's Trustee Committee met for less than an hour to discuss the proposed $8.5 billion settlement. Tr. (Bailey) 2399:18-20. Richard Stanley, the chair of the Trust Committee, never read the proposed Settlement Agreement, the Institutional Investor Agreement, the Proposed Final Order and Judgment, or any of the Trustees' advisors' reports before voting to approve the settlement.[5] Tr. (Stanley) 3179:12-3180:13. Neither Mr. Stanley nor Kelly Crosson, another BNYM managing director, had ever attended a Trust Committee meeting at BNYM where the Trust Committee did not approve the matter put before it. Tr. (Stanley) 3177:22-3178:20; R-4152 at 41:12-17 (Crosson Dep.).

96. The Trust Committee did not discuss a number of facts important to evaluating the reasonableness of the settlement and the Trustee's process, including: BofA's refusal to produce loan files; BofA's voluntary capital infusions into Countrywide; Mr. Lin's reliance on the GSE repurchase experience as the basis for the settlement amount; the $40 billion variance between the loss estimates of the Institutional Investors and Mr. Lin; the losses, or magnitude of the losses, in the 530 trusts; the quality of the servicing in the Covered Trusts; Mayer Brown's conflict that prevented it from suing BofA; or the Trustee's absence from the negotiations when the $8.5 billion offer was made. Tr. (Stanley) 3166:4-11, 3167:25-3168:8, 3174:20-3175:3, 3176:7-10, 3177:12-18, 3175:4-12, 3186:3-11; Tr. (Bailey) 2411:7-18; 2400:3-7. In short, the

[5] With respect to Mr. Lin's servicing report, there is inconsistent testimony regarding whether the Trust Committee even had the report prior to the vote approving the settlement. The Trustee's former in-house counsel, Bob Bailey, testified that the Trust Committee made its decision on the basis of a <u>draft</u> of the report. Tr. (Bailey) 2210:3-2211:22. In contrast, Mr. Lin testified that he never delivered any drafts of this servicing report. Tr. (Lin) 3808:17-20, 3812:18-3813:9.

Trust Committee was nothing but an ill-informed rubber stamp of the settlement that BNYM's conflicted lawyers crafted to protect BNYM from any potential liability.

BNYM Tied Its Hands Through the Further Assurances Clause

97. By Mr. Kravitt's own admission, the Further Assurances clause can "be described as changing [BNYM's] duties," Tr. (Kravitt) 1535:6-11, and "ties [BNYM's] hands," preventing the Trustee from helping certificateholders maximize their recovery, even "if a fact develops that dramatically changes the assumptions that were relied upon by the Trustee." *Id.* at 1548:7-14. This is more limiting than a typical such clause. Tr. (Bailey) 2415:22-2416:11.

ARGUMENT

The Settlement Proponents now unfairly ask this Court for a judicial blessing of all the conflicted, self-interested, and unreasonable conduct that led to this back-room settlement. *See* PFOJ (Doc. No. 7). Rather than simply enter a deal and live with the consequences, the Trustee and BofA want judicial protection. The Court does not have to, and on this record should not, provide it to them. Respondents respectfully request that the Court not approve the settlement as it currently stands, and decline to enter the overreaching PFOJ findings that Petitioners request.

I. Standard of Review[6]

The PFOJ contains numerous proposed findings that squarely present the questions: (1) whether the proposed settlement is fair, reasonable, and adequate; and (2) whether the Trustee's conduct during the settlement negotiations was reasonable, in good faith, and in accord with its duties. PFOJ ¶¶ h-p. Where, as here, a proposed settlement seeks to bind parties who were unrepresented in the settlement negotiations, courts must independently determine whether the settlement is "fair, reasonable, and adequate." *See Goldsholl v. Shapiro*, 417 F. Supp. 1291, 1295-96 (S.D.N.Y. 1976) (collecting cases); *Geltzer v. Andersen Worldwide, S.C.*, No. 05 Civ.

[6] Respondents have previously briefed the standard of review. *See* Doc. Nos. 244, 588, 771, 814.

3339 (GEL), 2007 WL 273526, at *1 (S.D.N.Y. Jan. 30, 2007). The burden of making this showing rests squarely on Petitioners. *Goldsholl*, 417 F. Supp. at 1296.

BNYM likewise bears the burden of proving that it acted reasonably, complied with its fiduciary duties, and is entitled to each of the separate findings it seeks. Bogert's Trusts & Trustees § 560 ("The burden of proving that a discretionary power has been properly used is on the person who is asserting rights resulting from the use of the power, for example, on the trustee claiming the approval of an account which shows that he exercised a power in a certain manner . . . .") (citing *In re Jaeck's Will*, 42 N.Y.S.2d 514 (Sur. Ct. 1943)). Courts do not defer to a trustee whose conduct is unreasonable, is based on an improper interpretation of the terms of the trust, or is otherwise inconsistent with the trustee's fiduciary duties. *See* Restatement (Third) Trusts § 87 cmt. b & c; *see also In re Stillman*, 107 Misc. 2d 102, 110-11 (Sur. Ct. 1980).

II. This Court Should Not Approve the Trustee's Settlement Conduct "In All Respects," PFOJ ¶ (l), Nor Enter Any of the Proposed Findings Related to BNYM's Conduct, PFOJ ¶¶ (f)-(h), (i), (j), (k), or (p)

Petitioners seek an array of factual findings related to the Trustee's settlement conduct, its investigation, and its evaluation of the settlement, PFOJ ¶¶ (f)-(l) & (p), even going so far as to seek judicial approval of the Trustee's conduct "in all respects." *Id.* ¶ (l). Those findings are not merited on this record, and the Court should decline to enter them.

A. In Evaluating BNYM's Conduct, This Court Should Apply the Highest Standards of Loyalty and Care

BNYM concedes that its participation in settlement negotiations and entry into the proposed Settlement Agreement were discretionary acts that it was not required to take. Pet. Br. at 6; Tr. (Lundberg) 4597:2-19. This type of discretionary act on another's behalf is quintessentially fiduciary. *See, e.g.*, *U.S. v. Chestman*, 947 F.2d 551, 569 (2d Cir. 1991) ("A fiduciary relationship involves discretionary authority and dependency: One person depends on another—the fiduciary—to serve his interests."); *Anonymous v. CVS Corp.*, 188 Misc. 2d 616, 620 (N.Y. Sup. Ct. 2001) ("[I]t is well-settled in New York that a fiduciary duty arises, even in a commercial transaction, where one party reposed trust and confidence in another who exercises discretionary functions for the party's benefit . . . .").

Accordingly, with respect to its settlement conduct and decision-making, the Trustee should be held to the highest standards of care and loyalty. The Trustee must "administer the trust solely in the interest of the beneficiary," *In re Heller*, 6 N.Y.3d 649, 655 (2006), and is not permitted "to create or to occupy a position in which he has interests to serve other than the interest of the trust estate." *City Bank Farmers Trust Co. v. Cannon,* 291 N.Y. 125, 131 (1943); *see also Birnbaum v. Birnbaum,* 73 N.Y.2d 461, 466 (1989) (The duty of undivided and undiluted loyalty "is a sensitive and 'inflexible' rule of fidelity, barring not only blatant self-dealing, but also requiring avoidance of situations in which a fiduciary's personal interest possibly conflicts with the interest of those owed a fiduciary duty.").

The Settlement Proponents cite Judge Learned Hand's opinion in *Dabney v. Chase National Bank*, 196 F.2d 668 (2d Cir. 1952), as supposedly endorsing their incorrect view that BNYM's duty of loyalty is limited to the duty "not to profit at the possible expense of his beneficiary." Pet. Br. at 41. But BNYM did exactly that here, seeking indemnity and ultimately a release for its conduct before and during the settlement, even though this meant capitulating to a low-ball settlement that failed to adequately compensate the certificateholders. In any event, *Dabney* clarified that refraining from profiting at the beneficiary's expense is only "part of [the Trustee's] obligation to give his beneficiary his undivided loyalty, free from any conflicting personal interest[.]" 196 F.2d at 670.

B. The Court Should Not Find that BNYM Acted "in Good Faith, Within its Discretion, and Within the Bounds of Reasonableness," PFOJ ¶ (k)

Ignoring the overwhelming evidence demonstrating that the Trustee abandoned certificateholders during the negotiations and even acted to their detriment for purposes of the Trustee's self-protection, Petitioners ask this Court to find that the Trustee acted "in good faith, within its discretion, and within the bounds of reasonableness." PFOJ ¶ (k). Given the lack of evidence to support this finding—and, indeed, the evidence demonstrating its falsity—the Court should not enter it.

1. <u>BNYM Acted in Bad Faith, Outside Its Discretion, and Unreasonably When It Failed to Represent Certificateholders' Interests During the Settlement Negotiations</u>

As noted by a federal bankruptcy court, "once BNYM chose to act as the Bondholders' representative and participate in the settlement negotiations on their behalf, it was obliged to represent the interests of the Bondholders faithfully." *In re Lower Bucks Hospital*, 471 B.R. 419, 453 (E.D. Pa. 2012). Here, BNYM failed miserably to represent certificateholder interests, first and foremost by hiring a law firm that was ethically barred from zealously representing the interests of all certificateholders, that could not file suit on BNYM's behalf against BofA, and that had both hands tied behind its back during the negotiations. SOE ¶¶ 4-6, 8-10.

Further, by BNYM's own admission, it only hired counsel to represent itself, *not* the interests of certificateholders, therefore leaving any certificateholders not represented by Gibbs & Bruns without representation during the settlement negotiations. SOE ¶¶ 4-5. The Trustee's failure to represent certificateholders' interests culminated in BNYM's abdication of responsibility for negotiating the settlement amount. Even though the settlement covers 530 trusts—consisting mostly of trusts in which the Institutional Investors lacked 25% voting rights—BNYM allowed the Institutional Investors to negotiate the Settlement Amount for all the trusts. SOE ¶¶ 44, 48-50. BNYM did not even bother to evaluate whether the Institutional Investors were similarly situated to or representative of other, absent certificateholders before allowing them to drive the negotiations. Tr. (Bailey) 2342:3-6. Stipulated facts demonstrate that at least with respect to BlackRock, who has extensive ties to BofA, the Institutional Investors are not adequate representatives. *See* R-4155.

2. BNYM Acted in Bad Faith, Outside Its Discretion, and Unreasonably When It Placed its Own Interests Above Those of Certificateholders

The Trustee not only failed to represent certificateholder interests, it actively worked throughout the process to benefit itself at the expense of certificateholders. Nowhere is the Trustee's conflict more clear than in the Trustee's decision to enter the Forbearance Agreement.

The occurrence of an Event of Default was not in BNYM's "self-interest" because it would have made BNYM subject to the prudent person standard, would have obligated BNYM to decide whether to replace the Master Servicer, and would have required BNYM to give notice to all certificateholders. SOE ¶ 21. Certificateholders, however, benefit from an Event of Default in several ways. For one, BNYM's duty to act as a prudent person in the conduct of its own affairs after an Event of Default, PSA § 8.01, would be immensely valuable when the trusts are losing billions of dollars.[7] Additionally, certificateholders must receive notice of an Event of Default. R-13 § 7.03(b). Finally, any group of certificateholders—not just those who started the 60-day cure period—can demand that BNYM remedy the default, and if BNYM fails to do so, can sue the Master Servicer directly under PSA § 10.08.[8]

[7] Of course, it is Respondents' position that BNYM was subject to the prudent person standard and had fiduciary duties irrespective of whether an Event of Default occurred, because they were acting as a fiduciary with respect to this settlement. Section II.A, *supra*.

[8] Nothing in the PSAs says that only the certificateholders who triggered the 60-day cure period (under § 7.01) can pursue post-Event of Default remedies (under § 10.08). And the record is clear that, during the settlement negotiations, the Settlement Proponents believed that a group other than the Institutional Investors could act under § 10.08 if the 60-day cure period ran. SOE ¶¶ 27-29.

By purporting to prevent an Event of Default from occurring through the Forbearance Agreement, BNYM relinquished critical *certificateholder* rights in exchange for *personal* benefits, in plain violation of the duty of loyalty. *See Dabney*, 196 F.2d at 670. With the Forbearance Agreement in place, BNYM could argue that no Event of Default was triggered, that it was not subject to the prudent person standard, and that it did not have to give notice and worry about other "wildmen" disrupting the march toward a low-ball settlement. The record conclusively establishes that BNYM, BofA, and the Institutional Investors all benefitted from the Event of Default. SOE ¶¶ 21, 22, 24, 25, 31, 35. Only the absent certificateholders did not benefit from the Forbearance Agreement and, in fact, were harmed by it. SOE ¶ 23.

3. <u>BNYM Acted in Bad Faith, Outside Its Discretion, and Unreasonably When It Decided Not to Give Certificateholders Notice of the Settlement Negotiations or of the Forbearance Agreement, in Exchange for Receiving Indemnity</u>

The record is clear that in December 2010, as BNYM was negotiating the Forbearance Agreement and considering giving certificateholders notice of the negotiations, the Trustee chose not to provide notice because BofA did not want notice to go out and BofA provided the Trustee protection in the form of the December Indemnity Agreement. SOE ¶¶ 42-43. This request for an indemnity in exchange for not providing certificateholder notice demonstrates that BNYM knew it was acting in ways not prescribed by the Governing Agreements. *See Harvey v. Guaranty Trust Co.*, 134 Misc. 417, 426 (N.Y. Sup. Ct. 1929) ("The trustee appears to have been cognizant of the fact that it was doing something irregular . . . . This recognition by the trustee of the doubtful propriety of its conduct is indicated by its exaction of the indemnity agreement . . . ."). There is no authority in the PSAs for BNYM to change the 60-day cure period through a Forbearance Agreement. SOE ¶ 26. Similarly, there is no express authority in the PSAs allowing the Trustee to compromise breach of representation and warranty claims for less than the contractually-defined "Purchase Price." *See* R-13 § 2.03(c). Nothing in the provision BNYM relies upon for its authority, § 2.01(b), expressly provides the power to settle repurchase claims for less than the contractual remedy.[9] Loretta Lundberg, BNYM's primary business person involved in the settlement process, conceded as much. Tr. (Lundberg) 4596:16-19. BNYM's decision not to provide notice to certificateholders of the extra-contractual conduct it was undertaking, in exchange for an indemnity protecting itself, violated the duty of loyalty.

4. BNYM Acted in Bad Faith, Outside Its Discretion, and Unreasonably When It Agreed to the Further Assurances Clause

Through the "Further Assurances" clause of the proposed Settlement Agreement, BNYM agreed to put BofA's interests in front of certificateholders' interests, in blatant violation of its duty of loyalty. This clause, which requires BNYM to support the proposed Settlement Agreement regardless of new information that may come to light, changes the Trustee's duties, ties the Trustee's hands, and prevents the Trustee from helping certificateholders maximize their recovery. SOE ¶ 97. For example, if BNYM becomes aware of facts that would undermine BofA's successor liability defense (such as that BofA has provided capital infusions to Countrywide) or that recent court decisions undermine BofA's successor liability or "material and adverse" defenses, BNYM would not be permitted to bring them to this Court's attention. Tr. (Kravitt) 2180:20-2181:22. The Further Assurances clause unreasonably binds BNYM to support BofA, rather than the certificateholders to whom it owes a duty of loyalty.

In sum, the Trustee's failure to represent certificateholder interests, its decision to purportedly avoid an Event of Default for its own benefit, its decision to forego notice to certificateholders in exchange for an indemnity, and its entry into the Further Assurances clause preclude entry of the requested finding in PFOJ ¶ (k).

[9] Accordingly, entry of PFOJ ¶ (f) is not appropriate.

C. The Court Should Not Find that BNYM Conducted a Meaningful Factual or Legal Investigation or Appropriately Evaluated the Terms, Benefits, and Consequences of the Settlement or the Strengths and Weaknesses of the Claims Being Settled, PFOJ ¶¶ (h)-(j)

As the record proves, the settlement rests on unverified assumptions, inapposite data, and abandoned leverage. Remarkably, Petitioners nonetheless ask this Court to find the settlement is the "result of" a factual and legal investigation by the Trustee (PFOJ ¶ h) and that the Trustee "appropriately evaluated" the claims being settled, the alternatives to settlement, and the settlement terms (PFOJ ¶¶ i-j). The Court should not enter any of these findings.

1. <u>BNYM Acted Unreasonably In Accepting the GSE Repurchase Experience as a Substitute for Loan File Review in the Covered Trusts</u>

The Trustee was unreasonable in adopting and relying on the GSE repurchase experience as a proxy for the repurchase exposure in the Covered Trusts without, at a minimum, insisting upon full disclosure and confirmatory discovery. The record makes plain that GSE loans are materially different from private-label loans, such as those in the Covered Trusts, and that those differences affect the relative repurchase exposure in the Covered Trusts. SOE ¶¶ 63-66. And none of the "adjustments" BofA made to the GSE repurchase experience were adequate to fully account for the differences between GSE and private-label pools. *Id.* As Freddie Mac's former General Counsel testified, using the GSE repurchase experience as a proxy for the repurchase exposure in the Covered Trusts is like "apples and oranges," "irrelevant," and "not even worthy of discussion." *Id.* ¶ 63.

BNYM has no reasonable excuse for relying on an inapposite proxy rather than obtaining the loan files to which it is contractually entitled, particularly when both BNYM's counsel and the Institutional Investors recognized the leverage a loan file review would create. SOE ¶¶ 57-58. BNYM could have investigated the loan files without cost to itself under the December Indemnity Agreement and under various PSA sections. *See* R-13 §§ 2.03(c), 3.07, 8.05; SOE ¶ 58. And loan file review is not the uncertain exercise the Petitioners claim. Rather, it is a generally accepted methodology used in almost every aspect of RMBS purchasing, due diligence, and litigation. Tr. (Burnaman) 2890:7-2891:15, 2977:8-12; Tr. (Cowan) 4103:3-23; *MBIA Ins. Corp. v. Countrywide Home Loans Inc.*, 30 Misc. 3d 1201(A), 2010 WL 5186702 (Sup. Ct. N.Y. Cnty. 2010).[10] BNYM could also have easily used available tools, including BofA's own databases, to target those loans that have the highest probability of containing defects. SOE ¶ 72.

In sum, the GSE proxy cannot reasonably form the basis of the settlement. Far from being transparent, it was a selectively adjusted proxy, controlled entirely by the liable party, and based on materially different loans than the ones in the Covered Trusts.

2. <u>BNYM's Only Investigation of the Settlement Amount Was the Work Performed by Mr. Lin, Who Unreasonably Adopted BofA's Unverified Numbers, Rejected in Whole the Institutional Investors' More Favorable Analysis, and Otherwise Artificially Deflated the Settlement Range</u>

Having chosen not to look at the primary evidence of the liability, BNYM's "investigation" and "evaluation" of the representation and warranty claims consisted of hiring Mr. Lin to evaluate the presentations made by BofA and the Institutional Investors, and from those derive a purportedly "reasonable" settlement range. In the end, Mr. Lin constructed an inapposite methodology, populated it with unverified data, and skewed the result by failing to account for all available data. The result was to severely undervalue the Covered Trusts' claims and to derive an unreasonably low settlement range.

Mr. Lin's approach consisted of three steps: (1) estimate aggregate lifetime losses to the Trusts, (2) multiply the losses by an assumed breach rate, and (3) multiply the product of that

[10] Also, in the recent ResCap bankruptcy proceedings, Judge Glenn approved the use of a loan file sampling. *See In re Residential Capital LLC*, No. 12-12020, Doc. No. 4102 at 44-45 (Bankr. S.D.N.Y. June 27, 2013) (Memo. Opinion Approving the Plan Support Agreement).

calculation by an assumed success rate. Each step was deeply flawed.

First, Mr. Lin estimated losses using a method that is designed to measure losses from borrower non-payment. *See* Tr. (Lin) 3953:17-21. But payment default is the wrong metric for determining repurchase liability. Under the PSAs, the Covered Trusts are entitled to a contractually-defined "Purchase Price" for breaches that cause *any* "material and adverse" effect to the interests of certificateholders, even if default has not occurred. R-13 § 2.03(c). Default is not the only material and adverse effect caused by breaches. Tr. (Cowan) 4237:24-4243:26; Tr. (Burnaman) 2806:22-2809:26. Therefore, Mr. Lin's methodology fails to capture all actionable harms. But even if default were the only form of material and adverse effect, Mr. Lin still understated the variables in the loss calculation. *See* Tr. (Burnaman) 2736:18-2737:4 (calculating losses at $84.7 billion); PTX 604 (calculating losses at more than $100 billion); Tr. (Cowan) 4234:5-26, 4185:26-4198:24. As a result, Mr. Lin began the next calculations with understated losses, necessarily producing an understated settlement amount.

Second, Mr. Lin multiplied his loss estimate by an assumed breach rate. Mr. Lin had two breach rate estimates to choose from: 36% from BofA, and 50%-65% from the Institutional Investors.[11] Although BofA's breach and success rates could not be confirmed for "[l]ack of historical data" (PTX 444 at 106) and the Institutional Investors' estimates came from a "forensic underwriting project of … approximately 250,000 loans of similar product types, and the same origination period as the [Covered Trusts]" (*id.* at 105), Mr. Lin simply accepted BofA's 36% breach rate and ignored the much higher estimates. SOE ¶¶ 61, 76.

Finally, Mr. Lin multiplied the product of the preceding calculation by a success rate, which "represents the percentage of loans submitted to BofA which would actually be

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[11] He would have been presented with a third, 91% (based on actual Countrywide loan files), had BNYM and BofA not insisted on excluding Quinn Emanuel from the negotiations.

repurchased." PTX 444 at 104. There were competing success rates provided by BofA and the Institutional Investors, and again Mr. Lin adopted BofA's 40% GSE-based success rate and ignored the Institutional Investors' 50%-75% success rates.[12]

Because Mr. Lin included *only* BofA's breach and success assumptions in both of his high and low estimates, his settlement range of $8.8 billion to $11 billion was artificially low and did not account for the Institutional Investors' analysis, which showed repurchase exposure ranging from $32.3 to $52.6 billion. Had Mr. Lin used all of the materials available to him, the high end of his "reasonable settlement range" would have been around $50 billion. Tr. (Cowan) 4185:26-4208:17. The problems with Mr. Lin's analysis were apparent from his report, but unquestioned by the Trustee. SOE ¶¶ 75-76.

3. <u>BNYM Used the Advisors It Hired to Actually Weaken Its Own Negotiating Position and Undermine the Strength of the Settled Claims, Not to Further a Good Faith Legal and Factual Investigation</u>

BNYM's purported reliance on its pre-settlement advisors to demonstrate a legal and factual investigation and justify its entry into the proposed Settlement Agreement is both misplaced and a deception. BNYM did not use the advisors to investigate critical facts, and largely limited the scope of their work. SOE ¶¶ 77-91. Rather than attempting to maximize the Trusts' recovery—as BNYM's own trust law expert opined it must—BNYM used its advisors to construct and support BofA's defenses.[13] *Id.*

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[12] The use of the success rate at all is another defect in Mr. Lin's design model. The success rate represents the "material and adverse effect" requirement and anything else required for a *successful* repurchase demand. Tr. (Smith) 623:23-25; 624:7-9. By first conditioning any recovery on default and then discounting for material and adverse effect, Mr. Lin gave BofA a double discount. BNYM then gave yet a third discount when it relied on Professor Adler's report to justify a settlement amount that is lower than the lowest boundary of Mr. Lin's range. *See* R-2 at 23-26.

[13] BNYM hired Yale law professor John Langbein as a litigation expert for this case. At his deposition, Professor Langbein testified that BNYM was a fiduciary with respect to all of its settlement conduct, and that its duties included maximizing recoveries for certificateholders. *See* Tr. (Kravitt) 1537:5-1538:6.

Nowhere is this more apparent than in connection with what BNYM says was its most critical settlement consideration—collectability from BofA.[14] Professor Daines advised BNYM that the Trustee might reach BofA assets if it could show that BofA underpaid for Countrywide's assets.[15] PTX 444 at 22-23. Tellingly, however, when BNYM then hired Capstone to "opine on the maximum economic value that BNYM could recover from [Countrywide] . . . ," PTX 444 at 5, BNYM assumed away the possibility that BofA underpaid for Countrywide's assets by giving Capstone three key limiting assumptions: (1) there was no basis on which a court could pierce the corporate veil between Countrywide and BofA, (2) the BofA merger left Countywide *solvent*, and (3) BofA paid *reasonably equivalent value* for Countrywide's assets. *Id.* at 7. In other words, BNYM assumed away even the few facts that could give rise to successor liability under Professor Daines's incorrect and overly narrow view of the doctrine.

BNYM did something similar with its causation expert, Professor Adler, who opined on the meaning of "materially and adversely affects" as applied to a breach of a representation and warranty in section 2.03(c) of the PSAs. Here, BNYM told Professor Adler that he needed only to opine on whether BofA's causation argument was "reasonable." SOE ¶ 87. As Professor Coates explained, BNYM acted improperly by doing so because it "just invites going to the least possible price that you could get away with." Tr. (Coates) 4852:18-4853:20. And on top of it all, BNYM never informed Professor Adler that more than 100 of the PSAs have a provision that

[14] Contrary to BNYM's stated litigation position, Loretta Lundberg testified that the possibility of a Countrywide bankruptcy was "not the concern" for BNYM in approving the settlement. Tr. (Lundberg) 4624:9-15. Perhaps this was because all of BofA's actions and public statements at the time indicated that, far from putting Countrywide into bankruptcy, BofA intended to stand behind its repurchase obligations and maintain its capitalization. *See* SOE ¶¶ 53-54.

[15] Professor Daines was wrong when he opined that fair value is required for successor liability to attach under New York law. Tr. (Coates) 4875:7-4876:24; *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 40 Misc. 3d 643, 674 (Sup. Ct. N.Y. Cnty. 2013).

deems certain breaches to materially and adversely affect the interests of certificateholders. SOE ¶ 89. This is a far cry from attempting to maximize recoveries.

Finally, BNYM hired Mr. Lin to perform essentially meaningless evaluations of the claimed servicing improvements and the repurchase exposure presentations. The flaws with Mr. Lin's repurchase exposure analysis are detailed above. Section II.C.2, *supra*. BNYM's hiring of Mr. Lin to evaluate the proposed settlement's servicing provisions was unreasonable given his lack of applicable background and experience. SOE ¶ 90. Moreover, Mr. Lin's opinion that the servicing provisions represent "improvements" was nearly worthless, given his failure to evaluate BofA's existing servicing practices.[16] SOE ¶ 91.

BNYM wants this Court to focus on the mere fact that it hired advisors at some point in the process, rather than the substance of what the advisors did and when they did it. Indeed, it was the Respondents, and not BNYM, who called the advisors to testify at trial. Their testimony, as well as the testimony of BNYM witnesses, makes clear why BNYM does not want to focus on the actual substance of the advisors' work—doing so demonstrates BNYM's guiding hand in pushing the advisors to reach conclusions BNYM and BofA desired.

4. <u>BNYM's Trust Committee Did Not Appropriately Evaluate BNYM's Conduct or the Terms of the Settlement Before Voting to Approve It</u>

BNYM's own expert agrees that the Trust Committee is an important part of the process and should not simply be a "rubber stamp." Tr. (Landau) 2661:6-2662:15. Mr. Landau assumed in rendering his opinion that the Trust Committee had all the relevant information it needed to evaluate the settlement, and that the members reviewed the information. Tr. (Landau) 2664:20-2665:2. This was clearly not the case, as the Trust Committee was never told critical facts about

[16] There is good reason why BNYM would not have directed Mr. Lin to compare the improvements to BofA's existing servicing—that investigation could have established the Event of Default that BNYM had worked so hard to avoid.

the settlement, and not even the committee Chair ever read the advisor reports the Trustee purports to have relied upon. SOE ¶¶ 95, 96. Rather than the Trust Committee serving as a meaningful evaluation of or "check" on the settlement, it was a 45-minute ill-informed rubber-stamp of what the attorneys recommended, consistent with BNYM's usual practice. *Id.*

In short, nothing in the record supports findings that the settlement is the "result of" a legal and factual investigation by the Trustee, or that the Trustee "appropriately evaluated" the strengths and weaknesses of the claims. The Court should not enter PFOJ ¶¶ (h)-(j).

D. This Court Should Not Enter the Proposed Release of BNYM Requested in PFOJ ¶¶ (p) & (q)

BNYM asks this Court to order that all certificateholders are "permanently barred and enjoined" from asserting any claims against BNYM arising from any of BNYM's settlement-related conduct. PFOJ ¶¶ (p) & (q). The release that BNYM effectively seeks is not justified given the record, for all of the same reasons that the other findings BNYM seeks with respect to its settlement conduct should be denied. *See* Sections II.A-II.C, *supra.*[17]

III. The Court Should Not Approve the Proposed Settlement and Settlement Agreement "In All Respects," PFOJ ¶¶ (m)-(o)

In addition to the array of findings Petitioners seek blessing the Trustee's conduct, they also request that the Court approve the settlement "in all respects," PFOJ ¶¶ (m)-(n), order the settlement consummated, PFOJ ¶ (m), and enter a comprehensive release for BofA/Countrywide from all claims arising out of or relating to: "(i) the origination, sale, or delivery of Mortgage Loans to the Covered Trusts . . . , (ii) the documentation of the Mortgage Loans held by the

[17] Petitioners' argument that the requested release simply makes explicit "the *res judicata* effect" of the Court entering certain findings violates the well-recognized principle that a court cannot predetermine the res judicata effect of its own judgment, which can only be tested in a subsequent action. *See, e.g., Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 805 (1985). And Petitioners' reliance on bankruptcy and class action settlements to support the proposed release falls short, as many of the procedural due process protections in class action and bankruptcy settlements, such as opt-out rights, are absent here.

Covered Trusts . . . , and (iii) the servicing of the Mortgage Loans held by the Covered Trusts . . . (collectively, all such claims being defined as the 'Trust Released Claims')." PFOJ ¶¶ (n)-(o). For the reasons detailed below, the Court should not enter these proposed findings.

A. BNYM Has Not Proven the Settlement Provides Adequate Compensation for the Claims that Would Be Released

BNYM has failed to meet its burden of establishing that the proposed settlement fairly compensates certificateholders in exchange for the valuable claims that are being relinquished.

Breach of Representation and Warranty Claims. As discussed above, the $8.5 billion Settlement Amount is not based on any investigation of the loan files or breach rates in these Covered Trusts. Section II.C, *supra*. Rather, as BNYM's own expert admits, "the entire analysis around the settlement of this case, is based on a series of assumptions." Tr. (Burnaman) 2879:5-7. At a minimum, the Court should order testing of the assumptions adopted by Mr. Lin and BNYM through loan sampling before approving the Settlement Amount.[18]

Servicing Provisions. It is undisputed that BNYM did not attempt to value the damages that had been caused by past servicing failures. SOE ¶¶ 92, 93. BNYM attempts to justify this omission by pointing to the settlement's purported servicing "improvements" as adequate consideration for releasing all servicing-related claims. But those provisions add little value, as the PSAs *already* require that BofA service the loans prudently. R-13 § 3.01. To the extent the servicing provisions of the settlement simply bring BofA up to industry standards, the Covered Trusts are receiving no more than what they were already contractually entitled to receive.

Documentation Cures. The Trustee never even valued the document-related liability. SOE ¶ 93. Further, as discussed below, the settlement's documentation cure provisions

[18] BNYM's experts, Messrs. Lin and Burnaman, agreed that the GSE proxy could have been tested with a loan file review, but was not. Tr. (Burnaman) 3067:4-14; Tr. (Lin) 3968:8-21.

eliminate some of the few protections the Trusts have and alter the PSAs in three primary ways: (1) narrowing the loans and defects subject to the cure provision, (2) requiring a confluence of multiple document exceptions before triggering a cure, and (3) imposing new causation requirements. Section III.B, *infra*.

In short, the Trustee has not shown that the Settlement Amount is fair, reasonable, and adequate compensation for the Trust Released Claims.

B. The Court Cannot Approve a Settlement that Amends the Governing Agreements Without Following the Contractual Requirements to Do So

This Court cannot rewrite the governing agreements. *See Fiore v. Fiore*, 46 N.Y.2d 971, 973 (1979) (contract); *see also In re Gilbert*, 350 N.Y.2d 663, 667 (1976) (trust instrument). It follows that the Court should not approve a settlement that has the same effect. Here, PSA § 10.01 specifically states that amendments which "(v) modify, alter, amend, add to or rescind any of the terms or provisions contained in [the PSA]," must be accompanied by an Opinion of Counsel that confirms the amendment does not "adversely affect in any material respect the interests of any Certificateholder[.]" R-13 § 10.01. In the absence of an Opinion of Counsel, an amendment may be effectuated "for the purpose of adding any provisions to or changing in any manner or eliminating any of the provisions of [the PSA] or of modifying in any manner the rights of the Holders of Certificates," only with the consent of a Majority in Interest of each Class of Certificates affected by such amendment. *Id.* at ¶ 2.

BNYM altered or seeks to alter the PSAs in multiple ways, as detailed below, but has never complied with the requirements of § 10.01.

<u>Forbearance Agreement</u>. By entering into the Forbearance Agreement, BNYM purportedly altered the contractually-mandated 60-day cure period set forth in § 7.01(ii).

Loan Modifications. The Settlement Agreement expressly provides loan modifications to occur without repurchase from the Covered Trusts, R-1 § 5(e), in contradiction to PSA provisions requiring that the Master Servicer repurchase modified loans. *See, e.g.*, R-13 § 3.11(b). Furthermore, under the Settlement Agreement (but not the PSAs) BofA is allowed to pass certain modification-related costs and liabilities on to the Covered Trusts. R-1 § 5(i).

Documentation Cures. The Settlement Agreement's documentation provisions alter the PSAs in several ways:

- Under PSA § 2.02, all loans in the trusts are subject to the remedies of cure, replacement or repurchase; under § 6 of the Settlement Agreement, all MERS-registered loans are excluded from the cure remedy.[19]

- Under PSA § 2.02, all document deficiencies must be remedied; under § 6(b) of the Settlement Agreement, only one of either the "Mortgage Exceptions" or the "Title Policy Exceptions" is subject to remedy.

- Under PSA § 2.02, the cure is required without regard to whether the document deficiency caused a specific harm; under § 6(c) of the Settlement Agreement, BofA will reimburse the Covered Trusts only where foreclosure is made impossible due to a "Mortgage Exception" and the trust is not reimbursed due to a "Title Policy Exception."

Waterfall Distribution. Jason Buechele, Managing Director of Structured Finance Analytics at BNYM, admitted in deposition that the Settlement Agreement alters—in at least one way—the PSA's distribution priorities. Buechele Dep. 86:3-87:10.[20]

Allocation Methodology. Under the PSA, each trust is entitled to the "Purchase Price" for every loan subject to repurchase. R-13 § 2.03(c). Thus, the amount each trust would receive

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[19] The Mortgage Electronic Registry System ("MERS") was created by the mortgage finance industry to bypass traditional recordation requirements. In the wake of the housing crisis, a number of courts have found that MERS registration is inadequate to create a security interest in the collateral such that foreclosure to protect Trust assets is impossible. The number of MERS loans in RMBS is substantial. By excluding MERS loans from the document cure—an exclusion that alters section 2.02 of the PSAs—BNYM alters BofA's obligations to the Trusts' detriment.

[20] Respondents intend to offer into evidence designations from Mr. Buechele's deposition when trial resumes in November. *See* CPLR § 3117(a)(2).

on repurchase claims contractually turns on the number of loans with material and adverse breaches. BNYM's allocation methodology, in contrast, does not allocate the Settlement Payment among the Covered Trusts according to the harm caused by breaches or the relative amount of breaches but, rather, according to the losses each trust expects to take *regardless of the cause of the losses.* Therefore, BNYM is effectively altering the contractual remedy for repurchase claims.

There is no legal basis upon which the Court can approve a settlement that amends the PSAs without the contractually-defined amendment requirements of § 10.01 having been followed. This is particularly true where, as here, the provisions being amended all involve altering the remedies that the parties—including certificateholders—bargained for.

C. There Has Been No Evidence Presented or Explanation of Opaque Terms

After nearly eight weeks of trial, Petitioners have failed to present any evidence on, or fully explain, material terms of the proposed settlement:

- Exclusion of Covered Trusts. Section 3(d)(iv) of the Settlement Agreement affords Bank of America complete discretion to exclude any Covered Trust in its entirety where just one bond is insured by a financial guaranty company, unless the insurer agrees not to pursue its rights against BofA. Further, under § 4(b), BofA appears to have a right to exclude trusts on some other unspecified basis. Petitioners have presented no evidence regarding how many trusts—or which ones—may become Excluded Covered Trusts under these provisions.

- Portion of Settlement Amount to be Retained by BofA. The Allocable Share of any Excluded Covered Trust will be retained by BofA. R-1 § 4(a). Neither the Court nor Respondents know what portion of the $8.5 billion will be so retained, though Mr. Kravitt testified on the stand it could be as high as $1 billion. Tr. (Kravitt) 1821:24-1822:9.

- "Confidential" Percentage. If a certain percentage of the unpaid principal balance of the Covered Trusts becomes Excluded Covered Trusts, BofA can walk away from the settlement (even following Court approval). R-1 § 4(b). Petitioners have not disclosed that confidential percentage.

- Allocation of Proceeds Among the Trusts. The Trustee chose not to even model a projected allocation of the Settlement Amount among the Covered Trusts until after judicial approval is obtained. Indeed, the Trustee instructed its advisor to stop working on the project because things were not moving along as fast as expected. Tr. (Sabry) 4355:2-25. Consequently, neither the certificateholders nor this Court knows even an estimate of how much each individual trust will receive.

- Magnitude of MERS Exclusion. Petitioners have not presented any evidence regarding the magnitude of the MERS exclusion from the settlement's document cure provisions. Any claims arising from document exceptions on MERS-registered loans are nonetheless released by the settlement.

The Court should not approve a settlement where such basic information remains unknown.

IV. The Court Should Not Enter PFOJ ¶¶ (c)-(d), or (s)

The Court should not approve BNYM's decision to give notice only after the proposed Settlement Agreement was signed. PFOJ ¶¶ (c)-(d). The "best notice practicable under the circumstances" would have been to give certificateholders notice of the settlement negotiations while they were taking place, when they could have had a voice in the process. Instead, BNYM deliberately waited to provide notice until after it signed the proposed Settlement Agreement and tied its own hands through the Further Assurances clause.

Finally, BNYM has made no showing that the Settlement Proponents should be released for actions "arising out of the determination, administration, or distribution . . . of the Allocable Shares." PFOJ ¶ (s). This finding, which incredibly seeks to release the Settlement Proponents of any liability for their *future* conduct, is yet another attempt by BNYM to achieve through this Court an overly broad release to which it is not entitled.

CONCLUSION

The Court should reject both the settlement and the Proposed Final Order and Judgment.

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